Westpac Institutional Bank

One hit wonder

Q1 Current account preview: 22/06 10:45am NZT

- **We expect reinsurance flows propelled New Zealand's Current Account into rare surplus territory in the year to March... just, at +0.2% of GDP.**
- **While multibillion-dollar reinsurance flows will dominate the headline this quarter, the underlying picture continues to be one of relative strength in New Zealand's external position.**
- **Exporters continue to benefit from record commodity prices, although volume growth was subdued this quarter. Imports carry on tracking higher in line with the recovery in consumer spending and improving business investment.**

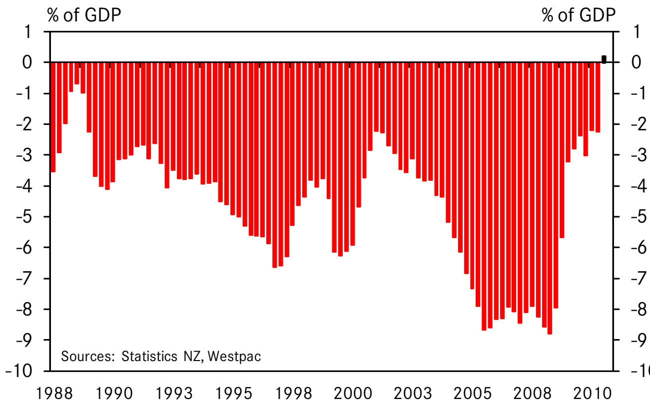
New Zealand's current account deficit has been shaken up in recent quarters as the national accounts feel the financial effects of the devastating Canterbury earthquakes. From a current account perspective, it is the flow of reinsurance funds from overseas reinsurers to New Zealand insurers that will dominate the March quarter (from the balance of payments perspective, regardless of when the money enters the country, it is recorded in the quarter in which the insured event occurred).

We, like other forecasters, believe a substantial proportion of the estimated $15bn plus cost of the Canterbury earthquakes will be covered by offshore reinsurance companies. But narrowing this down to a more concrete estimate is rather more difficult. We've gone with a $6bn contribution in the March quarter (which will come on top of the $3.6bn of reinsurance flows already recorded in the September quarter). But just to confuse matters further, even if reinsurance flows do eventually add up to this total, this may not be Stats NZ's first estimate. (As we saw in the September quarter, the first estimate put reinsurance flows at $1.7bn, this was more than doubled in the second estimate to $3.6bn.)

Yet whatever the size of these reinsurance flows, the direction of their impact is clear. The March quarter will see a substantial, sharp and temporary improvement in New Zealand's current account deficit.

The earthquake prompted a fall in the number of overseas visitors arriving in NZ in the March quarter – arrivals were down 2%. Yet surprisingly, surveys suggest that overall spending by visitors actually rose slightly in the 3 months to March. At the same time, the strength of the NZD combined with affordable international airfares have seen increasing numbers of New Zealanders heading overseas (short term departures rose 2.1% in the quarter). On balance, we expect the services trade deficit to narrow marginally in the March quarter.

NZ annual current account deficit



Current Account components ($million)

	Mar-10	Jun	Sep	Dec	Mar (f)
Goods Balance s.a.	919	1,166	790	568	480
Services Balance s.a.	-44	-86	-166	-247	-240
Investment Inc Bal	-2,346	-2,885	-2,393	-3096	-2,950
Transfers Balance	167	-121	3,506	-12	5,950
Current Account Bal	-1,305	-1,927	1,737	-2,813	3,290
CAB Annual total	-4,458	-5,707	-4,188	-4,380	360
Annual CAB, %	-2.4	-3.0	-2.2	-2.3	0.2

While uncertainty abounds in transfer flows, the underlying merchandise trade story is an altogether more transparent one. Clearly, emerging market demand for commodities has pushed prices higher – to record levels in a number of cases –benefiting New Zealand's external position. Imports continue to increase, in line with the modest improvement in retail spending, but another trade surplus will be recorded this quarter.

Market Implications:

New Zealand's current account hasn't been garnering too much attention of late as it remains much smaller than recent levels. To the extent that the March quarter current account data will be swamped by one-off reinsurance flows, even a current account surplus shouldn't surprise informed market participants too much.

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