

No cause for alarm

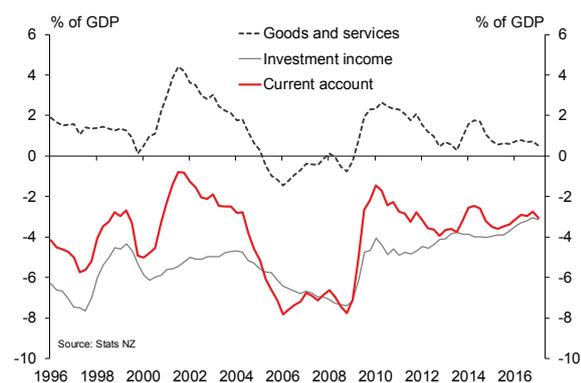
Q1 current account widens to 3.1% of GDP

14 June 2017

- The current account deficit widened to 3.1% of GDP in the year to March.
- The increase in the deficit reflected temporary weakness in export volumes, stronger spending by New Zealanders overseas, and stronger profits for overseas-owned firms in New Zealand.
- A string of modest current account deficits has led to a marked improvement in New Zealand's external debt position in recent years.

Current account balance	Q1 2017	Q4 2016
Quarterly (s.a.) \$m	-2,836	-1,693
Annual \$m	-8,132	-7,192
Annual % of GDP	3.1%	2.8%

Annual current account balance



New Zealand's current account deficit widened to 3.1% of GDP in the year to March, compared to an upwardly revised deficit of 2.8% in December. This result was in contrast to market expectations of an unchanged deficit, but was close to our forecast of -3.0%.

The widening of the deficit was due to a combination of factors, none of which were particular cause for alarm. The current account deficit is effectively back to where it was a year ago, and it remains remarkably low compared to history. New Zealand's net international liability position continues to shrink, and as a share of GDP is at its smallest in decades.

Today's data has no implications for tomorrow's March quarter GDP report, where we expect a 0.8% increase. The only surprise relative to our forecasts was a larger investment income deficit, which doesn't enter the activity data.

Details

In seasonally adjusted terms, the goods trade deficit widened to \$1.2bn in the March quarter, the weakest quarterly balance since June 2008. While New Zealand's terms of trade (the ratio of export prices to import prices) rose to a 44-year high, trade volumes were relatively unfavourable. In particular, export volumes appear to have to fallen sharply for a second straight quarter.

We think the weakness in exports will be temporary. Milk production was very weak in late 2016, and given the usual lag between production and shipment, this manifested as a drop in dairy export volumes in the December and March quarters. However, we know that milk production has since rebounded, as the weather has improved and higher milk prices have encouraged more production. Consequently, we expect a strong rebound in exports in the June quarter and beyond.

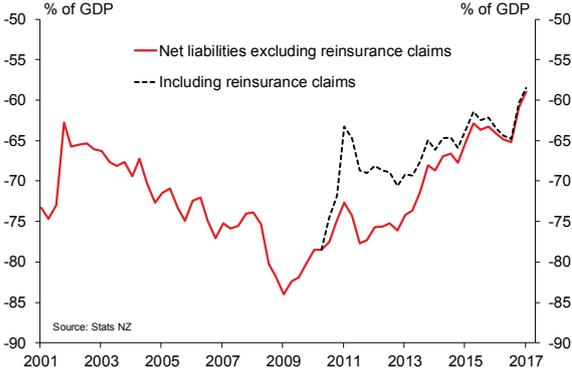
The services trade balance receded from \$1.2bn to \$1.0bn in the March quarter. A modest rise in spending by overseas visitors in New Zealand was outweighed by a strong rise in spending by New Zealanders overseas. The latter, along with strong growth in local retail sales over the quarter, suggests that households are still keen to spend.

The investment income deficit widened to \$2.2bn in March compared to \$2.0bn in December. This was largely due to a sharp lift in profits earned by overseas-owned firms in New Zealand (excluding bank profits, which according to our records were flat for the quarter). This is a positive indicator of business conditions within New Zealand, although we'd be wary of putting too much weight on this quite volatile component.

New Zealand's net liability position improved further in the March, reaching a multi-decade low of 58.5% of GDP. Only a small part of this improvement is due to reinsurance claims from the Christchurch and Kaikoura earthquakes. The main drivers have been the persistently low current account deficit (which has meant a relatively modest funding requirement), and favourable movements in the market value of assets.

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International investment position



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