INTERNATIONAL MONETARY FUND

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NEW ZEALAND

May 2022

2022 ARTICLE IV CONSULTATION—PRESS RELEASE; AND STAFF REPORT

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2022 Article IV consultation with New Zealand, the following documents have been released and are included in this package:

- A **Press Release**
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse-of-time basis, following discussions that ended on March 23, 2022, with the officials of New Zealand on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 29, 2022.
- An **Informational Annex** prepared by the IMF staff.

The documents listed below has been separately released.

Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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International Monetary Fund
Washington, D.C.

IMF Executive Board Concludes 2022 Article IV Consultation with New Zealand

FOR IMMEDIATE RELEASE

Washington, DC – **May 13, 2022:** The Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with New Zealand on May 13, 2022 and endorsed the staff appraisal without a meeting on a lapse-of-time basis.[2]

New Zealand has reached a strong cyclical position as a result of successful management of the pandemic and significant policy support. Strong public health policies and border controls helped contain the COVID-19 waves in 2020 and 2021, and high vaccination rates have allowed a shift to a living-with-COVID strategy during the current Omicron wave. The economy rebounded strongly in 2021, growing 5.6 percent, aided by significant fiscal support and accommodative monetary policy. As a result, the labor market tightened significantly, with historically low unemployment and rising wage pressures in the face of labor shortages, exacerbated by border closures. Inflation has risen significantly above the Reserve Bank of New Zealand's (RBNZ) target range, driven by higher food and energy costs, supply chain disruptions, surging house prices, and rising wages. Record low mortgage rates, easy credit availability, and COVID-related pent-up demand in the face of inelastic supply, boosted house prices significantly, which in turn has rapidly reduced housing affordability.

Economic growth is set to slow to about 2.7 percent in 2022, reflecting withdrawal of COVID-19 related policy support, the global economic slowdown, and temporary setbacks from the ongoing COVID wave. The housing market has turned, and house prices are expected to continue slowing as interest rates increase, credit conditions tighten, and supply improves. The unemployment rate will likely remain very low given labor shortages, with a further pickup expected in wage growth. High commodity prices due to the war in Ukraine, persistent supply chain disruptions, and New Zealand's tight labor market will likely contribute to inflation staying above the RBNZ's target range in 2022-23.

Downside risks dominate in the near and medium term. Near-term risks to the outlook include further outbreaks of COVID-19 variants and an intensification of geopolitical tensions, which could adversely affect economic activity, add to global supply chain disruptions, and push inflation higher. Slower-than-expected growth in China is a risk to New Zealand given strong trading links. The housing market also constitutes a risk in view of borrowers' vulnerability to rising mortgage rates, high household debt, and banks' exposure to housing.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

Executive Board Assessment

In concluding the 2022 Article IV consultation with New Zealand, Executive Directors endorsed the staff's appraisal, as follows:

New Zealand managed the transition to living with COVID well. Strong health and economic policies supported quick recovery from lockdowns in 2021. Following a slow start, swift progress in the vaccination campaign has offered a pathway to a new normal. The expected border reopening will provide an additional economic boost to the tourism and education sectors. Still, economic growth is expected to moderate this year, reflecting policy tightening, global spillovers, and the ongoing Omicron wave. Amid commodity price pressures related to the war in Ukraine, continued supply chain disruptions, and a tight labor market, inflation is expected to remain high and stay well above the RBNZ's target range this year. Overall, the outlook remains highly uncertain, contingent on the trajectory of the pandemic and geopolitical developments.

The path of macroeconomic policy normalization needs to be calibrated to evolving economic conditions. With output above potential and stronger-than-expected inflation, the authorities are appropriately withdrawing fiscal and monetary support. Under baseline expectations for growth and inflation, the pace of planned policy support withdrawal is adequate. That said, the pace should be adjusted nimbly in case upside or downside risks materialize.

Fiscal policy should remain agile amid continued uncertainty. While the scheduled tightening of fiscal policy is appropriate, the authorities should calibrate the fiscal stance on the evolution of the pandemic and economic conditions, providing additional, targeted support where needed in case of renewed, COVID-related disruptions. Fiscal policy should also focus on promoting long-term growth while addressing emerging structural issues. As uncertainty related to the pandemic recedes, the authorities should update their fiscal targets, which were suspended during the pandemic, to provide an anchor for fiscal policy and manage long-term spending pressures.

Monetary policy should remain data dependent, and continued, swift policy normalization will be appropriate under baseline conditions. Given New Zealand's cyclical position, continued, significant increases in the OCR in the near term would signal the RBNZ's commitment to addressing inflation. In the event downside risks to growth materialize, more gradual tightening, coupled with a pause in reducing the RBNZ's balance sheet, can be considered, but elevated inflation suggests that room for additional monetary stimulus is limited.

Raising bank capital requirements and enlarging the MPM toolkit will help the system weather future shocks. Higher bank capital requirements will help insulate the banking system from future shocks, though the impact on lending rates should be monitored. The DTB is a step forward in adopting international good practices to strengthen financial regulation and supervision and enhance depositor protection, and opportunities for further strengthening the proposed law should be seized, including by addressing remaining FSAP recommendations.

Continued focus is needed on addressing housing imbalances. The macroprudential measures implemented last year should be maintained, and work to expand the macroprudential toolkit is appropriate. Increasing the stock of social housing remains important in the near term as a durable solution to housing affordability is achieved over time by addressing supply constraints.

The external position is broadly consistent with economic fundamentals and desired policy settings. The assessment is subject to large uncertainty and assumes that the extraordinary impact of COVID-19 on the tourism and transportation sectors is temporary.

Stronger efforts are needed to meet GHG emissions goals. The recent rise in carbon prices is welcome, and the forthcoming Emissions Reduction Plan is an opportunity to further strengthen the price-based mechanism and lay out complementary policies. The planned introduction of prices on agricultural emissions will be important to include the largest emissions source in New Zealand's climate mitigation efforts, incentivizing the adoption of new technologies and methods to lower emissions. Proceeds of higher carbon prices should be used to invest in emissions reduction and to compensate those adversely affected by carbon price increases, particularly vulnerable groups.

Structural policies should promote durable and inclusive growth. The authorities should promote innovation and digitalization, and tax reforms would support long-term growth. Infrastructure spending should aim at reducing the infrastructure gap and supporting the transition to a net zero carbon growth path. Unemployment insurance should be calibrated carefully to address trade-offs between insurance and disincentives, and minimum wage increases should be aligned with underlying labor productivity growth.

Table 1. Main Economic Indicators, 2017-2027
(Annual percent change, unless otherwise indicated)

