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Economic Analysis - New Zealand's Fiscal Surplus To Narrow Due To Slowing Revenue Collection

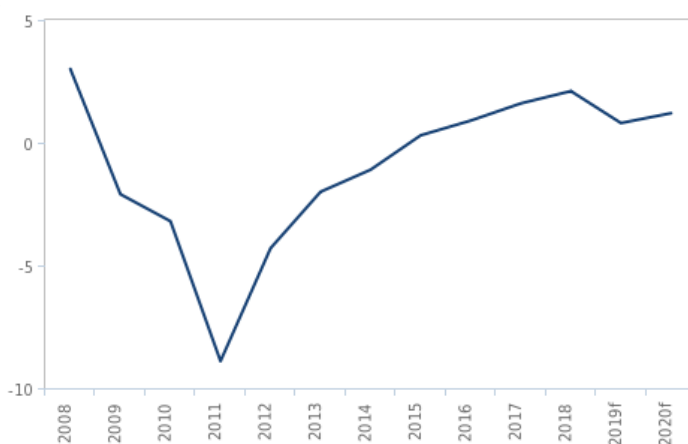
24 Jan 2019 | New Zealand | Fiscal Policy

- We forecast New Zealand's fiscal surplus to narrow to 0.8% of GDP in FY2018/19 (July-June) and 1.2% in FY2019/20, relative to 2.1% in FY2017/18, marking a downward revision from our previous forecasts of 2.0% and 1.9% respectively.
- This is on the back of the country's slowing economic growth, which we expect to weigh on revenue collection over the coming quarters, combined with greater spending as outlined in the new Wellbeing Budget for 2019.
- That said, New Zealand's public finances are likely to remain healthy, posing little risk to macroeconomic stability.

We at Fitch Solutions have revised our forecast for New Zealand's fiscal surplus as a share of GDP to 0.8% in FY2018/19 (July-June) and 1.2% in FY2019/20 (from 2.0% and 1.9% respectively). Our view is informed by an expected slowdown in GDP growth, coupled with increased expenditure from the country's upcoming 2019 budget set to be released in May. That said, we believe that New Zealand will continue to enjoy a strong fiscal position, with room for the government to enact expansionary fiscal policy if necessary.

Fiscal Surplus Expected To Narrow

New Zealand - Fiscal Balance, % Of GDP



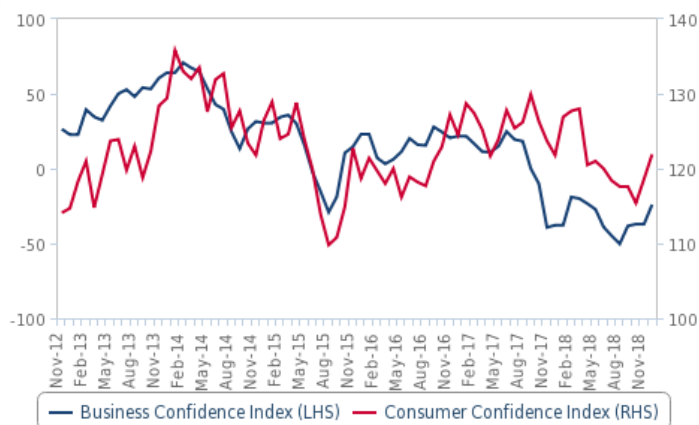
Source: New Zealand Treasury, Fitch Solutions

On December 13, New Zealand released its updated fiscal figures for FY2018/19, and updated its forecasts for fiscal revenue and expenditure up until FY2022/23 in its Half-Year Economic and Fiscal Update 2018 release. The government forecasts the fiscal surplus to decline to 0.7% of GDP in FY2018/19 and 1.4% in FY2019/20 from 2.1% in FY2017/18. This marks a downward revision from its previous forecast of 1.4% in FY2018/19 and 1.8% in FY2019/20, respectively.

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Consumption And Investment Sentiment To Remain Weak

New Zealand - Business Confidence Index & Consumer Confidence Index



Source: Bloomberg, Fitch Solutions

We expect a slowdown in the New Zealand economy to weigh on revenue collection and put downward pressure on the country's fiscal surplus. We forecast revenue growth to come in at 5.0% in FY2018/19 and 4.5% in FY2019/20, compared to the Treasury's latest forecasts of 5.7% and 5.5% respectively. Our forecasts are slightly lower than the Treasury's estimates given our slightly less sanguine view of the economy. We forecast real GDP growth to come in at 2.6% in 2019 and 2.3% in 2020, compared to the Treasury's more bullish forecasts of 3.0% and 3.2% respectively.

We expect growth to slow due to continued weak business and consumer confidence sentiment, which will weigh on investment and private consumption growth (see 'Reserve Bank Of New Zealand To Remain On Hold', November 8). Business confidence in New Zealand remains on a downward trend, with a figure of -37.1 in November 2018, down from 24.8 in June 2017, which will likely weigh on investment. Continued weakness will likely have a direct effect on corporate tax revenue, which makes up 14.8% of the country's revenue.

Additionally, consumer confidence has also declined to 115.4 in October from a peak of 128.0 in March, suggesting the potential for lower consumer spending over the short term, especially as New Zealand's household debt remains high at slightly more than 120% of GDP. The slowdown in consumer spending could also weigh on GST collection, which makes up 24.3% of total revenue.

