



## **New Zealand: Recent Economic Developments**

---

### **Key facts about the New Zealand government:**

- Prime Minister: Jacinda Ardern (Labour Party).
- Finance Minister: Grant Robertson (Labour Party).
- Governing coalition:
  - Labour – New Zealand First coalition (55 of 120 seats in the Parliament) with external support from the Green party (8 seats).
- Date of next parliamentary elections: by November 2020.
- Economics issues the government is pursuing:
  - Revising fiscal policy by potentially introducing a capital gains tax, among other proposed changes.
  - Strengthening its trade relationship with China, its largest trading partner, following recent political and U.S.-trade tensions.
  - Negotiating a free trade agreement with the European Union.
- Governor of the Reserve Bank of New Zealand: Adrian Orr (to serve until March 27, 2023).

### **Suggested topics of discussion on the New Zealand economy:**

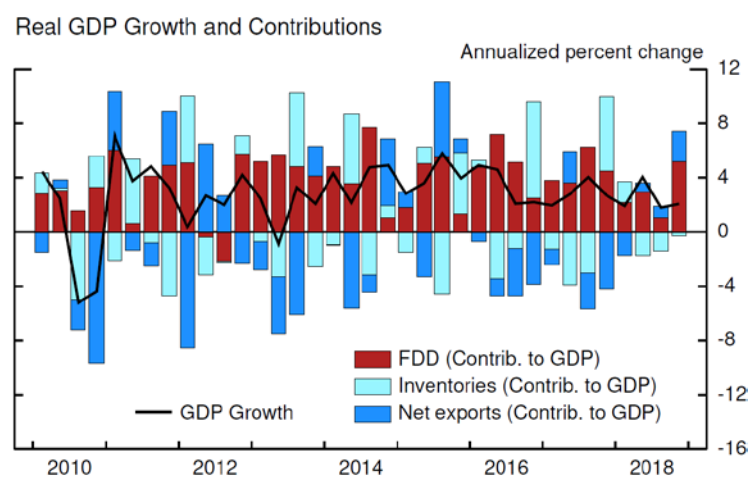
- How might a *Chinese slowdown and/or further U.S.-trade tensions with China* affect the New Zealand economy?
- How might Brexit affect New Zealand's *trade and/or ongoing trade negotiations* with the European Union?
- The New Zealand government may soon propose a *capital gains tax* and plans to release a proposal for a *digital services tax* in May. What are the prospects for these taxes, and what issues could they raise?
- How might the Reserve Bank of New Zealand's *new Monetary Policy Committee* alter monetary policy decisions and the monetary policy path in New Zealand?

## Fiscal Policy

- **New Zealand's budget balance has returned to positive territory following years of deficit spending in the wake of the global financial crisis and natural disasters.** The operating balance reached 1.9 percent of GDP in 2018, up from negative 9 percent of GDP in 2011, a 24-year low. The operating balance increased gradually over the intervening years thanks to shrinking government expenditures and strong economic growth.
  - In its Half Year Economic and Fiscal Update from December 2018, the Treasury forecasted a dip in the operating balance in 2019, followed by a gradual rise to above its current level. The next government budget will be released in May.
  - New Zealand's central government debt has risen to 32 percent of GDP from 16 percent of GDP in 2007, and has been trending downward in recent years.
- **New Zealand's government is pursuing several fiscal reforms.** On April 1, an R&D tax credit was introduced, levies for state-sponsored accident insurance were decreased, and the minimum wage was raised. The government is also considering a digital services tax and, controversially, a capital gains tax, following recommendations from the Tax Working Group, a government-sanctioned fiscal advisory group.

## Economic Activity

- **New Zealand has enjoyed strong economic growth since 2013,** fueled by accommodative monetary policy, an influx of migrants and tourists, improving terms of trade, and healthy residential and construction investment.
  - According to the Treasury, low business confidence threatens the domestic outlook, while U.S.-China trade tensions and Brexit put some of New Zealand's important trading partners at risk.