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
						Projections					
NATIONAL ACCOUNTS											
Real GDP (production)	3.5	3.4	2.9	-2.1	5.6	2.7	2.6	1.9	1.7	2.4	2.3
Real GDP (expenditure)	4.0	4.3	3.3	-0.9	5.0	1.9	2.6	1.9	1.6	2.4	2.2
Domestic demand	5.2	5.2	3.2	-1.9	9.6	3.8	1.3	2.4	2.3	2.0	2.1
Private consumption	5.5	4.6	3.2	-1.2	6.6	2.6	2.6	3.7	2.7	2.4	2.4
Public consumption	3.5	3.3	5.1	6.8	10.4	7.9	-1.4	-0.2	1.3	0.4	0.2
Investment	5.5	8.0	2.4	-10.1	16.6	0.7	0.5	1.5	2.1	2.4	2.9
Public	7.4	2.2	2.0	-6.8	6.9	-0.9	0.6	3.0	4.4	4.7	4.8
Private	3.8	8.0	5.1	-7.2	10.6	5.7	0.5	1.1	1.5	1.7	2.3
Private business	6.5	13.0	5.0	-8.9	10.5	6.6	0.1	1.3	1.3	1.5	3.1
Dwelling	-1.1	-1.6	5.4	-3.3	11.0	4.1	1.2	0.7	1.8	2.2	0.7
Inventories (contribution to growth, percent)	0.2	0.3	-0.5	-0.8	1.6	-1.0	0.0	0.0	0.0	0.0	0.0
Net exports (contribution to growth, percent)	-1.6	-1.2	0.0	1.7	-5.1	-2.3	1.1	-0.7	-0.9	0.2	-0.1
Real gross domestic income	5.4	3.7	3.3	-0.6	4.2	4.4	2.4	3.9	2.4	1.9	2.0
Investment (percent of GDP)	23.3	24.3	24.1	21.7	24.5	24.4	24.0	23.4	23.4	23.3	23.2
Public	5.5	5.4	5.3	5.0	5.1	5.0	4.9	4.9	5.0	5.0	5.1
Private	17.9	18.9	18.8	16.7	19.5	19.4	19.1	18.6	18.4	18.2	18.1
Savings (gross, percent of GDP)	20.5	20.3	21.2	20.8	18.7	17.9	18.6	19.2	19.2	19.1	18.9
Public	1.3	1.3	-2.5	-4.0	-4.9	-4.9	-1.8	-1.2	-0.4	0.1	0.1
Private	19.2	19.0	23.6	24.9	23.7	22.8	20.4	20.4	19.6	19.0	18.8
Potential output	3.0	3.0	3.1	1.6	1.5	1.9	2.5	2.5	2.5	2.5	2.5
Output gap (percent of potential)	0.5	0.9	0.7	-3.0	0.9	1.7	1.9	1.3	0.4	0.3	0.0
LABOR MARKET											
Employment	4.2	2.9	1.3	1.3	2.4	1.7	1.0	1.4	1.2	1.2	1.3
Unemployment (percent of labor force, ann.	4.7	4.3	4.2	4.6	3.8	3.6	3.9	3.9	4.1	4.3	4.4
Wages (nominal percent change)	2.6	3.0	3.4	3.8	3.8	4.9	4.6	3.7	3.5	3.7	3.3
PRICES											
Terms of trade index (goods and services, %	5.0	-1.4	0.1	1.2	-1.2	8.3	-2.0	5.2	1.2	-2.1	-1.6
Terms of trade index (goods, % change)	7.3	-1.8	0.4	2.3	1.7	9.1	-3.3	2.5	-1.4	-4.5	-5.1
Consumer prices (avg, % change)	1.9	1.6	1.6	1.7	3.9	5.9	3.5	2.4	2.2	2.1	2.0
GDP deflator (avg, % change)	3.3	1.3	2.4	2.2	2.9	5.7	4.1	3.4	3.0	2.8	2.5
MACRO-FINANCIAL											
Official cash rate (policy rate, percent, avg)	1.8	1.8	1.4	0.4	0.4	1.7	3.3	3.5	3.0	2.5	2.5
Credit to the private sector (percent change)	4.9	5.4	5.6	3.9	6.1	2.7	1.1	4.0	4.5	4.2	4.1
Interest payments (percent of disposable	7.7	7.5	7.1	6.2	6.0	8.2	8.3	8.3	8.1	7.8	7.7
Household savings (percent of disposable	3.3	3.2	3.4	3.6	3.6	3.2	2.7	2.5	2.4	2.3	2.3
Household debt (percent of disposable income)	159	158	159	164	169	160	152	151	150	148	147
GENERAL GOVERNMENT (percent of GDP)											
Revenue	37.4	36.8	37.8	36.1	37.7	37.1	37.3	37.4	37.3	37.4	37.4
Expenditure	36.1	35.5	36.6	42.2	39.6	44.9	39.5	38.8	38.2	37.4	37.3
Net lending/borrowing	1.3	1.3	1.2	-6.1	-1.9	-7.7	-2.2	-1.4	-0.9	0.0	0.1
Operating balance	2.9	3.2	3.2	-4.3	-0.3	-5.1	0.6	1.7	1.9	2.3	2.4
Cyclically adjusted balance 2/	1.3	1.0	0.9	-4.8	-2.4	-7.5	-2.2	-1.8	-0.2	0.1	0.6
Gross debt	32.5	30.0	26.2	38.4	45.9	51.5	51.3	51.9	49.3	47.7	45.0
Net debt	6.0	5.2	4.3	9.6	10.4	19.2	20.8	22.1	20.3	19.3	16.8
Net worth	88.2	91.4	93.2	83.6	92.0	80.5	77.3	77.0	76.8	78.4	80.3
BALANCE OF PAYMENTS											
Current account (percent of GDP)	-2.8	-4.0	-2.9	-0.8	-5.8	-6.5	-5.3	-4.2	-4.2	-4.2	-4.3
Export volume	2.7	3.2	2.4	-12.9	-2.5	7.3	9.1	6.4	6.0	5.7	5.7
Import volume	7.3	6.4	2.1	-15.9	15.4	12.6	3.1	6.8	6.8	3.7	4.4
Net international investment position (percent	-52.3	-56.2	-53.6	-55.6	-46.1	-49.2	-51.4	-53.0	-54.9	-56.3	-58.1
Gross official reserves (bn US$)	20.3	17.6	17.0	13.0	…	…	…	…	…	…	…
MEMORANDUM ITEMS											
Nominal GDP (bn NZ$)	286	303	320	324	350	377	403	425	444	468	490
Percent change	7.4	5.7	5.8	1.3	8.0	7.8	6.8	5.4	4.7	5.3	4.8
Nominal GDP per capita (US$)	42,271	42,767	42,321	41,418	48,413	49,835	52,957	54,996	56,324	58,227	60,042
Real gross national disposable income per	51,235	52,213	53,601	52,710	54,387	55,769	56,572	57,879	58,463	58,813	59,135
Percent change	2.3	1.9	2.7	-1.7	3.2	2.5	1.4	2.3	1.0	0.6	0.5
Population (million)	4.8	4.9	5.0	5.1	5.1	5.2	5.2	5.3	5.4	5.4	5.5
US$/NZ$ (average level)	0.711	0.693	0.659	0.650	…	…	…	…	…	…	…
Nominal effective exchange rate	111.1	106.8	105.2	103.8	…	…	…	…	…	…	…
Real effective exchange rate	107.4	102.9	101.4	100.6	…	…	…	…	…	…	…

Sources: Authorities' data and IMF staff estimates and projections.
1/ Fiscal year.
2/ In percent of potential GDP.

INTERNATIONAL MONETARY FUND

NEW ZEALAND

STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION

April 28, 2022

KEY ISSUES

Context. New Zealand's management of the pandemic, including health policy and macroeconomic policy support, has been effective in ensuring economic recovery. Output has already recovered to above potential, the labor market is tight, and inflation has risen to above the Reserve Bank of New Zealand's (RBNZ) target range.

Outlook and risks. Economic growth is expected to moderate to 2.7 percent in 2022 on policy tightening and near-term uncertainty with respect to the ongoing Omicron outbreak and high and volatile commodity prices in the wake of the war in Ukraine. Inflation is expected to remain high and revert to its target range only after 2023. Given the unpredictable trajectory of the pandemic and the global environment, risks are tilted to the downside.

Policy recommendations

- **Macroeconomic policies**. The normalization of macroeconomic policies has started as fiscal COVID-19 support measures have been scaled down and monetary policy stimulus is being withdrawn to address inflation. Policy tightening should continue, with the pace calibrated to evolving economic conditions.

- **Financial sector policies**. Macroprudential measures (MPMs) introduced to preserve financial stability amid rapid house price growth are showing effect. Ongoing work to enlarge the MPM toolkit is welcome and will provide additional policy options that can be deployed to safeguard financial stability, if needed. The planned increase in bank capital requirements will help further insulate the banking system from future shocks.