2019 Budget Will Be Expansionary

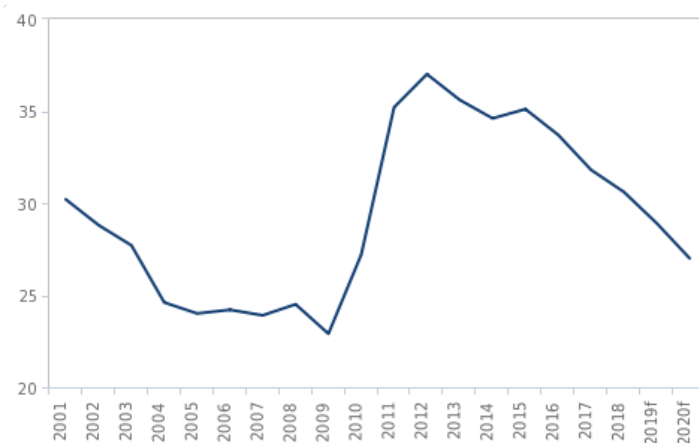
In addition to slowing revenue growth, we expect an increase in public spending to weigh on the country's fiscal surplus in 2019. In December, the government announced the key priorities of its 2019 Budget in its Budget Policy Statement. Although the final budget figures will only be released in May 2019, the statement was notable for flagging the country's first-ever Wellbeing Budget, which emphasises environmental sustainability, productivity, and supporting the mental wellbeing of New Zealanders.

The five key planks of the Wellbeing Budget are: 1) Creating opportunities for productive businesses for a sustainable and low-emissions economy; 2) supporting a thriving nation in the digital age through innovation, and social and economic opportunities; 3) lifting Māori and Pacific incomes, skills and opportunities; 4) reducing child poverty and improving child wellbeing, including addressing family violence; and 5) supporting the mental wellbeing of all New Zealanders, with a special focus on under 24-year-olds. Looking ahead, we expect the areas of social security & welfare, and healthcare to remain the largest components of government expenditure, accounting for 29.0% and 16.1%, respectively, of the 2018 total. In particular, we forecast the share of the pensionable population (those aged 65 and above) to rise to 20.0% over the next decade from 15.6% in 2018.

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Still Room To Support Growth If Needed

New Zealand - Total Gross Debt, % Of GDP



f = Fitch Solutions forecast. Source: New Zealand Treasury, Fitch Solutions

Despite the narrowing fiscal surplus, we expect New Zealand's government debt levels to remain healthy as it is one of the least indebted countries among OECD economies, with total gross debt of 30.6% in 2018, comfortably below the OECD average of 73%, and on a declining trend. As such, there is ample buffer for policymakers to enact expansionary fiscal policy to support the economy should growth decelerate significantly.

MACROECONOMIC FORECASTS (NEW ZEALAND 2015-2021)

Indicator	2015	2016e	2017e	2018e	2019f	2020f	2021f
Population, mn	4.61	4.66	4.71	4.75	4.79	4.83	4.88
Nominal GDP, USDbn	175.1	185.2	201.4	206.9	210.0	206.9	217.3
GDP per capita, USD	37,940	39,731	42,801	43,566	43,812	42,803	44,571
Real GDP growth, % y-o-y	4.0	4.2	2.6	2.9	2.6	2.3	2.4
Consumer price inflation, % y-o-y, ave	0.3	0.6	1.9	1.6	2.0	2.3	2.5
Consumer price inflation, % y-o-y, eop	0.1	1.3	1.6	1.3	2.0	2.5	2.5
Central bank policy rate, % eop	2.50	1.75	1.75	1.75	1.75	1.75	2.00
Exchange rate NZD/USD, ave	1.43	1.44	1.41	1.43	1.47	1.56	1.56
Exchange rate NZD/USD, eop	1.46	1.44	1.41	1.54	1.59	1.54	1.59
Budget balance, NZDbn	0.7	2.3	4.4	6.0	2.4	3.5	4.3
Budget balance, % of GDP	0.3	0.9	1.6	2.0	0.8	1.1	1.3
Goods and services exports, USDbn	48.7	48.6	54.4	58.4	60.2	59.9	63.4
Goods and services imports, USDbn	47.6	47.4	52.7	57.5	58.4	57.5	60.1
Current account balance, USDbn	-5.4	-4.0	-5.3	-6.1	-5.2	-4.2	-3.5
Current account balance, % of GDP	-3.1	-2.2	-2.6	-3.0	-2.5	-2.0	-1.6
Foreign reserves ex gold, USDbn	14.7	17.8	20.0	22.5	25.4	28.5	32.1
Import cover, months	3.7	4.5	4.6	4.7	5.2	6.0	6.4
Total external debt stock, USDbn	142.1	153.7	163.6	171.8	177.2	176.5	186.2
Total external debt stock, % of GDP	81.2	83.0	81.2	83.0	84.4	85.3	85.7
Crude, NGPL & other liquids prod, 000b/d	48.0	41.0	38.0	30.1	27.6	25.4	23.3
Total net oil exports (crude & products), 000b/d	-108.8	-122.0	-134.0	-141.9	-147.9	-152.8	-156.7
Dry natural gas production, bcm	4.6	5.1	5.2	4.7	4.3	4.1	3.9
Dry natural gas consumption, bcm	4.6	5.1	5.2	4.7	4.3	4.1	3.9

e/f = Fitch Solutions estimate/forecast; Source: National Sources, Fitch Solutions