Economic Bulletin.

17 June 2021

GDP review, March quarter 2021.

- GDP rose by 1.6% in the March quarter, following a 1% loss in December.
- The surprise was not in the sources of growth, but rather the magnitude.
- Efforts to capture the disruptive effects of Covid-19 on activity appear to have introduced more volatility into the data.
- The reported growth in household spending is particularly hard to account for.
- We think that some of the surprises in today's data will be unwound. We've trimmed back our forecast of June quarter GDP growth from 1.2% to 0.6%.
- We still regard the economy as running below its full potential, although the gap is closing faster than we expected.

Michael Gordon, Senior Economist
+64 9 336 5670

Gregorius Steven, Economist
+64 9 367 3978

Key results	Mar 21	Dec 20	Westpac f/c	Market f/c
GDP qtr %	**1.6%**	-1.0%	0.6%	0.5%
GDP ann %	**2.4%**	-0.8%	0.9%	0.9%
GDP ann avg %	**-2.3%**	-2.9%	-2.7%	-2.8%

New Zealand's GDP rose by 1.6% in the March quarter, following the 1% drop in the December quarter last year. The result was stronger than our forecast of a 0.6% rise, which was in line with the rest of the market. The Reserve Bank had assumed a 0.6% fall in its May *Monetary Policy Statement*.

We're not convinced that all of this quarter's surprise will be sustained. Accordingly, we've shaded down our growth forecast for the following quarter from 1.2% to 0.6%. That's still a solid gain, and reflects the fact that the economy has now moved beyond the challenge of a summer without overseas tourists.

The level of GDP is around 3% below what we were forecasting before Covid-19 hit. Lower population growth due to the near-halt on migration accounts for about 1 percentage point of that; the rest is in line with the net impact from the loss of international tourism. Consequently, we're less concerned than others about the risk of overheating and inflation – we still see the economy as running below its full potential, though admittedly the gap is narrowing faster than we expected.

Details.

The sources of growth in the March quarter were mostly in line with our forecast. Rising incomes and house prices have boosted sectors such as retailing and hospitality, while the red-hot construction sector has in turn lifted demand in areas such as manufacturing. The continued containment of Covid has meant that domestic tourism has been able to provide something of a cushion to the hospitality sector.

What surprised us was the magnitude of the gains. Some of these sectors saw even stronger growth than what their usual indicators had suggested, and in some cases the rate of growth is hard to fathom. Over the last year, Stats NZ has been using different data sources and methods to try to capture the disruptive effects of Covid-19. But in doing so, this seems to have introduced some new volatility into the data.

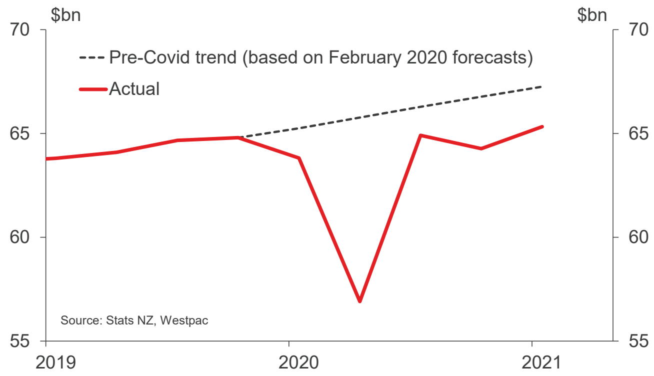
The results are even more puzzling when we turn to the expenditure measure of GDP, particularly the reported 5.5% surge in household consumption. Some aspects of this are plausible – for instance, spending on household goods has been unusually high as people have substituted away from spending on overseas travel.

Other aspects are more questionable. Recreational and cultural spending was reported to be 25% above pre-Covid levels, even with fewer movie releases, concerts, sporting events and so on. Meanwhile, restaurants and hotels will be surprised to hear that their turnover was 45% above pre-Covid levels.

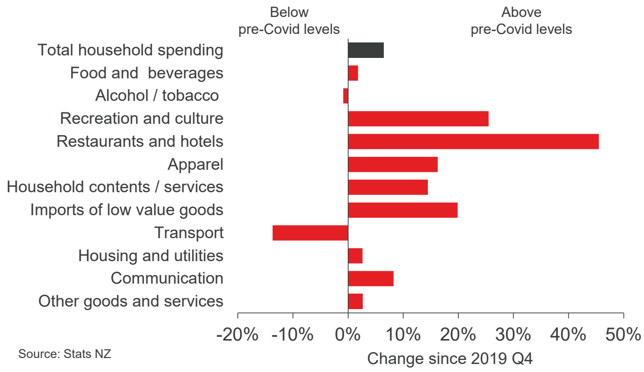
Generally it’s not a good reason to dismiss the official data just because it doesn’t fit with your existing views. But the fact is that we’ve been here before. In the September quarter we saw similarly large upside surprises in sectors like construction and healthcare. Those were promptly reversed in the December, leaving us with a 1% drop in GDP. We see a risk of a similar correction this time, if not immediately then in subsequent quarters.

The reality is that it could be several years, and many rounds of data revisions, before we get a reliable picture of how the economy fared through the Covid era. In the meantime, it will pay to look at a broader suite of indicators to gauge how hot the economy is running. For example, an unemployment rate of 4.7% suggests that there’s still slack in the labour market as a whole, which is consistent with our view that the level of GDP is below its full potential.

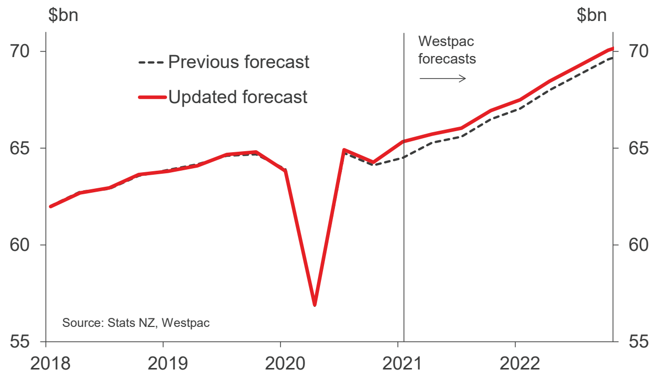
Quarterly GDP level



Household spending compared to pre-Covid levels



Quarterly GDP forecasts



Contact the Westpac economics team.

Michael Gordon, Acting Chief Economist
+64 9 336 5670

Satish Ranchhod, Senior Economist
+64 9 336 5668

Nathan Penny, Senior Agri Economist
+64 9 348 9114

Paul Clark, Industry Economist
+64 9 336 5656

Gregorius Steven, Economist
+64 9 367 3978

Any questions email:
economics@westpac.co.nz

Past performance is not a reliable indicator of future performance. The forecasts given in this document are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Disclaimer.