Economic Update

GDP Review – Q1 2017

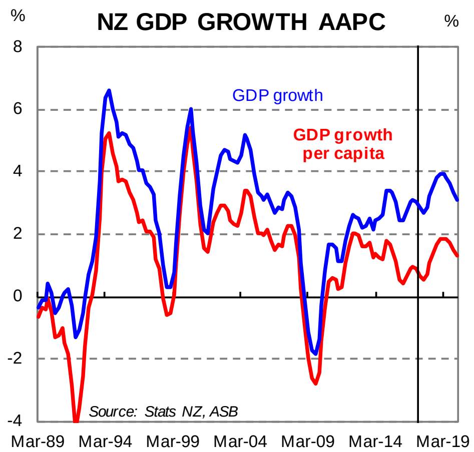
15 June 2017

Sub-trend growth reinforces RBNZ lack of urgency to hike rates

- Q1 GDP grew 0.5%, weaker than market and RBNZ expectations, but in line with ASB's forecasts.
- Two quarters of sub-trend growth is a concern but we remain upbeat about the medium-term growth outlook.
- GDP reinforces there is no hurry to lift the OCR: no hikes expected until late 2018.

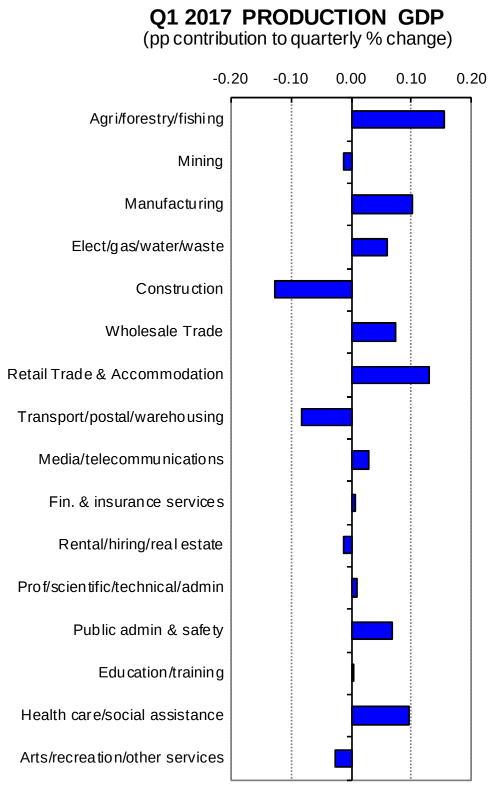
Q1 GDP lifted in line with our own expectation of 0.5%, but below market expectations and the RBNZ's May MPS forecast (see table below). Lacklustre Q1 growth follows weak growth of just 0.4% in Q4, marking two quarters of sub-trend growth. However, **we remain confident in the medium-term growth outlook, which will be supported by high Terms of Trade, low interest rates and population growth.**

We continue to expect the RBNZ to leave the OCR on hold at 1.75% until late-2018. Next week the RBNZ is likely to retain May's cautious stance that OCR hikes are a considerable time off.



GDP - March 2017	Previous	Actual	ASB	RBNZ	Market
quarterly % growth	0.4	**0.5**	0.5	0.9	0.7
annual % growth	2.7	**2.5**	2.5	2.9	2.7
annual average % growth	3.1	**3.0**	3.0		

Q1 GDP growth was sub-trend for the second consecutive quarter, and below the RBNZ's May MPS forecast. As expected, a **rebound in dairy production** and lifts in retail trade and manufacturing activity were the key drivers of Q1 growth. Health care and public administration services also lifted by more than we expected. Meanwhile, a fall in construction activity and an unexpected (and surprisingly sharp) fall in transport activity weighed on growth over Q1.



StatsNZ noted that **all components of transport activity fell**, excluding road transport. It appears a fall in rail transport was a key factor (likely reflecting the severe transport disruption taking place in the top of the South Island). While it appears road provided some offset, weakness in all other areas (i.e. postal and warehousing) gives some pause for thought of the underlying momentum in this sector.

Nonetheless, **we remain upbeat about the medium-term outlook for growth**. NZ's growth will remain supported by strong Terms of Trade, low interest rates and strong population growth. **We expect construction activity to recover** (and we are hoping to see a stronger lift in building consents in coming months to confirm this). The **stunning lift in plant and machinery investment is a very encouraging** sign that businesses are seeing increased activity and willing to invest in greater capacity. **Household consumer spending lifted strongly** and consumer confidence remains resilient, supported by a strong labour market and low interest rates. We also expect the **recovery in dairy prices to support consumer and investment spending** over the coming years.

Nonetheless, **weaker growth outcomes should not be dismissed outright**. Growth **contributions from tourism and construction are likely to be smaller** over the next few years, compared to the previous years. If **the rest of the economy is not firing on all cylinders** when growth slows in those sectors, then growth will struggle to lift above its trend rate. Fortunately, **time is on the RBNZ's side**. With no urgency to hike (or cut) the RBNZ can hold the OCR at current levels for the next year or so while it waits for growth to pick up with greater momentum than we are seeing currently.

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