- **Structural policies.** Priorities include improving the economy's productivity performance and promoting inclusiveness and sustainability. To achieve greenhouse gas emissions targets, it will be critical to strengthen the price-based mechanism by allowing carbon prices to rise further and pricing agricultural emissions. While the housing market has begun to turn, housing affordability remains a concern, requiring continued focus on boosting supply and expanding social housing.

Approved By
Krishna Srinivasan (APD) and Kristina Kostial (SPR)

Virtual discussions took place during March 7-23, 2022. The mission team comprised: Harald Finger (head), Pragyan Deb, Yosuke Kido, Evan Papageorgiou, and Narayanan Raman (all APD). Oscar Parkyn (OED) joined the discussions. Mr. Srinivasan joined selected meetings. Ioana Hussiada and Nadine Dubost assisted in the preparation of this report.

CONTENTS

ANNEXES

STRONG RECOVERY MEETS RISING UNCERTAINTY

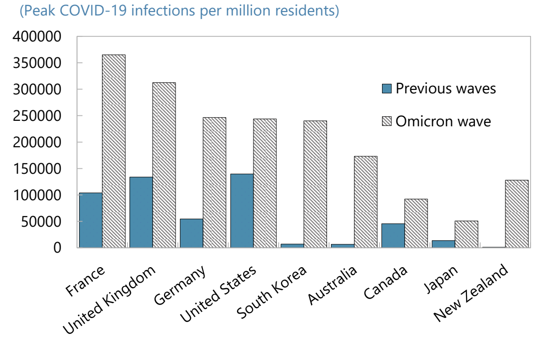
A. Context and Recent Developments

1. New Zealand's management of the COVID-19 crisis has been successful. Strong public health policies and tight border controls allowed for effective containment of two infection waves in 2020 and 2021, enabling quick economic recovery following strict lockdowns. After a slow start, New Zealand managed to achieve very high vaccination rates, prompting a strategic shift towards risk-based mitigation and a living-with-COVID strategy. The Omicron wave led to a steep increase in infections in early 2022, but cases have fallen significantly from their peak in early March. A gradual border reopening is underway (Annex I).

2. The economy rebounded strongly in 2021. The growth impact of the strict lockdowns in 2021 was much less than that in 2020. The economy grew 5.6 percent in 2021, as firms and households adapted to live with the pandemic, and the recovery was faster than in most advanced economies (AEs). The output gap has already turned positive, despite international tourism still impaired by border restrictions.

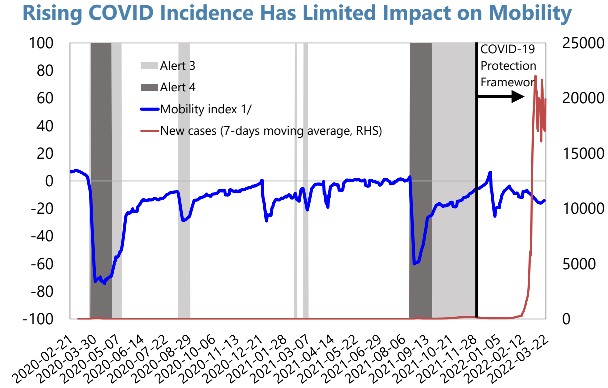
Despite Omicron Surge, COVID Remains Manageable

(Peak COVID-19 infections per million residents)



Source: JHU COVID Database.
Note: Peak calculated using average number of new infections over a 7-day period during COVID waves.

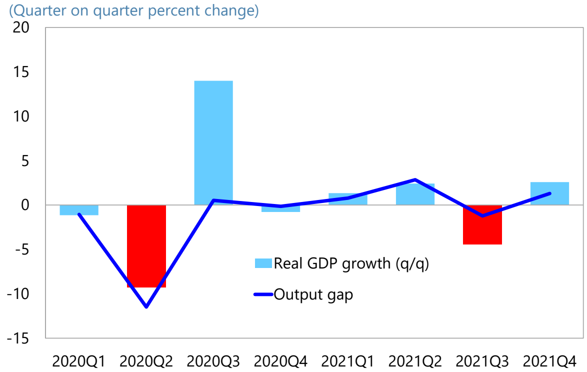
Rising COVID Incidence Has Limited Impact on Mobility



Source: Our World in Data, Google.
1/ Simple average of retail, grocery, transport, and workplace.

Growth Impact of Renewed Lockdown Was Smaller

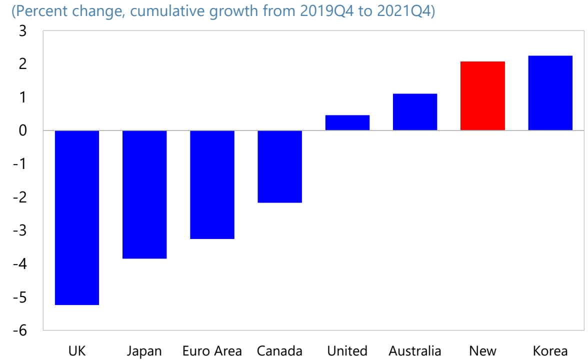
(Quarter on quarter percent change)



Sources: Stats NZ and IMF staff calculations.

Faster Recovery From COVID Shock

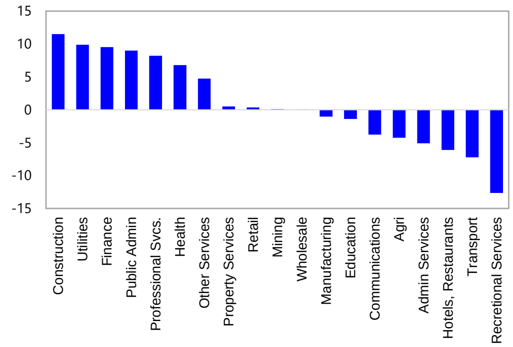
(Percent change, cumulative growth from 2019Q4 to 2021Q4)



Source: IMF World Economic Outlook.

3. The labor market tightened as the economy rebounded, and inflation has risen. Despite heterogeneity across sectors, the unemployment rate fell to historically low levels (3.2 percent at end-2021 relative to an estimated NAIRU of 4.5 percent), putting upward pressure on wages (3.8 percent y/y at end-2021). A spike in food and fuel costs, supply chain disruptions, rising house prices, higher wages, and the positive output gap pushed inflation to 6.9 percent in 2022Q1, significantly above the 1-3 percent target (Annex II).

Uneven Sectoral Distribution of Employment
(Jan. 2022, percent change from pre-COVID)

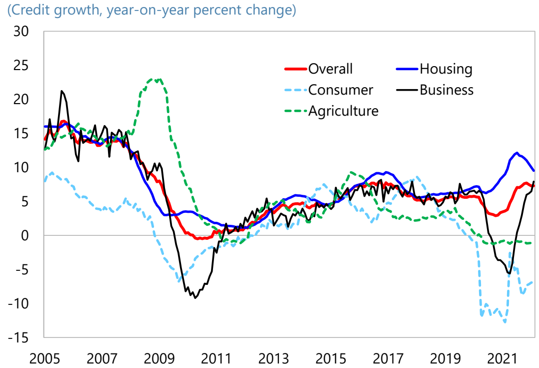


Sources: Stats NZ and IMF staff calculations.

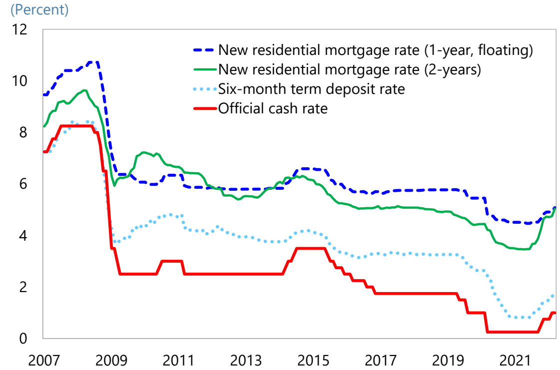
4. The external position in 2021 was broadly in line with fundamentals and desired policy settings. The economic rebound increased the current account deficit to 5.8 percent of GDP in 2021. Imports surged while exports remained subdued, partly due to unfavorable weather conditions. The Fund's external balance assessment does not point to significant currency misalignment (Annex III), although the assessment is subject to exceptionally high uncertainty given the pandemic. Gross reserves increased to US$16 billion, largely on account of the SDR allocation that supplemented reserve assets. New Zealand's external liabilities are either denominated in New Zealand dollars or almost fully hedged, limiting balance sheet risks from exchange rate movements.