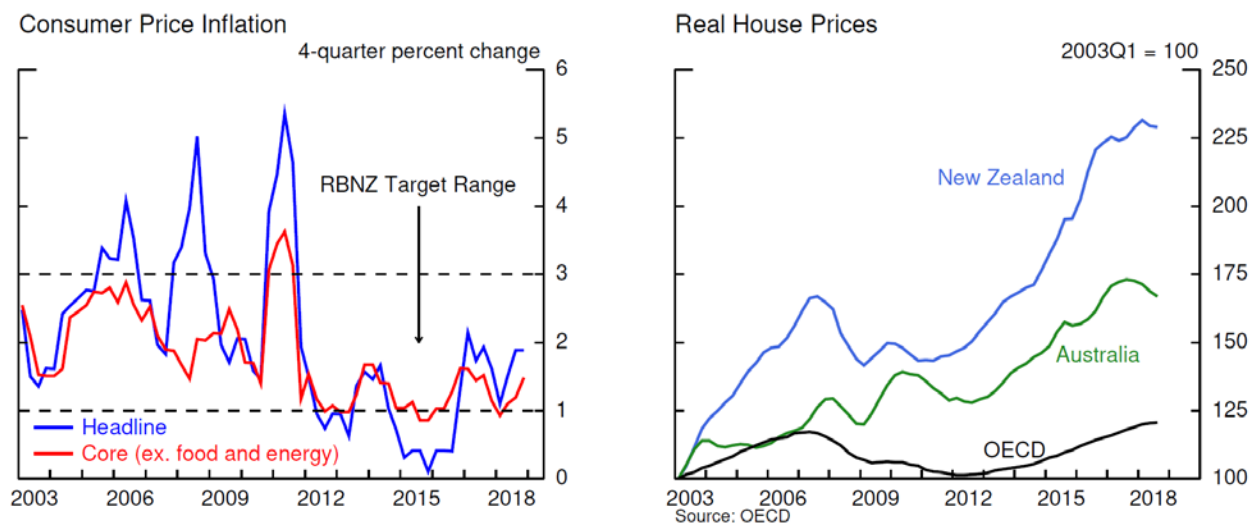


- **The labor market is tight, putting recent upward pressure on wages.** The unemployment rate decreased from a 13-year high of 6.7 percent in 2012 to 4.3 percent in 2018, near the Reserve Bank of New Zealand's estimate of the NAIRU, and the labor force participation rate reached an all-time high last year. Meanwhile, 4-quarter average hourly earnings growth recently rose to above its long-term average.

- **China is an important trading partner for New Zealand.** Exports to China have quadrupled since a free-trade agreement took effect in 2008, and currently account for about one-third of New Zealand's total exports. By comparison, exports to the United States account for just over eight percent of New Zealand's total exports.
  - New Zealand is seeking to upgrade its trade agreement with China and is negotiating a free-trade agreement with the European Union, another important trading partner.

## Inflation

- **Headline inflation has been in the Reserve Bank of New Zealand (RBNZ) 1-3 percent target range since 2016.** In 2018, headline inflation returned to the 2 percent midpoint target amid increasing oil prices. The RBNZ expects low interest rates, a strong labor market, and declining profit margins to cause a gradual increase in inflation in the near term.

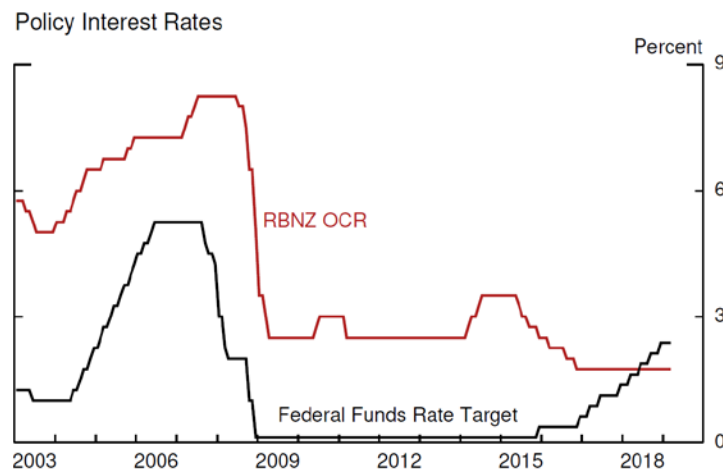


- **Nominal house prices have increased 60 percent since the beginning of 2011**, though they have shown signs of moderation since 2017, prompting the RBNZ to relax loan-to-value-ratio restrictions first enacted in October 2013. Despite the recent price moderation, the RBNZ acknowledged in their most recent Financial Stability Report that household consumption remains vulnerable due to the possibility of a housing price correction.

## Monetary Policy

- **Adrian Orr was appointed Governor of the Reserve Bank of New Zealand (RBNZ) in March 2018**, after which Governor Orr and Finance Minister Grant Robertson agreed to add maximum employment to the RBNZ's policy mandate. Prior to April 2019, the RBNZ's governor had full control over policy rate changes; RBNZ policy decisions are now conducted by a monetary policy committee composed of seven members.
- **The RBNZ has held its main policy rate, the Official Cash Rate (OCR), at a record low of 1.75 percent since November 2016.**

- After leaving the policy rate unchanged on March 27, Governor Orr said the next move in the OCR will more likely be down than up, citing a weaker outlook among key trading partners such as Australia, Europe, and China, a softer housing sector, and low business sentiment as cause for a more dovish outlook.
- The RBNZ last raised rates in mid-2014 amid rising domestic demand, but cut rates during 2015 and 2016 to combat disinflationary pressures and a weaker growth outlook. The OCR has been on hold for the past two years.



## Financial Markets

- **The New Zealand dollar (the “Kiwi”) is currently trading at 1.48 per U.S. dollar.** Relative to the U.S. dollar, the Kiwi has appreciated 8 percent since its six year low in September 2015 and just 1 percent year-to-date. The Reserve Bank of New Zealand said in March that the Kiwi is facing upward pressure due easing policy outlooks among other central banks.
- **The New Zealand equity price index, NZX50, has experienced high returns relative to global financial markets.** The NZX50 has appreciated 13 percent year-to-date.

