

New Zealand Business Forecast Report Q1 2015

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Abstracts

Core Views

The free trade agreement (FTA) between New Zealand and South Korea is set to be ratified by Q115, subject to parliamentary approval, and will provide significant benefits to New Zealand's meat and dairy exports. Additionally, reduced import tariffs on consumer goods should support real incomes, helping to offset the impact of weakening terms of trade and a depreciating currency.

We are beginning to see signs of a slight slowdown in the New Zealand economy. The crucial agricultural sector is cooling, while the services and construction sectors are currently the only drivers of growth, leaving the economy susceptible to weakness in the New Zealand dollar and the property market.

Our contrarian view of a no further interest rate hikes by the Reserve Bank of New Zealand (RBNZ) until 2016 is gaining credence as consensus expectations continue to gradually decline while interest rate markets price out aggressive hikes. As real GDP growth weakens, and macro-prudential housing measures remain in place, inflationary pressures will remain benign.

The New Zealand government is set to run a small fiscal deficit in Fiscal Year 2014/15, but the overall trends of narrower deficits and falling spending relative to GDP remain in place. We forecast a deficit equivalent to 0.2% of GDP in FY2014/15, before flipping to a surplus of 0.3% of GDP in FY2015/16.

We forecast the NZD to average USD0.7400/NZD in 2015 and USD0.7000/NZD in 2016. The recent low of USD0.7700/NZD is a key technical support level, and a break below this would suggest a move down to USD0.7000/NZD and possibly below. Fundamentally, the Reserve Bank of New Zealand continues to talk down the currency,

and widespread expectations of interest rate hikes are gradually being unwound, which will act as headwinds to the currency.

Major Forecast Changes

We have not made any significant revisions since our previous Business Forecast Report. We continue to see real GDP growth slowing in 2015 to 2.4% from an estimated 3.2% from 2014. We also expect the government to fail to achieve a fiscal surplus until Fiscal Year 2015/16. We also remain bearish on the New Zealand dollar, which, will continue to be undermined by weak commodity prices and a falling interest rate expectations.

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Stability To Prevail, But Not Without Challenges

New Zealand is likely to remain one of the most stable states in the world over the coming decade. The government's main challenges are to rein in the budget deficit, improve the business environment to attract greater foreign investment and raise opportunities for the indigenous Maori population. In the realm of foreign policy, New Zealand is likely to continue relying on Australia as its guardian. A key wild card is whether New Zealand deepens political ties with its neighbour, possibly in the form of a confederation.

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We are beginning to see signs of a slight slowdown in the New Zealand economy. The crucial agricultural sector is cooling, while the services and construction sectors are currently the only drivers of growth, leaving the economy susceptible to weakness in the New Zealand dollar and the property market.

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The New Zealand government is set to run a small fiscal deficit in Fiscal Year 2014/15, but the overall trends of narrower deficits and falling spending relative to GDP remain in place. We forecast a deficit equivalent to 0.2% of GDP in FY2014/15, before flipping to a surplus of 0.3% of GDP in FY2015/16.

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Fundamentally, the Reserve Bank of New Zealand continues to talk down the currency, and widespread expectations of interest rate hikes are gradually being unwound, which will act as headwinds to the currency.

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Population growth will slow, terms of trade support will be hard to come by, and we expect New Zealand households will eventually experience protracted deleveraging cycle. These factors should see real GDP growth average 2.5% over the 2014-2023 period, below the 3.6% growth rate seen over the 1999-2007 boom years.

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