5. The banking system has remained resilient. Banks report strong capitalization, ample liquidity, and a rapid improvement in profitability. Credit growth has recovered since 2020, despite weak loan activity in agricultural and consumer sectors. Housing credit growth has slowed significantly due to rising mortgage rates, removal of tax incentives for investors, and tighter macroprudential settings. Lending to businesses has recovered strongly, in line with strong private investment. After relying on the RBNZ's liquidity support through a large part of 2020, banks are returning to the domestic funding market. RBNZ stress tests suggest that systemic risks are contained, as banks can meet minimum capital standards in the event of a 1-in-50 to 1-in-75-year shock, including a 39 percent decline in house prices.

Growth in Mortgages Peaked in July 2021
(Credit growth, year-on-year percent change)



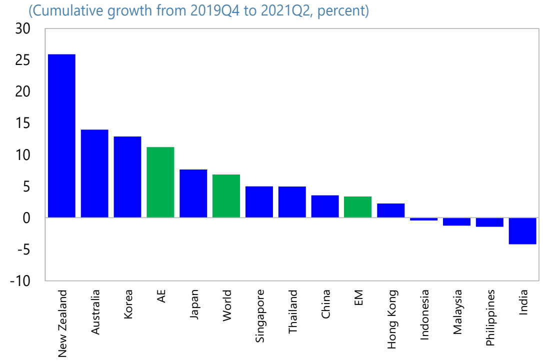
Retail Interest Rates Trending Upward
(Percent)



Source: RBNZ.

6. House prices continued to surge in 2021, amplifying affordability concerns, though the market is now turning. House prices increased 24 percent y/y in December 2021, driven by record low mortgage rates, credit availability, COVID-related pent-up demand, and lagged effects of population growth. This resulted in rapidly declining affordability, with the average property valued at 7.9 times the average annual household income (2021Q2), significantly above its long-term average. The average debt-to-income (DTI) ratio and average mortgage payments as a proportion of household income have also increased rapidly, mirroring the increase in household debt from 169 percent of disposable income at end-2019 to 174 percent in December 2021. There are recent signs of a market slowdown: sales volumes and new mortgages are declining, while prices have begun to drop mildly from their peak.

Real House Price Growth After COVID
(Cumulative growth from 2019Q4 to 2021Q2, percent)



Source: Bank for International Settlement.

B. Outlook and Risks

7. Economic growth is expected to moderate, reflecting policy tightening, global spillovers, and the ongoing COVID wave. Lost hours worked due to the Omicron wave are weighing on growth in the near term, while the weakening global economy will affect exports. The withdrawal of policy support and the slowdown in the housing market are also contributing to a moderation of economic growth to 2.7 percent in 2022. While the growth impact of higher prices of imported energy is offset by higher commodity export prices, particularly for food items, higher food and energy prices related to the war in Ukraine are putting upward pressure on inflation. Considering also continued supply chain disruptions and a tight labor market, inflation is expected to remain high and to stay well above the RBNZ's target range this year.

8. Downside risks dominate (Annex IV). The most immediate risks are further domestic or global outbreaks of COVID-19 variants and further intensification of geopolitical tensions, which could adversely affect economic activity and inflation through weaker external demand, higher commodity prices, and extended global supply chain disruptions. Slower growth in China could have a significant impact on New Zealand given China's importance as a trading partner. Domestic risks are centered around financial stability and growth implications of housing market developments due to high household debt,[1] borrowers' vulnerability to rising interest rates,[2] and banks' high exposure to housing (¶34). De-anchoring of inflation expectations and natural disasters are additional sources of risk.

[1] Household debt to net wealth has remained relatively contained (10.7 percent in September 2021) as higher house prices have offset the increase in debt. A correction in prices would likely leave household balance sheets relatively healthy, though with smaller buffers, and could have an effect on household consumption.

[2] Higher mortgage rates could have a significant impact: the 1 percentage point increase in mortgage rates since June 2021 has increased average interest payments by 1.6 percentage points of household disposable income, which is set to rise to around 2.4 percentage points by June 2022 (see the accompanying Selected Issues Paper).

C. Authorities' Views

9. The authorities agreed with staff's assessment and emphasized that the outlook remains highly uncertain. A slowdown is expected, and longer-term spillovers from geopolitical realignment were seen as a notable risk. Since the Omicron variant is the first full-blown COVID-19 wave in New Zealand, the impact on consumer and business confidence has been pronounced, though the authorities felt that confidence may bounce back quickly as Omicron recedes. They also pointed to tailwinds from an improvement in the terms of trade in the near term given higher agricultural export prices. They agreed that while repricing of mortgages at higher rates will be a drag on private consumption, this would be mitigated by higher interest income from financial assets. Like staff, the authorities expected near-term inflationary pressures and suggested that temporary factors, such as fuel and food prices, supply chain disruptions, and the lagged effect of rising house prices may play a larger role than wage pressures in the near term. The authorities saw no significant exchange rate misalignment, noting that the exchange rate has remained fully flexible.

PACING THE WITHDRAWAL OF POLICY STIMULUS

10. After sizeable economic stimulus measures during the initial COVID-19 waves, the normalization of macroeconomic policies has started. While fiscal policy support played a central role during the 2021 lockdown, COVID-related measures have been downsized as the vaccination rate has risen and lockdown measures have been lifted. The RBNZ was among the first AE central banks to start tightening monetary policy in response to faster economic recovery and emerging inflationary pressures.

11. The authorities deployed fiscal support in response to the pandemic's resurgence and the rise in commodity prices. Contingency measures activated during the 2021 lockdown included the Wage Subsidy Scheme and Resurgence Support Payments, which cushioned the impact on households and firms (Annex V) and have since been downsized.[3] The COVID Support Payment, a temporary relief measure deployed in response to the Omicron variant in early 2022, is targeted to severely affected firms. In March, the government announced a temporary reduction of the fuel excise duty and road user charges to provide relief to consumers in response to the rise in fuel prices due to the war in Ukraine, to be reviewed after three months.[4] The government has also increased social benefits to tackle inequality, financed by the recent increase in the top income tax rate. The fiscal deficit is projected to reach 7.7 percent of GDP in FY2021/22.[5]

12. Going forward, significant fiscal tightening is expected, with a shift in policy focus to structural issues. With the strategic pivot to relying less on lockdowns, a reduced need for fiscal

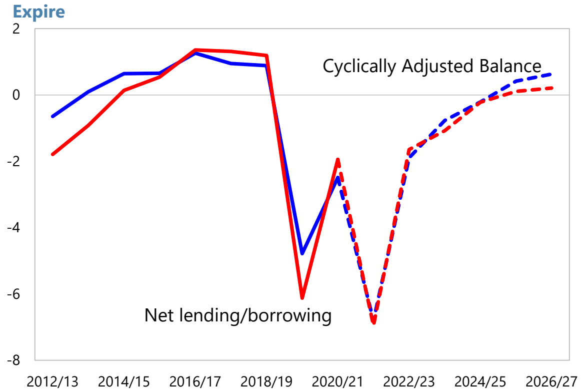
[3] The authorities have committed to maintaining transparency in procurement and issued guidance tailored to COVID-19 emergency situations. They publish information on awarded contracts.

[4] New Zealand has also imposed sanctions against Russia, including tariffs on Russian imports, export restrictions, sanctions on banks, and selective travel bans and asset freezes.

