

NZ Q3 GDP: Crawling out

Q3 GDP rises 0.2% q/q

- The economy crawled out of recession in Q2 and Q3.
- Primary sectors drove growth in Q3, goods producing industries were weak.
- Consumer spending growth was stronger than expected.
- Monetary policy outlook remains unchanged, we expect the OCR to rise early in the New Year.

Key results

	Actuals		Q3 expectations		
	Q2	Q3	WBC	Mkt	RBNZ
GDP q/q	0.2	0.2	0.2	0.4	0.4
GDP y/y	-2.1	-1.3	-1.5	-1.2	
GDP annual average	-2.1	-2.2	-2.1	-2.0	-2.0

The economy crawled out of recession in the second and third quarters of 2009. The economy expanded 0.2% in Q3, the same rate of growth as in Q2 (that was revised up to 0.2% from the 0.1% originally published). All up, the GDP data gives further confirmation that the five quarter recession ended in the first three months of this year.

Even with the modest expansion through the middle of 2009, the level of activity in Q3 was still 2.9% below its peak in late 2007. For the economy as a whole, Q3 is likely to have been the toughest part of the cycle where activity was at its lowest point relative to its trend. Forecasts of strong growth ahead need to be put in the context of a weak starting point.

The details for Q3 showed strong growth in the primary sector, further contraction in manufacturing, construction and wholesale trade, with pockets of growth across the service sector.

Primary sector activity lifted 3.9% in Q3, with strong increases in mining, fishing, forestry and a solid lift in agriculture. Mining was the standout with an 11.0% increase in activity as the Maari oil field hit full production and an increase in exploration activity.

Figure 1: Production Based GDP

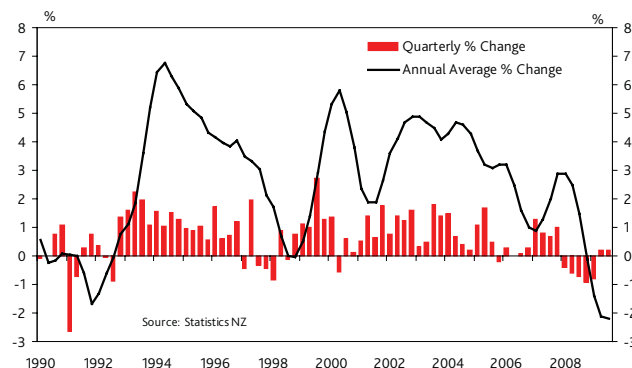


Figure 2: GDP Production Components

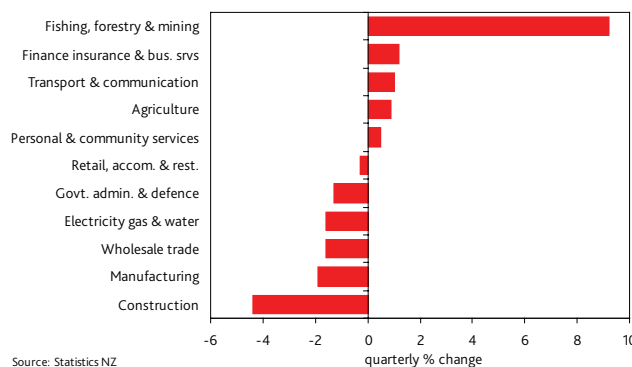
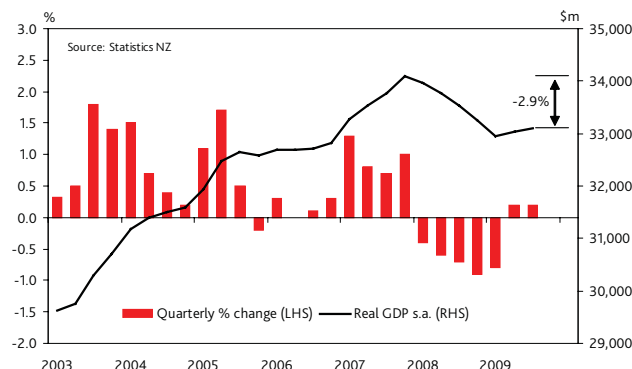


Figure 3: GDP level and growth



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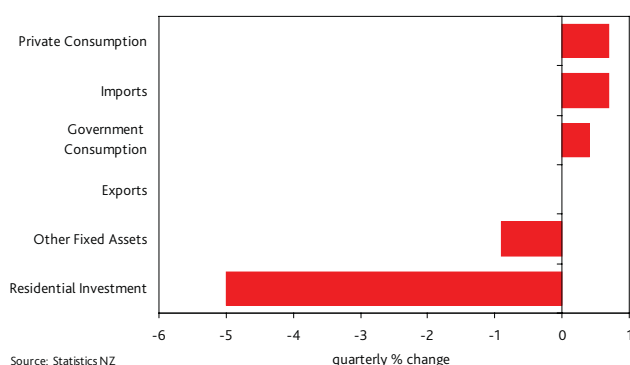
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The goods producing sector was still under the gun in Q3, posting its seventh consecutive quarter of decline. Manufacturing activity declined by 1.9%, driven by a 4.8% reduction in the food, beverage and tobacco manufacturing industry.

However, there were some positives, like the 1.3% lift in metal products as production at the Tiwai Point aluminium smelter was restored after a transformer failed in November 2008. Construction was as weak as we expected, falling 4.4%, driven by a 5% decline in residential investment.

The service sector was a mixed bag with a strong increase in the real estate and business services sector, but declines in wholesale and retail trade. At first glance, the contribution to quarterly growth from government is unclear with a 1.7% decline central government activity on the production side of GDP, but a 1.0% increase in central government expenditure. The expenditure measure is a better guide as it includes health and education, important for Q3 given that the Ministry of Health reported an increase in consultation rates for influenza-like illness above the normal winter levels. Despite a Swine Flu boost to activity in the health sector, we suspect there were larger negative effects spread across other sectors via absenteeism and/or less spending.

Figure 4: GDP Expenditure Components



Outlook positive

Our positive view for growth ahead remains unchanged with overall Q3 GDP panning out as we expected. If anything, we have gained more confidence in our view with stronger than expected consumer spending. The solid 0.8% increase in household spending will help stir growth in the goods producing sector ahead, as will a strong Australian economy and a favourable exchange rate. The very low level of construction activity in Q3 and the gains in building consents to date suggest the construction sector, along with the goods producing sector, will make a strong contribution to economic growth in 2010.

Market implications and outlook

Q3 GDP was a mild downside surprise to market expectations, with the NZD dropping around a third of a cent against the USD following the release. However, the degree of surprise was watered down by a mild upward revision to Q2 and the return of solid consumer spending. We estimate consumer spending growth in the quarter was around 0.5% higher than the RBNZ had factored in. These positive details have no doubt encouraged the NZD to recover about half of its initial drop.

Overall, the data was most likely not sufficiently different to expectations to materially alter anyone's view on the economy. We think significantly stronger growth in Q4 and beyond, combined with the early-than-expected return of the consumer, suggest the first hike in interest rates will come relative early in the New Year. Our pick remains March for the first hike in the OCR.

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