Westpac

Institutional Bank

14 March 2014

Better times

Preview of December 2013 quarter GDP (20 Mar, 10:45am) and current account (19 Mar, 10:45am)

- We estimate that GDP rose 0.9% in the December quarter, following a 1.4% rise in the September quarter.
- Excluding the impact of the drought in early 2013 and the subsequent rebound, our forecast implies that quarterly GDP growth steadily gathered momentum over 2013.
- The annual current account deficit is likely to have narrowed sharply as dairy exports returned to their pre-drought trend.

	Sep-13 actual	Dec-13 Westpac f/c	Dec-13 Market f/c
Balance of Payments (19 Mar)			
Current account balance $m	-4,774	-1,340	-1,410
Annual balance $m	-8,764	-7,350	-7,410
Annual balance % of GDP	-4.1	-3.3	-3.3
GDP (20 Mar)			
Quarterly % chg	1.4	0.9	0.9
Annual % chg	3.5	3.0	3.0
Annual average % chg	2.6	2.7	2.7

Next week's national accounts data will show a continuation of the strong form that the New Zealand economy exhibited over the course of 2013. We estimate that the annual current account deficit narrowed to 3.3% of GDP as dairy export volumes rebounded sharply from the drought earlier in the year. In terms of production, though, the recovery in dairying actually occurred in the September quarter; in contrast, we don't see any standout factors driving December quarter GDP, and the 0.9% increase that we're expecting is probably a fair reflection of the economy's general momentum.

Q4 GDP, 20 March

The short but intense drought in early 2013 led to some choppiness in the quarterly GDP figures over the course of the year, restraining growth over the first half then driving a sharp bounce in the September quarter. Agriculture (including meat and dairy processing) accounted for around 0.6 percentage points of the 1.4% rise in September quarter GDP, implying an underlying growth pace of around 0.8%.

In contrast, with agriculture and processing more or less back in full swing by the December quarter, we estimate their total contribution to growth was close to zero. Instead, our forecast of a 0.9% rise in GDP reflects steady gains across a broad range of sectors, and suggests that ex-agricultural GDP growth gradually accelerated over the course of 2013.

The largest contributions to growth in the December quarter were from manufacturing and wholesale trade (though the latter is a reflection of strong activity more generally, rather than a source of growth in its own right). We also expect solid gains in personal and business services, retail trade, electricity (due to a shift to higher-value hydro generation), transport and financial services.

Construction is shaping up for another quarter of weakness, despite the clear ramping-up of rebuilding activity in the Canterbury region. The building work survey showed a 1% decline in Q4, though this could be offset by a pickup in infrastructure work after a steep fall in Q3. We don't think that the recent outturns threaten the story that building activity will be an important driver of growth over 2014; building consents show that there is a great deal of work in the pipeline, and the timeline for the Christchurch rebuild points to a fresh wave of activity this year.

Q4 current account, 19 March

We estimate that the current account deficit narrowed to 3.3% of GDP in the year to December, from 4.1% in the year to September. If so, this would be the biggest one-quarter improvement in the deficit on record outside of a recession (the deficit tends to narrow in recessions as import demand falls).

The main factor behind this is an almost unprecedented jump in export volumes (in the order of 10% in seasonally adjusted terms).Although milk production had returned to its pre-drought trend by the September quarter, shipments of dairy exports didn't follow suit until the December quarter. In addition, there was a strong lift in exports of meat and manufactured goods, both of which had softened over the previous two quarters.

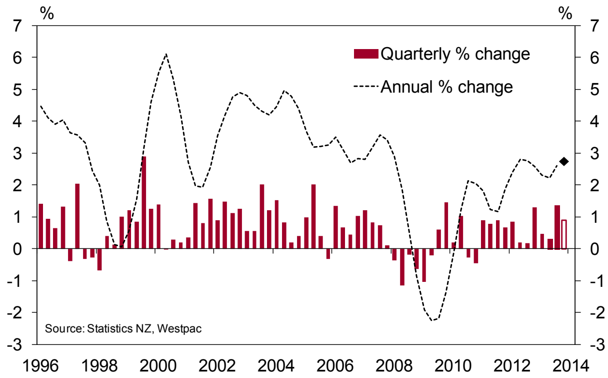
The dramatic improvement in the goods trade balance could be offset to a small degree by a widening of the investment income deficit. Profits of overseas-owned firms in New Zealand have been gradually increasing as the economy gathers momentum. As interest rates rise over the next few years, higher interest costs on overseas borrowing are likely to widen the deficit further.

Market implications

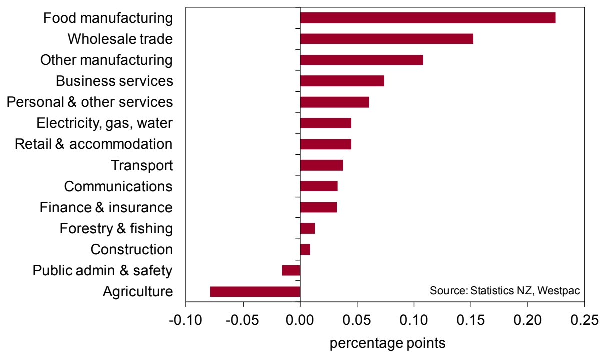
While good economic results are always welcome, they're unlikely to cause much of a stir in financial markets if they come in as we expect. The median market forecasts for both the current account and GDP are bang in line with our own forecasts, while the Reserve Bank estimated a 0.8% lift in GDP in yesterday's *Monetary Policy Statement* (though this would have been finalised before the sectoral indicators that were published over the last fortnight).

Interest rate markets are still not quite on board with the RBNZ's projection of five OCR hikes this year (including yesterday's opener), so a stronger than expected outturn on GDP has the potential to shunt interest rates higher.

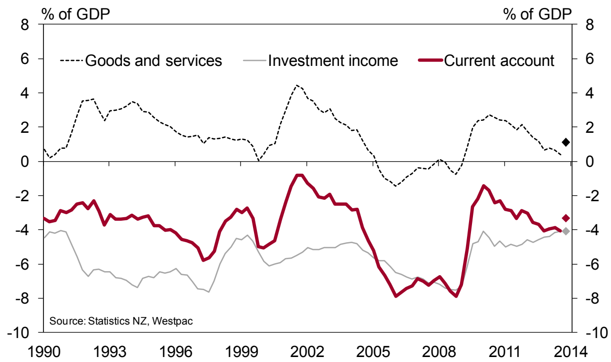
Production-based GDP



Contributions to Q4 GDP growth



Annual current account balance



Michael Gordon
Senior Economist

Westpac economics team contact details

Dominick Stephens, Chief Economist
+64 9 336 5671

Michael Gordon, Senior Economist
+64 9 336 5670

Felix Delbrück, Senior Economist
+64 9 336 5668

Anne Boniface, Senior Economist
+64 9 336 5669

Any questions email:
economics@westpac.co.nz

For email address changes contact:
WNZResearch@westpac.co.nz

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