Economic Note

Q3 2020 GDP Preview

11 December 2020

Epic recovery

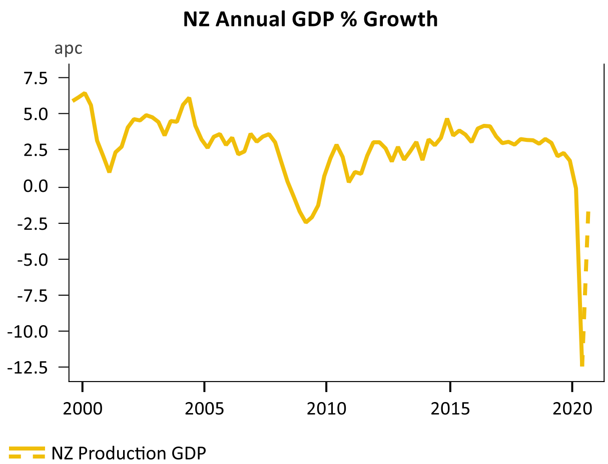
- We expect StatsNZ's first estimate of Q3 GDP to show a 13% qoq lift, a solid bounce back from the 12.2% decline in Q2.
- The NZ economy appears to be recovering from recession faster than expected.
- The key question is how much momentum can be sustained over 2021.

Summary & implications

We expect Q3 GDP rebounded 13% qoq over Q3, following the previous quarter's 12.2% decline, close to the RBNZ pick. This will still leave NZ GDP 2.2% below pre-COVID-19 levels (i.e. Dec-19 quarter GDP). The Q3 release will include the annual benchmarking revisions which could change the historical level and profile of recent GDP outturns.

The NZ economy looks to have been more resilient and has recovered from lockdown much faster than expected earlier this year. The key question going forward is whether momentum can be sustained? We expect growth will be modest over 2021, given a number of headwinds, including the international border restrictions and higher unemployment. But there are also a number of tail winds, including a strong (goods) export sector, low interest rates and strong housing demand. The outlook is still highly uncertain, and we will be keeping close tabs on incoming data and events. At present we believe the economy has enough going for it and sufficient policy support in place such that no further OCR cuts are needed.

GDP - Sep 2020	Previous	ASB	RBNZ
quarterly % growth	-12.2	13.0	13.4
annual % growth	-12.4	-1.7	-1.3
annual average % growth	-2.1	-3.1	



Source: Macrobond, ASB

Record rise to follow record decline

StatsNZ will release its first estimate of Q3 GDP on Thursday 17th of December at 10.45 am. **We expect Q3 GDP lifted 13% qoq (-1.7% yoy)**, following on from the previous quarter's 12.2% qoq contraction. Our forecast is very close to the RBNZ's November Monetary Policy Statement forecast of +13.4% qoq (-1.3% yoy).

Over the first half of 2020 GDP declined 13.4% and NZ fell into recession largely as a result of the COVID-19 pandemic and subsequent strict Alert Level 4 lockdown which was implemented in late March. High frequency indicators show that economic activity quickly bounced back as the Alert Level restrictions were gradually eased over May and June. By July it was largely business as usual, although the August resurgence in COVID-19 in NZ saw a reinstatement of higher Alert

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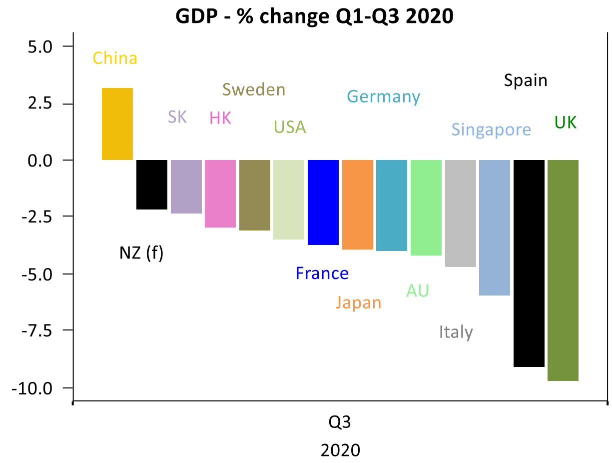
Levels (Level 3 for Auckland and Level 2 elsewhere) for a period and likely dampened the pace of recovery in Q3.

The strength of the Q3 bounce back in activity has been phenomenal given the disruptions and with international tourism severely impacted. We estimate economic activity was just 1.7% below year-ago levels in Q3. It is also clear that the NZ economy is climbing out of recession over H2 much faster than we had previously expected.

NZ has performed well over the first 9-months of this year compared to most of our key trading partners (see accompanying chart). NZ's hard and early approach to try to eliminate the virus, combined with a reasonable degree of luck and our geographical isolation, look to have delivered a more modest drop in GDP and likely better health outcomes.



Source: Macrobond, ASB

Outlook and RBNZ Implications

We expect Q3 GDP growth will be close to the RBNZ's forecast and confirm that NZ is recovering from recession faster than expected earlier this year. At the November MPS the RBNZ was unconvinced that this momentum would be sustained and forecast that the economy will re-enter recession over H1 2021. While we are not quite so downbeat, we do acknowledge that further growth over 2021 is likely to be relatively soft given a number of headwinds, including closed international borders and higher unemployment. But there are also a number of tailwinds supporting NZ growth, including a strong (goods) export sector, low interest rates and strong housing demand. Furthermore, many New Zealanders will be looking forward to a nice break over summer and given the inability to travel overseas this past year, increased spending domestically may help fill in some of the hole left by dramatically fewer international visitors. The outlook still remains highly uncertain and we will be closely monitoring economic indicators and other readings on domestic and global growth. Early indicators for 2021 will be key in determining future policy direction for the RBNZ, but given the sizeable degree of monetary and fiscal support in place, positive vaccine developments (providing light at the end of the tunnel for firms and households) we believe no further OCR cuts are needed.

September quarter forecast detail

Within the retail sector, **accommodation and food services** were most impacted by the Alert Level restrictions, and the Retail Trade Survey shows activity for these retail sectors lifted 66% over Q3. While not a full recovery from pre-COVID levels, the level of activity did recover by more than we initially expected. Meanwhile, other retail volumes lifted 24%. The size of the lift in retail activity suggests there was an element of "catch up" from lost sales activity in Q2 supporting spending in Q3 – with spending on household durables particularly strong. Going forward the question is how well this can be sustained, with monthly electronic card spending data showing resilience. Low interest rates and record high levels of housing construction will continue to support spending on household furnishings and appliances. The key uncertainty will be to what extent the massive reduction in international visitors will hold back retail spending over the summer months.

Construction on buildings lifted 33% over Q3, with the level of housing construction lifting above pre-COVID levels. The strong housing market and rising dwelling consents suggests growth in construction activity will continue.

We expect **agricultural output** to be supported by solid milk production and a strong recovery in forestry production.

Manufacturing and wholesale trade activity have both bounced back strongly over Q3.

Given the resilience of the NZ economy, we expect **business services** will recover lost ground from the large Q2 fall. However, in **other services sectors** expect to only see a partial recovery given the ongoing impacts of the COVID-19 pandemic, and the higher Alert Levels during August. Areas more sensitive to border closures and higher alert levels include **transport and arts and recreation services.**

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