Westpac Institutional Bank

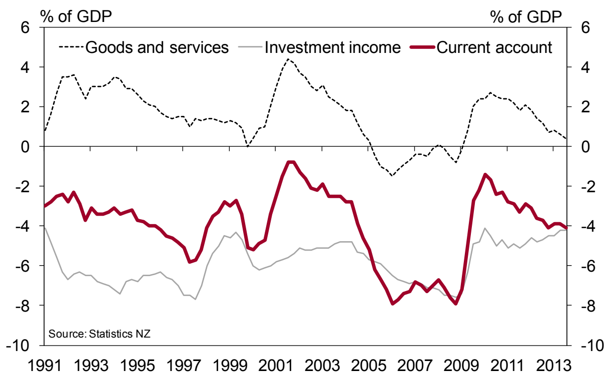
18 December 2013

Rewriting history

Q3 current account deficit widens after revisions, to 4.1% of GDP

- The current account deficit widened to 4.1% of GDP in the year to September, from a revised 3.9% deficit in June.
- Imports rose faster than exports in the September quarter, with a sharp lift in imports of capital equipment that partly reflects one-off items.
- Improvements to the measurement of some series have narrowed the size of the deficit going back several decades.
- While New Zealand still faces a persistent current account deficit, it is no longer the international outlier that it once seemed.

NZ annual current account balance



New Zealand's current account deficit over the year to September was in line with our forecast and the median market expectation of 4.1% of GDP. The deficit widened relative to June thanks to a sharp rise in imports, though to some degree this reflected valuable business investment as the domestic economy continues to pick up. Revisions to history have resulted in an improvement in New Zealand's external position going back more than three decades, though these revisions were well flagged ahead of the release.

The improved measurement of the current account deficit is a positive for perceptions of New Zealand's international position. We have long argued that New Zealand's current account deficit is overstated, and the revisions in today's release are just the latest in a series of improvements by Statistics NZ that have narrowed the reported deficit.

Details

In seasonally adjusted terms, the current account deficit widened to $2.58bn in the September quarter, from $2.23bn in the June quarter. The main source of the deterioration was the balance of trade in goods, which fell to a $524m deficit in September from a $167m deficit in June.

Goods exports rose by around 6%, as a sharp lift in dairy product prices more than compensated for subdued volumes as a result of the drought earlier this year. However, imports jumped by around 9% for the quarter, one of the biggest quarterly increases on record. As detailed in the Terms of Trade earlier this month, part of the rise was due to non-recurring items: a floating oil platform and a group of military helicopters, both items worth around $200m each. But there was also a sizeable lift in imports of capital equipment, passenger cars and consumer goods – a symptom of growing domestic demand.

The services balance narrowed slightly to a $297m surplus. A lift in spending by overseas visitors was offset by a drop in exports of business services, while imports of services rose across a range of categories.

The investment income deficit was little changed at $2.18bn, more or less in line with our forecast although both sides of the ledger were larger than we expected. Overseas investment income earned by New Zealanders rose to $1.72bn, the second-largest quarter on record. As the outlook for the global economy has picked up, New Zealanders have both reallocated their portfolios towards overseas equities, and have received better returns on those equities. On the other side, though, profits of overseas-owned firms in New Zealand rose by more than we expected. (There was also an upward revision to the June quarter figure, which had looked surprisingly low at the time.)

Revisions

Statistics NZ has made two substantial improvements to the measurement of the current account, narrowing the level of the deficit over history. The first is an improved estimate of spending by overseas visitors (backdated as far as 1982) and international students (back to 2003), which has added around $2.1bn to exports of services over the last year. The second change is a new estimate of imports of low-value items (which are not otherwise recorded by Customs), worth around $1bn in the last year.

The net impact is that the current account deficit over the year to September was around $1bn or 0.5% of GDP narrower than it would have been without these improvements. The net revisions have been even greater in past years, peaking at an improvement of 1.4% of GDP in the year to March 2004 (from -4.2% to -2.8%). However, the impact has waned in the last few years as imports of low-value goods have grown faster than spending by overseas visitors, and that will probably remain the case for a while longer.

We have long been arguing that New Zealand's international accounts suffer from mismeasurements that make us look like an implausibly large outlier, and revisions over the last several years have gone some way to addressing our concerns. Notably, the revisions to the current account deficit have not been accompanied by a revision to New Zealand's net international liabilities – even though it amounts to around $30bn of accumulated 'deficits' that no longer exist and hence no longer need an account of how they were funded.

Implications

The annual current account balance was in line with market forecasts, though we suspect there may have been offsetting surprises – the deficit for the September quarter was larger than markets expected, but few forecasters seem to have anticipated the revisions to history. The New Zealand dollar was unmoved after the release.

Today's revisions suggest that the New Zealand economy is on stronger macroeconomic ground than was previously portrayed. In theory, this should be positive for the NZ dollar, and put downward pressure on government bond yields – a better balance of payments position may make international investors more predisposed to lend to New Zealand entities, and may ease the concerns of credit rating agencies. Indeed, it's notable that our current account deficit is no longer the outlier among developed economies. Today's revisions (along with revisions that have widened Australia's deficit) mean that since 1988 our current account deficit has averaged 3.8% of GDP, compared to 4.3% in Australia. Our net liability position remains an outlier, but we suspect there are some gaps in the data (particularly for holdings of overseas assets) that would leave us closer to the pack if they could be addressed.

Michael Gordon
Senior Economist

Current Account components ($m)

	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13
Goods balance (s.a.)	-39	159	340	-167	-524
Services balance (s.a.)	286	156	313	380	297
Balance on investment income	-2,208	-2,243	-2,240	-2,205	-2,184
Balnace on current transfers	-149	-91	-140	-205	-149
Current account balance (s.a.)	-2145	-2053	-1758	-2229	-2578
Annual current account balance	-7744	-8590	-8349	-8244	-8766
Annual CAB, % of GDP	-3.7	-4.1	-3.9	-3.9	-4.1

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