[5] New Zealand's fiscal year runs from July to June.

support is expected. Given the expiration of previous support measures, a sizeable tightening of the fiscal stance is projected for FY2022/23. The government will focus on emerging structural issues and has introduced the Climate Emergency Response Fund (CERF), amounting to 1.4 percent of GDP, while also scaling up spending for health sector reforms.

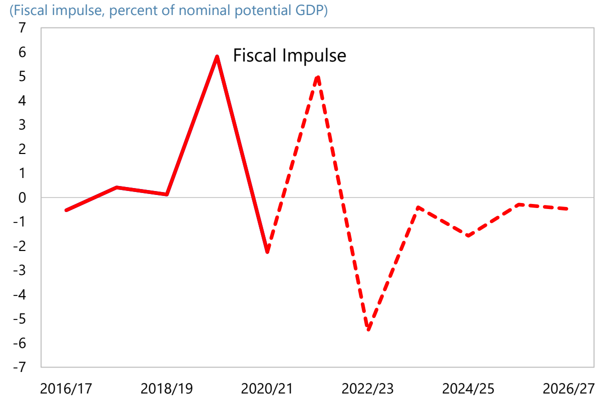
Fiscal Deficit Is Expected to Shrink as COVID-Relief Measures Expire



Source: IMF staff estimates.

Fiscal Stance Will Tighten in FY2022/23

(Fiscal impulse, percent of nominal potential GDP)

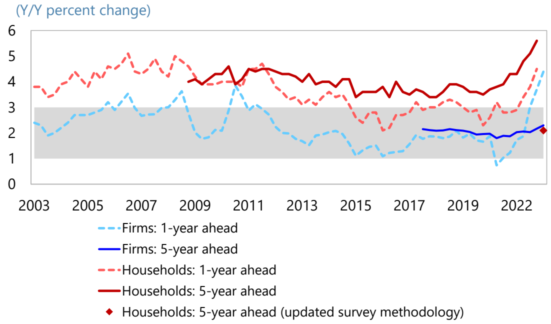


Source: IMF staff estimates.

13. The RBNZ tightened monetary policy to address rising inflation (Figure 2). Inflation has accelerated, inflation expectations have risen for the 1- to 2-year horizon, and wage growth is strong. The Monetary Policy Committee (MPC) discontinued asset purchases under the Large-Scale Asset Purchase (LSAP) program in July 2021 and raised the Official Cash Rate (OCR) by 125 bps cumulatively since October 2021. The MPC has signaled significant further OCR hikes ahead and announced the unwinding of LSAP holdings. By letting securities mature and targeting an additional redemption of NZ$5 billion annually (starting in July 2022), the bond portfolio will be fully unwound by 2027. To avoid market volatility, the RBNZ intends to redeem the securities directly with New Zealand Debt Management, rather than through secondary market sales. The RBNZ has stated that it considers house prices to be unsustainable and welcomes the recent cooling in the market. Nevertheless, its monetary policy objective remains focused on maintaining price stability and supporting maximum sustainable employment.

Near-Term Inflation Expectations Have Risen, But Medium-Term Expectations Remain Anchored

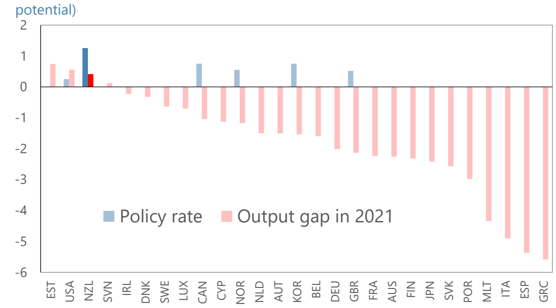
(Y/Y percent change)



Source: RBNZ.

RBNZ Raised Policy Rate as Output Gap Closed

Change in policy rate since end-2020 (p.p.), Output gap in 2021 (percent of potential)



Sources: Bank for International Settlements and World Economic Outlook.

Staff Views

14. During the exit from exceptional, crisis-related policy support, the pace of policy normalization needs to be calibrated carefully. With tight labor market conditions and elevated inflation, it is appropriate to withdraw fiscal and monetary support as envisaged. But considering continued uncertainty, the speed of policy tightening should be under continuous review and dependent on macroeconomic conditions.

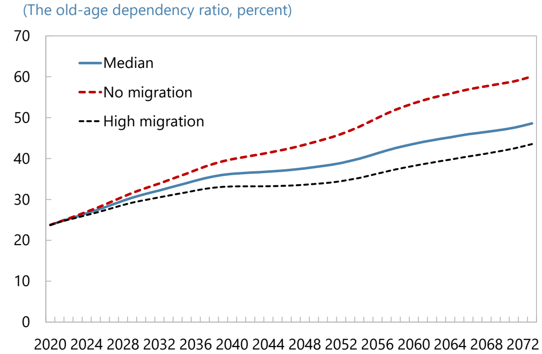
15. Fiscal policy should remain agile in light of continued uncertainty. Given tight labor market conditions, elevated inflation, and exit from COVID-19 support measures, the significant fiscal consolidation in FY2022/23 (fiscal impulse of -5.3 percent of potential GDP) is appropriate. If downside risks materialize, additional fiscal support, including well-targeted lifeline measures and public investment, should be considered. Conversely, spending can be reduced more quickly if labor market conditions tighten further and high inflation persists.

16. Fiscal measures can help render growth more durable, inclusive, and sustainable. The recent increase in social spending and active labor market policies targeted to disadvantaged groups is welcome and will help mitigate long-standing inequality. Given weak productivity performance, additional fiscal spending should center on growth-enhancing public investment, and further green investment should be considered in support of the government's emission targets. The temporary reduction of fuel excise duty and road user charges is very broad and should be replaced by targeted transfers if continued support is needed after the announced period.

17. Long-term fiscal challenges from population aging underscore the case for a credible fiscal anchor. Despite pandemic-related fiscal stimulus, New Zealand's public debt is expected to remain low compared to peer AEs, with gross debt peaking at 52 percent of GDP in FY2023/24. Public debt sustainability remains robust, and substantial fiscal space is available to address downside risks (Annex VI). However, outlays for pensions and health care are expected to rise markedly over coming decades given an aging population (especially if migration inflows remain weak), which will likely require substantial adjustments. As pandemic-related uncertainty subsides, the authorities should set a fiscal anchor to replace the suspended debt target range.[6] The strategy should be calibrated carefully to secure growth-enhancing investment over the longer term and should be aligned with New Zealand's existing long-term fiscal framework. Staff supports the authorities in considering the establishment of an Independent Fiscal Institute, which would provide independent assessments and strengthen the fiscal policy framework.

Population Is Expected to Age Gradually

(The old-age dependency ratio, percent)



Source: Stats NZ.

[6] Before the pandemic, New Zealand operated with a net core crown debt target of 15-25 percent of GDP.

18. Significant further monetary tightening is appropriate in the near term. Cyclical indicators such as inflation, output gap estimates, and tight labor market conditions support the planned withdrawal of monetary support. Further upside surprises to inflation or inflation expectations would warrant a faster pace of tightening, while a quicker normalization of inflation or setbacks to growth from COVID-19 could justify a more measured pace. The OCR will likely need to rise to above the neutral rate (of around 2.5 percent) to address demand pressures. As market and retail interest rates have moved ahead of the increase in the OCR, the size of the RBNZ's balance sheet can be reduced gradually based on evolving economic conditions.

Authorities' Views

19. The authorities deemed the scheduled policy normalization appropriate. They highlighted that continued policy tightening is warranted given the strong cyclical position and elevated inflation, and indicated that the focus of fiscal policy would shift to structural issues such as climate change and health sector reform. The authorities stressed that the reduction of the fuel excise duty and road user charges was intended to provide direct support to consumers in a timely manner, and that it was intended to be strictly temporary. They highlighted that the pace of monetary and fiscal policy normalization would be tailored to evolving economic conditions, noting their ample policy space that can be deployed if downside risks materialize.

