# As bad as it gets?

## Q4 current account deficit widens to 3.7% of GDP

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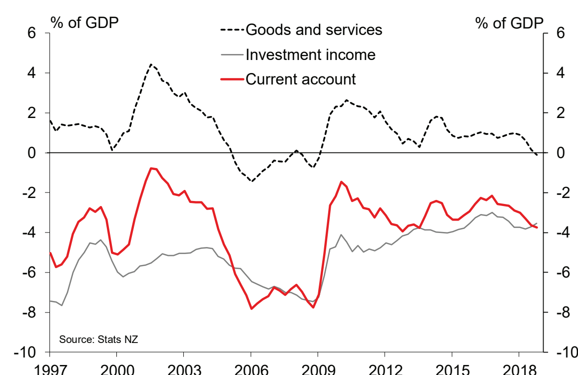
- The current account deficit widened from 3.6% to 3.7% of GDP in the year to December, a smaller increase than we expected.
- The balance of goods trade moved further into deficit, offset by higher tourism earnings and solid investment income inflows.
- The deficit has widened over the last year due to a decline in the terms of trade and, until recently, high import volumes.
- With trade prices turning more favourable in recent months, we expect the current account deficit to narrow again over 2019.

| Current account balance | Dec 2018 | Sep 2018 |
|---|---|---|
| Quarterly (s.a.) $m | -2,471 | -2,494 |
| Annual $m | -10,974 | -10,565 |
| Annual % of GDP | 3.7% | 3.6% |

**Annual current account balance**




New Zealand's annual current account deficit widened from 3.6% to 3.7% of GDP in the December quarter, reaching its highest level since September 2013. That was less of an increase than we expected, but the surprises in today's release don't have much bearing on the state of the local economy.

The widening of the current account deficit over the last year is not too concerning by historic standards. That said, it is getting a bit beyond what we would consider to be sustainable over the long term. New Zealand's net overseas debt position has been steadily improving over the last decade, but that improvement would soon start to reverse course if the current account deficit widened further.

Fortunately, there are some more positive signs on the horizon. New Zealand's trade prices have turned more favourable in recent months, with a sharp rise in dairy export prices and a fall in oil import prices. We expect the deficit to narrow again over the course of 2019.

Today's results have no implications for tomorrow's GDP release. We expect a subdued 0.3% rise in GDP for the December quarter.

### Details

In seasonally adjusted terms, the December quarter deficit was close to $2.5bn, similar to the previous quarter. The goods trade deficit worsened, but this was balanced out by a small improvement in the services trade balance and stronger investment income inflows.

The widening of the goods trade deficit over the last year partly reflects a decline in the terms of trade. Dairy export prices fell over 2018, while oil import prices rose significantly. (The sharp fall in oil prices in late 2018 had yet to be reflected in the shipments to New Zealand up to December.) Import volumes also remained high over much of 2018, though they look to have eased back in the latest quarter.

Trade in services maintained its substantial surplus. Tourism earnings rose as visitor numbers picked up in the December quarter, after a small decline in the September quarter.

The investment income deficit narrowed in the December quarter. New Zealanders enjoyed better returns on their overseas investments, while the returns accruing to foreign investors in New Zealand were down a little.

Relative to our forecast, the surprise in today's figures was down to two factors. The first was that earnings from New Zealand's overseas investments were substantially higher than we expected – typically there is a seasonal dip in the December quarter.

The second factor was an unusually large negative 'conceptual adjustment' to imports. These adjustments usually relate to matters of timing, or of ownership – for instance, capital equipment that was brought into the country during the quarter may have been reclassified as leased rather than owned. From a GDP perspective, this will probably detract from imports and business investment in equal measure, with no net impact.

New Zealand's net overseas liabilities widened substantially to 57% of GDP in the December quarter, breaking a recent run of steady improvements. However, this wasn't due to an increase in overseas borrowing – the net debt proportion of the balance actually improved slightly, from -52% to -51% of GDP. Rather, it was driven by a mark-to-market loss on the value of equity investments, as global sharemarkets lurched lower at the end of 2018. That fall has largely been reversed in the early part of this year.

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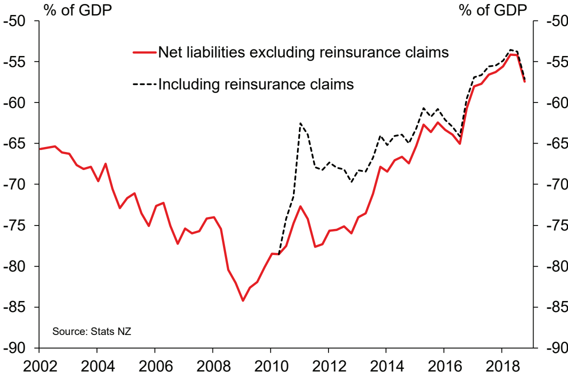
Senior Economist

**International investment position**



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