

Economic Note

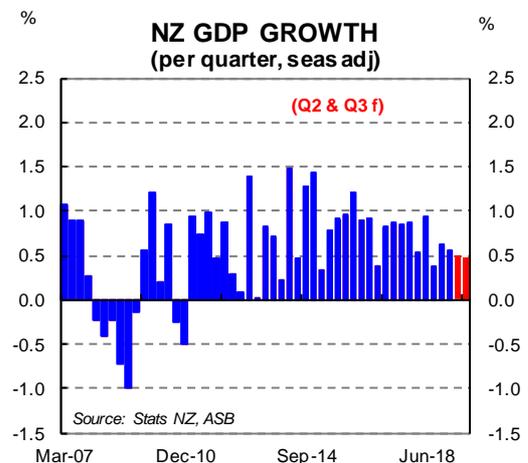
Q2 2019 GDP Preview

13 September 2019

Services sector may support Q2 growth

- We expect Q2 2019 GDP increased by 0.5% qoq, with annual growth slowing to just 2.1%.
- The RBNZ also expects muted Q2 GDP growth, with the 50 basis point OCR cut in August partly prompted by growing evidence of continued weak economic growth.
- The growth performance over the next year hinges on consumer confidence and the ongoing strength in the labour market.

GDP - Jun 2019	Previous	ASB	RBNZ
quarterly % growth	0.6	0.5	0.5
annual % growth	2.5	2.1	2.0
annual average % growth	2.7	2.5	



Summary & implications

Statistics NZ will release its estimate of Q2 GDP on Thursday 19th June at 10.45am. **We expect Q2 GDP lifted by 0.5% qoq (production basis) which should see annual growth slow to 2.1%** from 2.5%. NZ economic growth remained sub-trend over H1 2019

and ongoing weakness in business confidence suggests growth is likely to remain weak over H2 2019 as well. **The Reserve Bank of New Zealand (RBNZ) also expects quarterly growth of 0.5%, with annual growth slowing to 2%.** At the August Monetary Policy Statement, the RBNZ cut the OCR relatively aggressively (by 50 basis points). The move was in reaction to a range of economic indicators which highlighted weakening economic growth and growing downside risks to the outlook. The August OCR decision had a fair degree of ‘bad’ economic news already baked into the underlying economic forecasts, so **it would take a material surprise on GDP to prompt the RBNZ to cut the Official Cash Rate (OCR) again at the September meeting. But we continue to expect another 25bp OCR cut, possibly at the November Monetary Policy Statement.**

Sub-trend growth well signalled by leading indicators

We expect quarterly GDP growth of 0.5% in Q2, which follows a year of muted quarterly growth outcomes. Another weak quarter of growth has been well foreshadowed by leading economic indicators, which point to an underlying trend (i.e. smoothing through some of the inherent quarterly volatility in NZ GDP data) of around 0.3-0.4% qoq. **This suggests to some downside risk to our component-based formal forecast of 0.5% qoq.** NZ GDP growth has slowed below its full potential pace and requires policy support to prevent growth slowing further and limit the risk that a recession forms. The RBNZ has already stepped up, and delivered 75 basis points of OCR cuts in response to weaker

growth, but the risks remain skewed for further action.

Services sector still solid

In Q2, we expect to weak activity in primary and goods production, but for the services sector to record reasonable rates of growth.

Construction activity in Q1 fell, according to the Building Work Put in Place survey. But the drop followed strong growth in the previous two quarters and a strong pipeline of building consents indicating further activity growth going forward.

Manufacturing activity was likely weighed down by a fall in meat processing. The Economic Survey of Manufacturing suggests growth in ex-primary manufacturing production may have held up better than some other leading indicators suggest.

The Retail Trade Survey was weak, with volumes up just 0.2%qoq, suggesting NZ household spending remained muted with cautious consumers keeping a tight grip on wallets. In addition, a **fall in overseas visitor arrivals likely weighed on activity for the hospitality sector and accommodation providers.**

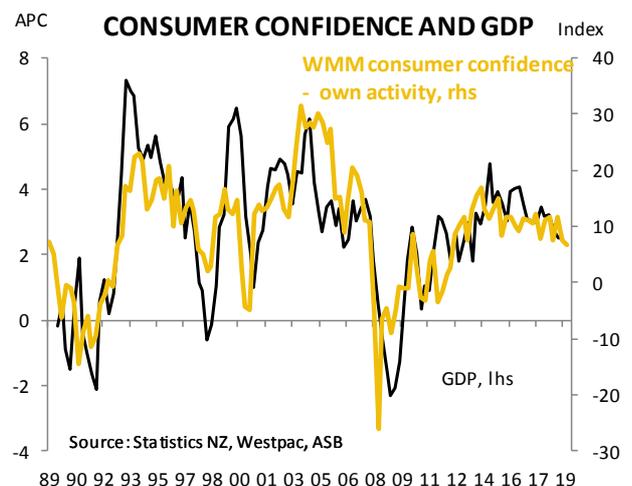
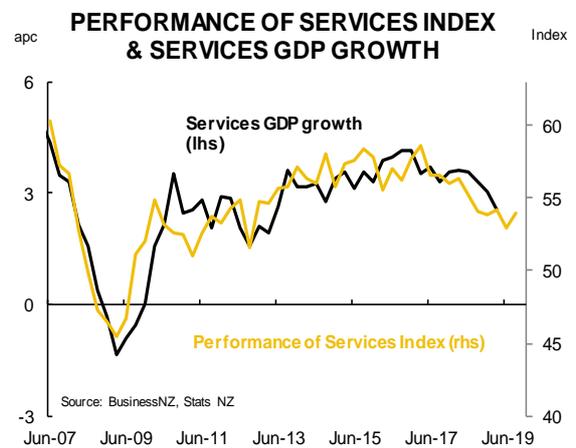
In contrast, **growth in the services sector was likely robust over Q2**, as indicated by strong labour demand and pockets of strength in in the Selected Services Survey. We expect strong growth in Arts and Recreation services along with reasonably firm growth in business support services (professional, scientific, technical, admin and support).

Growth outlook hinges on consumer confidence

Going forward, the outlook for the economy rests on the resilience of the labour market and NZ households' willingness/ability to spend on goods and services. Business confidence has fallen over the past year, with weaker activity, rising costs and squeezed profit margins creating a challenging environment. Businesses have responded by holding back on investment plans over the past year which has weighed directly on growth. The [ASB Recession Probability Model](#) points to a 30% chance of a recession starting in Q2 2019. Fortunately, **despite weak business confidence, hiring has continued and the labour market has remained strong. This source of strength has likely kept the economy away from recession for now and we will be watching measures of consumer confidence and labour market data very closely from here.**

RBNZ expecting weak growth

We expect the RBNZ to cut the OCR at least once more this year, most likely in November. The aggressive 50bp OCR cut in August pre-empted a certain amount of 'bad' economic news, including muted GDP growth over Q2. **The RBNZ expects annual growth to fall to 2%, so it will likely require a material downside surprise to prompt the RBNZ to cut the OCR another 25bp as soon as the September OCR review.** Rather, we think the RBNZ will likely take some additional time to assess the impact of the recent rate cuts on business and consumer confidence – in particular – and the economic outlook in general.



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