20. The authorities stressed the need to return to a fiscal anchor. They indicated strong commitment to keeping debt at prudent levels and maintaining significant buffers that can be deployed in case of future shocks. An update to the fiscal strategy, including new fiscal rules, is expected in the May 2022 Budget.

21. The RBNZ noted that its least regrets approach to monetary policy currently implies a strong stance against rising inflation. It saw the planned increases of the OCR as an appropriate response to price pressures but noted the need to assess the situation continuously given high uncertainty. Reducing the size of the balance sheet will restore room to deploy unconventional policies in the future as needed, while ensuring that LSAP holdings, which account for a significant portion of some maturities, do not unduly impinge on the functioning of the government bond market as fiscal consolidation takes effect.

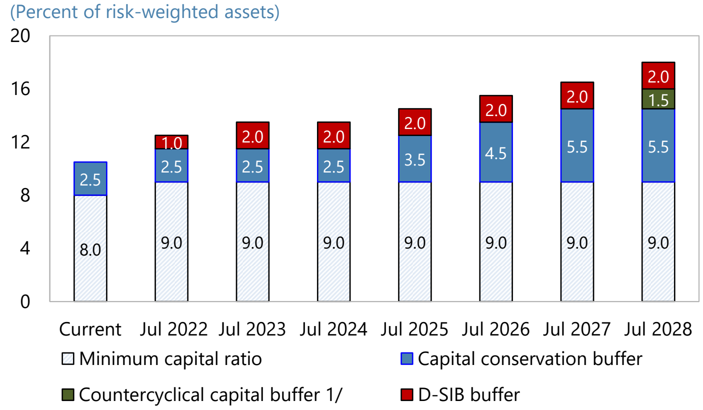
REINFORCING FINANCIAL SECTOR RESILIENCE

22. The RBNZ is implementing measures to strengthen financial stability. Bank capital requirements will rise from 10.5 percent of risk-weighted assets currently to at least 16 percent in 2028. Domestic systemically important banks will be subject to an additional two-percent buffer. The increase corresponds to the RBNZ's estimates of capital needed to withstand a one-in-200-year crisis without public support. Banks are ahead of schedule to meet the new standards, driven by higher retained earnings. RBNZ analysis suggests the impact on banks' activities and lending rates would be limited: higher lending costs (central estimate of 20 bps in the steady state) would reduce potential GDP by 0.2 percent. But this would be more than offset by the estimated benefits from a lower incidence of financial crises (+0.8 percent of steady state potential GDP). The floor on the core funding ratio, which was lowered to 50 percent in March 2020, reverted to the pre-pandemic minimum of 75 percent in January 2022.

23. A new Reserve Bank Act takes effect in July 2022, broadening the RBNZ's mandate to include financial stability. A Financial Policy Remit issued by the Minister of Finance will set out matters—potentially, for example, about sustainable house prices or climate change policies—that the RBNZ must incorporate when making strategic prudential decisions. This does not affect the formulation of monetary policy, which remains focused on price stability and sustainable employment, and monetary policy objectives are unchanged. The Act also contains significant governance changes, including a new Board, distinct from the Monetary Policy Committee, that will take all (non-monetary policy) decisions, ending the current single decision-maker model.

Bank Capital Requirements to Begin Rising in 2022

(Percent of risk-weighted assets)



Source: RBNZ.

1/ Neutral level of the buffer to be introduced.

24. A new Deposit Takers Act to strengthen the financial stability framework is being prepared (Annex VII). The Deposit Takers Bill (DTB), which has been released for public comments, seeks to improve the existing supervisory and crisis management frameworks, including by implementing a single regime for both banks and non-bank deposit takers, introducing a Depositor Compensation Scheme (DCS) to cover up to NZ$100,000 per eligible depositor per institution, and proposing resolution amendments. The Bill also clarifies the RBNZ's independence in instituting early intervention measures.

25. The RBNZ started preparatory work on digital money. It issued two papers and conducted a public consultation. The RBNZ's initial considerations focus on a public policy case for or against a "general-purpose" central bank digital currency (CBDC), which would be available to all individuals, communities, and businesses. The RBNZ plans to put forward concrete proposals for public consultation in the coming months.

Staff Views

26. The RBNZ's focus on strengthening banks' resilience is timely. The higher capital requirements are in line with assessments of the adoption of Basel III elsewhere. The high exposure to the housing sector (64 percent of total bank credit outstanding) also warrants a prudent stance. The careful approach to a CBDC is welcome, as consultations regarding design and policy issues would help shape public acceptance in an environment where the use of physical cash is expected to decline.

27. The new RBNZ Act strengthens governance and clarifies the RBNZ's role in financial stability. Many provisions in the Act are in line with recent Fund advice, particularly related to the RBNZ's decision-making structure, including Board composition to improve policy coordination, the Governor's status, and criteria for Board membership. The Minister's power to assign new functions to the RBNZ is now more constrained and conditional on RBNZ requests. However, scope for improvement remains regarding the lack of clarity in balancing multiple central bank objectives, and central bank autonomy.[7]

28. The DTB proposes several useful changes that strengthen the RBNZ's capacity to maintain and strengthen financial stability, though scope for further improvement remains. Improvements to the supervisory and crisis management frameworks are welcome, including creation of a single regime for all deposit takers, resolution amendments, and introduction of the DCS. These changes also address a number of recommendations of the 2017 Financial Sector Assessment Program (FSAP) report for New Zealand (Annex X). That said, there remains scope for further strengthening the regime by amending the corporate governance and early intervention frameworks, buttressing the RBNZ's autonomy in bank resolution and granting it statutory bail-in powers, clarifying the rules for public funding in bank resolution cases, and specifying the legal status and governance arrangements for the DCS. There is also scope for integrating risks related to climate change into the supervisory framework.

Authorities' Views

29. The authorities highlighted ongoing progress in financial sector reforms. They noted that the DTB represents a shift in New Zealand's approach to financial stability. The strengthening of the regulatory and supervisory pillars necessitates an increase in resources devoted to financial supervision, which is underway. They noted that there is scope to substantially address several of staff's comments through implementing regulations and the use of civil (contractual) commitments (for example, in setting out a process to bail in creditors and shareholders in bank resolution). The planned implementation of the new capital framework, which is well underway, is expected to further strengthen banks' resilience and will be supplemented by a review of the liquidity framework, which will be launched shortly. On CBDC implementation, the RBNZ emphasized that no decisions have been taken yet and work will be guided by demonstrable benefits from a CBDC, while also ensuring risks are well-understood and manageable.

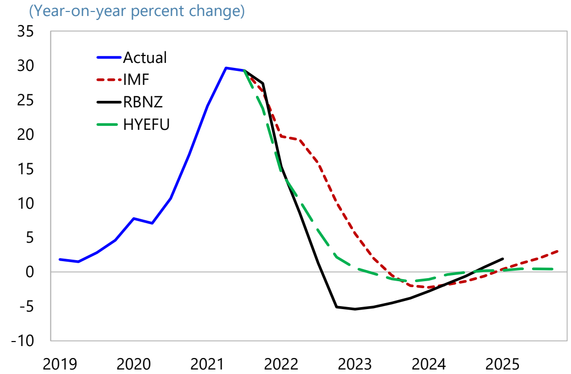
[7] See Annex VI of the staff report for the 2021 Article IV Consultation with New Zealand.

REBALANCING THE HOUSING SECTOR

30. House prices have peaked and are expected to correct. The market is turning given that important drivers over previous years, such as low mortgage rates and easy credit availability, are now reversing (see the accompanying Selected Issues Paper). The recent trend of falling sales volumes and mortgage lending is expected to continue, supporting a house price correction, although the period and intensity are difficult to estimate.

