NEW ZEALAND

Economic growth is projected to edge down to 2.6% by 2020, mainly reflecting slowing private consumption as the boost from increased financial support for families passes, net immigration diminishes and housing wealth gains subside. Export growth is also set to decline once the current rebound from a dry spell is over. Inflation is projected to increase to slightly over 2% in 2019 and 2020, buoyed by higher import prices and domestic wage growth.

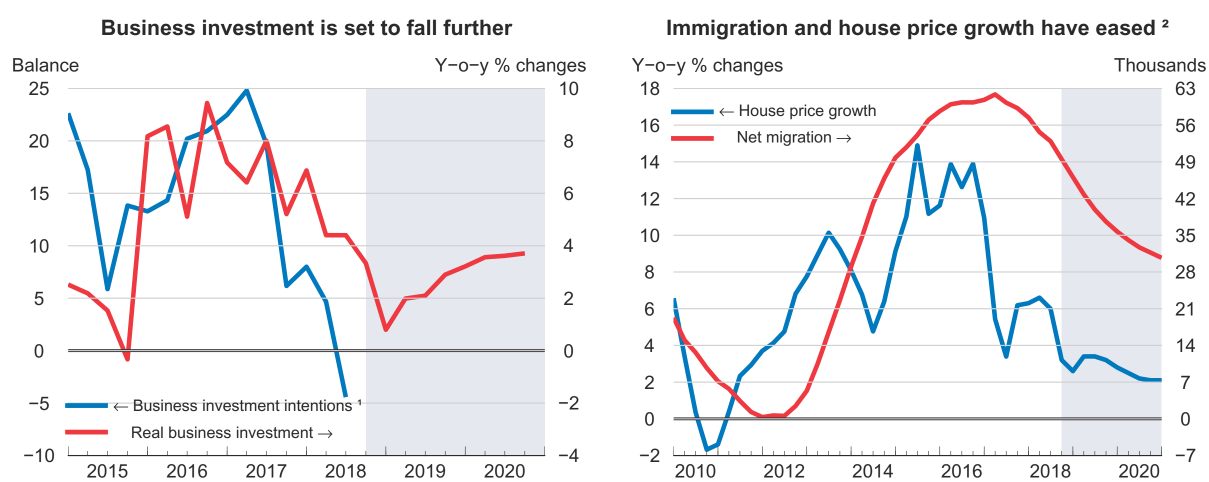
Monetary policy is projected to tighten gradually from late 2019. Fiscal policy is also projected to tighten somewhat, which is appropriate for the advanced stage of the business cycle. Better targeting of some recent government initiatives would support the achievement of social goals.

Economic growth remains solid

Economic growth has been solid over the past year, with second quarter growth supported by a rebound in agricultural and related exports following drought in parts of the country in late 2017. Business investment has held up despite business confidence reaching its lowest level since 2009, but has begun to show signs of weakness. Low business confidence reflects concerns about government policy, the cost and availability of labour, and tight profit margins.

The labour market is tight, with unemployment reaching a ten-year low. However, wage growth is moderate. Inflation has increased to just under the 2% mid-point of the target range, pushed higher by petrol excise duty hikes and rising import prices following exchange rate depreciation and oil price rises. Core inflation is somewhat lower, reflecting the importance of transitory factors. House prices have been flat in Auckland over the past 18 months, but have continued to grow elsewhere.

New Zealand



1. Percentage of firms expecting to increase investment in property, plant and equipment in a year's time less percentage expecting to decrease investment.
2. RBNZ projections. Net migration data are for the working-age population.

Source: ANZ Bank, Business Outlook Survey; OECD Economic Outlook 104 database; and Reserve Bank of New Zealand (2018), Monetary Policy Statement, November.

StatLink http://dx.doi.org/10.1787/888933877088

New Zealand: **Demand, output and prices**

	2015	2016	2017	2018	2019	2020
	Current prices NZD billion	Percentage changes, volume (2009/2010 prices)				
GDP at market prices	251.4	4.1	2.7	2.9	2.8	2.6
Private consumption	144.8	4.8	4.4	2.9	2.9	2.4
Government consumption	46.5	1.6	4.5	4.2	2.2	1.7
Gross fixed capital formation	57.5	6.4	3.4	3.8	2.8	3.8
Final domestic demand	248.7	4.6	4.2	3.4	2.7	2.6
Stockbuilding[1]	0.6	0.0	-0.1	0.5	-0.1	0.0
Total domestic demand	249.4	4.6	4.1	3.9	2.6	2.6
Exports of goods and services	70.3	2.1	1.8	4.2	4.2	3.3
Imports of goods and services	68.3	3.4	7.0	7.4	3.4	3.2
Net exports[1]	2.0	-0.3	-1.3	-0.8	0.2	0.0
Memorandum items						
GDP deflator	_	1.8	3.4	1.1	2.0	2.1
Consumer price index	_	0.6	1.9	1.7	2.3	2.2
Core inflation index[2]	_	1.3	1.4	1.2	2.2	2.2
Unemployment rate (% of labour force)	_	5.1	4.7	4.2	4.1	4.2
Household saving ratio, net (% of disposable income)	_	-2.8	-3.3	-1.6	-1.4	-1.2
General government financial balance (% of GDP)	_	1.2	0.9	0.0	0.0	0.4
General government gross debt (% of GDP)	_	37.6	36.0	36.0	36.0	35.6
Current account balance (% of GDP)	_	-2.2	-2.9	-3.6	-3.1	-2.9

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 104 database.

StatLink http://dx.doi.org/10.1787/888933878019

Fiscal and monetary policy settings will become less supportive

Fiscal policy is currently expansionary, driven by higher spending. Additional spending does not threaten fiscal sustainability as government debt continues to decline as a share of GDP. However, some of the new expenditure has been poorly targeted. For example, Winter Energy Payments are not means tested for those aged 65 and over, free tertiary education favours more advantaged socio-economic groups and KiwiBuild delivers the greatest benefits to people who can afford to buy a house. Slower spending growth will yield a mildly contractionary fiscal stance by 2020.

The central bank is projected to raise its policy interest rate in late 2019 and 2020 in order to contain inflation. Higher interest rates will place additional pressure on housing affordability as rapid house price growth since 2011 has pushed up household debt considerably. House price increases have been moderated by government decisions to ban foreign purchases of existing housing, enhance heating and insulation standards for rental properties, and extend taxation of gains on sales of investment properties. If implemented, proposals to tax capital gains on investment properties more generally, ring-fence rental losses and provide greater certainty of tenure would further restrain price increases. Residential investment will be supported from mid-2019 by the KiwiBuild programme, although not all of this activity is assumed to be additional as constraints remain around planning, infrastructure provision and construction industry capacity.

Growth is projected to ease

Tighter monetary and fiscal stances, as well as weaker private consumption, will lead to slower economic growth in 2020, notwithstanding some offset from rising residential and business investment. Wage growth will be supported by gender pay equity decisions, public sector wage increases and plans to increase the minimum wage by 21% by 2021. Consumption growth would be higher if net migration declines less than assumed, particularly if this triggered a resumption of wealth gains through house price growth in Auckland. Risks from high household debt associated with high house prices have eased with improvements in lending standards, but remain the most important domestic risk. There are also downside risks for business investment if business confidence recovers more slowly than anticipated.