House Price Growth Is Expected to Decline

(Year-on-year percent change)

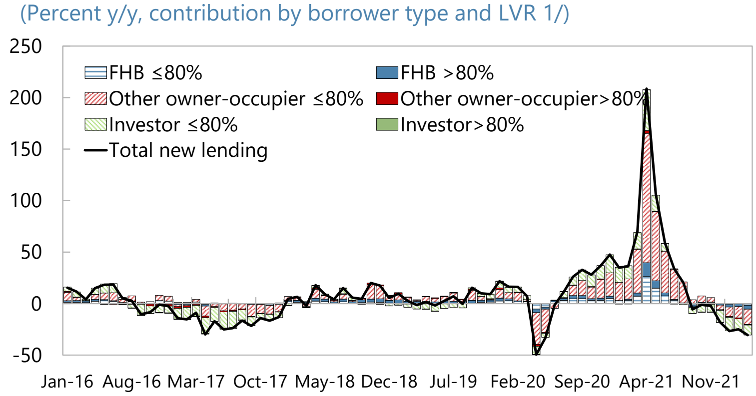


Sources: Stats NZ; IMF; RBNZ; and HYEFU.

31. Rising mortgage rates and recent policy actions are curbing demand. In response to actual and expected withdrawal of monetary stimulus, standard mortgage rates rose by between 40 and 150 bps in 2021H2. The removal of property investors' tax deductibility of mortgage interest and the extension of the minimum holding period to exempt capital gains on investment properties from income tax have contributed to a decline in investor demand.[8] The RBNZ re-introduced loan-to-value ratio (LVR) limits on mortgages in March 2021 and tightened them in May and November. The December 2021 amendments to the Credit Contracts and Consumer Finance Act (CCCFA), designed to protect borrowers and strengthen the consumer credit regulatory regime, had the unintended effect of tightening credit conditions further. These developments contributed to a significant decline in mortgage lending (-31 percent y/y in March 2022), with new loans to investors and highly leveraged buyers (LVR exceeding 80 percent) declining more rapidly (-44 percent and -56 percent y/y, respectively). The RBNZ intends to implement additional MPMs for potential future use to broaden its toolkit. A framework to introduce DTI ceilings will be released by end-2022 for implementation by mid-2023. The RBNZ is also looking at the possible use of a floor on test interest rates to assess borrowers' ability to meet debt service obligations.

New Residential Mortgage Lending Declined Across All Borrower Types, Led by Investors

(Percent y/y, contribution by borrower type and LVR 1/)



Sources: RBNZ; and IMF staff calculations.

1/ FHB: First-home buyer. LVR: Loan-to-value ratio.

[8] Interest deductions are not allowed for existing properties acquired since end-March 2021, and deductions for earlier purchases are being phased out. The minimum holding period to exempt capital gains on investment properties from income tax ("bright-line test") was extended from 5 to 10 years.

32. Efforts are ongoing to improve housing supply. A NZ$3.8 billion (around 1.1 percent of GDP) allocation was made to the Housing Acceleration Fund to increase housing supply and improve affordability. Amendments to the Resource Management Act (RMA) in October 2021 allow for higher-density housing construction without requiring resource consent, making it easier to build new homes. However, these measures will take time to bear fruit: a cost-benefit appraisal by the Treasury estimated that about 75,000 additional dwellings would be built in the next 5-8 years, with more than 200,000 additional dwellings available in 20 years. The government is also in the process of reforming the RMA, which should streamline planning processes. There are plans to boost effective land supply by incentivizing local authorities to approve new housing projects faster.

Staff Views

33. Tackling housing imbalances requires a comprehensive approach, and recent initiatives will help address these imbalances. Achieving long-term housing sustainability and affordability depends critically on freeing up land supply, improving planning and zoning, and fostering infrastructure investments to enable fast-track housing developments and lower construction costs. There is a need for continued spending on land, infrastructure, and housing, including financial incentives that enable and incentivize local councils and iwi (Māori tribal organizations) to provide infrastructure for new developments. Increasing the stock of social housing also remains important in the near term, while supply constraints are addressed over time.

34. A moderation of prices is widely expected, and macroprudential policy should be adjusted commensurate with the evolution of financial stability risks. The use of macroprudential measures to address the financial stability impact of surging house prices has been appropriate. LVR restrictions have been effective in making lending for housing more cautious. Restrictions could be relaxed in case of a stronger-than-expected downturn in the housing market. Financial stability risks from a sharp downturn in the housing market are limited given high bank capitalization, but pockets of vulnerability, particularly among recent borrowers, may exist. More broadly, in case of a sharp downturn, potentially reinforced by a faster rise in interest rates, there could be a significant impact on consumption through wealth and confidence effects (see accompanying Selected Issues Paper). A more extensive MPM toolkit, including the ability to readily implement DTI ceilings and loan serviceability test interest rate requirements when warranted, would be useful in addressing future risks.

Authorities' Views

35. The authorities stressed that, while the housing cycle had likely turned, improving affordability remained a key priority. While prices are expected to decline in 2022, this only partially reverses the very large increases of recent years and will therefore not make a significant impact on affordability. A comprehensive approach covering the demand and supply sides of housing is underway, with more initiatives planed under the wider review of the RMA and laid out in the National Policy Statement on Urban Development. The Housing Acceleration Fund will provide funding at the local level for infrastructure development, and the first tranche of projects is likely to be approved soon. The authorities emphasized their commitment to invest in social housing. They agreed that the CCCFA amendments may have impacted credit conditions, though the effect is hard to quantify. They noted that clarifications have already been issued, with further changes being considered in consultation with the industry.

PROMOTING INCLUSIVE AND SUSTAINABLE GROWTH

36. Efforts should continue to address structural impediments to inclusive and sustainable growth. New Zealand's productivity performance has been weak compared to peer AEs, with innovative investment and entry of foreign firms remaining low. ICT-related sectors in New Zealand remain relatively small, with some skill shortages and room for expansion. While overall labor market conditions have been strong, with the gender gap narrowing, a large dispersion across ethnic and age groups remains. The authorities plan to introduce an unemployment insurance scheme, largely replacing the existing tax-financed Jobseeker Support, with the aim of strengthening social insurance (Annex VIII). The minimum wage has increased markedly in recent years, and, relative to the median wage, is among the highest in advanced economies (Annex IX).

37. New Zealand has some distance to go to meet its targets on reducing greenhouse gas (GHG) emissions.[9] While New Zealand's per capita emissions have steadily fallen over two decades, the level is high relative to OECD peers. The bulk of emissions are from the agricultural sector, primarily methane. At COP26, New Zealand committed to limiting net GHG emissions by 2030 to no more than 50 percent of 2005 gross emissions and reaffirmed its aim to achieve by 2050 net zero non-agricultural emissions while reducing agricultural methane emissions to 24-47 percent below the 2017 level. The primary policy instrument for reducing non-agricultural emissions is the Emissions Trading Scheme (ETS), a cap-and-trade system which aims to make it costly to emit carbon while rewarding efforts to increase carbon capture through afforestation. The ETS has been successful in incentivizing investment in afforestation, though gross emissions continue to rise. In 2021, the ETS was liberalized, causing prices to nearly double to NZ$70 per unit by March 2022. The authorities estimate that prices will need to rise by around 2-3 times this level to bring CO_2 to net zero by 2050, while modeling by staff suggests a real doubling of prices would not be sufficient to meet the commitments. Agricultural emissions are currently not included in the ETS but all other GHGs are part of the scheme.

38. An Emissions Reduction Plan (ERP), to be released in May 2022, will outline how the government intends to meet its targets. Policy proposals in the authorities' public consultation include strengthening the ETS, reducing vehicle use and encouraging uptake of zero- and low-emissions transport, increasing funding for research and development into new technologies and improvements in agriculture, providing financing to encourage energy efficiency in building and construction, integrating emissions assessments in public project selection, and committing to reach net zero in the public sector by 2025. Consultations are under way for options to price agricultural emissions. The government is also considering investment in offshore abatement as a possible avenue to help deliver on New Zealand's 2030 climate goals. Preparation of a National Climate

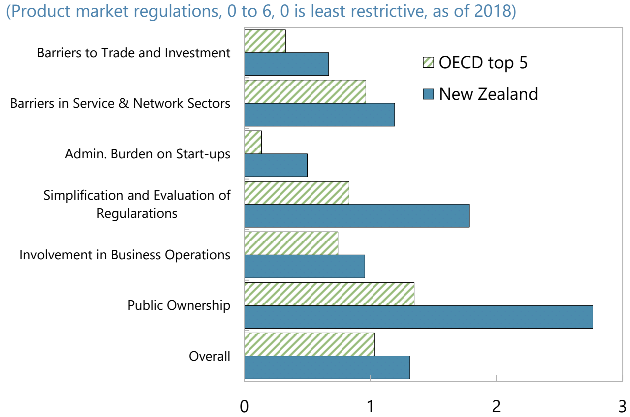
[9] See accompanying Selected Issues Paper.

Adaptation Plan is underway and will be ready by August 2022. New Zealand is also leading the way in requiring disclosure in climate change risks in financial statements.

Staff Views

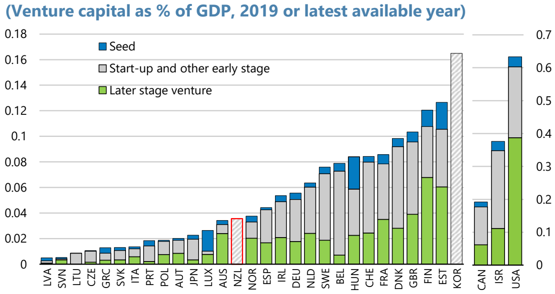
39. Strengthening productivity should remain a priority. The authorities should promote innovative investment by expanding R&D tax credits and other support measures, while also promoting their take-up and scaling up government investment on R&D. Government efforts to promote digitalization, including Digital Boost for SMEs, are welcome and can help lay the foundation for post-COVID growth. Alleviating financial constraints faced by SMEs and innovative firms would be essential to promote innovation and digitalization. There is scope for reducing product market regulations further, which would promote competition, entry of foreign firms, and long-term productivity growth. In this context, the streamlining of foreign investment rules under the Overseas Investment Act (OIA) in 2021 is welcome.[10]

Productivity Can Be Lifted By Further Deregulations
(Product market regulations, 0 to 6, 0 is least restrictive, as of 2018)



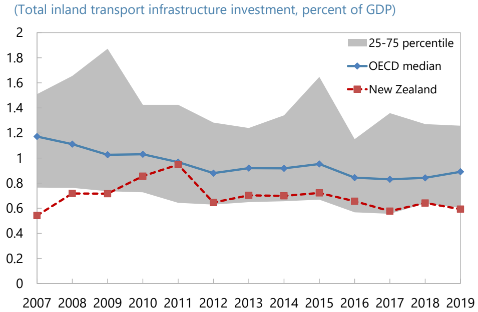
Source: OECD.

There Is Scope for Expanding Venture Capital Investment
(Venture capital as % of GDP, 2019 or latest available year)



Source: OECD.

Infrastructure Investment Remained Relatively Low
(Total inland transport infrastructure investment, percent of GDP)



Source: OECD.

40. Upgrading physical capital is important to support durable and sustainable growth. The recent increase in infrastructure spending will help reduce the existing infrastructure gap.[11] The priority is now to overcome supply bottlenecks to ensure timely implementation of infrastructure

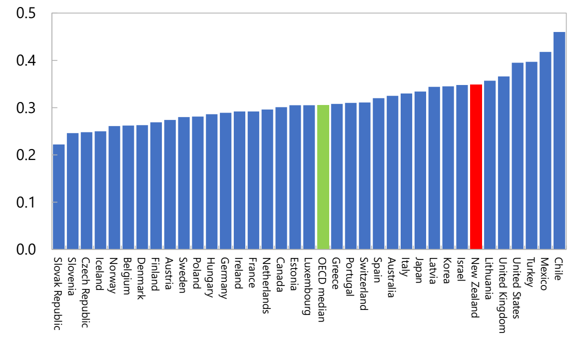
[10] The 2021 changes are expected to decrease screening times, increase clarity for overseas investors, and reduce the number of low-risk transactions being screened. For example, increases to existing interests that do not cross control limits (25, 50, 75 or 100 percent) are no longer screened. The powers to prohibit investments under the enduring national interest assessment have been used sparingly, and staff encouraged continued, judicious use. A broader review of restrictions for foreign investment in residential real estate, which had been previously classified as a capital flow management measure (see 2018 Staff Report), is currently not envisaged.

[11] Infrastructure gap is estimated to be between NZ$17 billion to NZ$104 billion.

projects. Further efforts to support local councils' infrastructure funding and financing would also facilitate timely infrastructure provision.

41. Labor market policies should support inclusive growth while strengthening macroeconomic stability. While overall labor market conditions have tightened, long-standing dispersion among age and ethnicity groups remains. In this respect, the recent expansion of active labor market policies is an important step, and further targeted support should be considered to promote inclusive growth. There is room for promoting female labor force participation, which would help longer-term growth. While the introduction of the Income Insurance Scheme aims to enhance automatic stabilizer effects, the tradeoff between insurance and disincentives should be managed carefully, for example by topping up benefits only during downturns, which could alleviate the tradeoff (Annex VIII). Further increases in the minimum wage should be carefully calibrated and linked to underlying labor productivity growth.

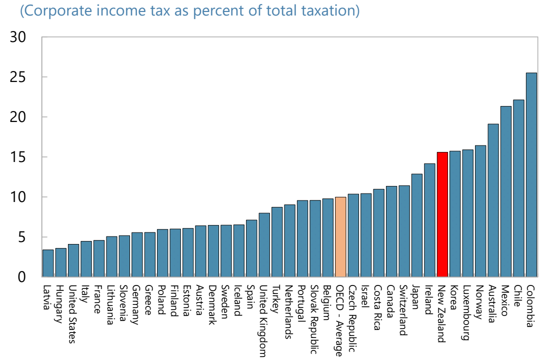
Gini Coefficient
(Latest available data, 2017-2019)



Source: OECD.

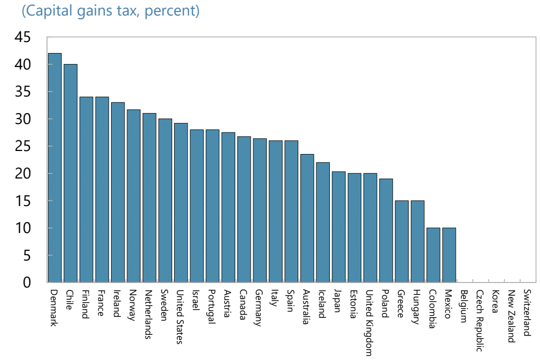
42. Tax reforms would help promote efficiency. The corporate income tax rate is relatively high compared to peer advanced economies. Transitioning to other sources, including capital gains and possibly land taxes would boost business investment and entry of new businesses, thereby promoting productivity growth, without reducing aggregate revenues.

Reliance on Corporate Income Tax Is High
(Corporate income tax as percent of total taxation)



Source: OECD.

New Zealand Does Not Have a Capital Gains Tax
(Capital gains tax, percent)



Source: Tax Foundation.

43. Strengthening the price-based mechanism is critical for meeting GHG emissions targets and mitigating risks. The recent liberalization of ETS prices is welcome and will allow for more transparent price signals to transmit through the economy. The forthcoming Emissions Reduction Plan is an opportunity to further strengthen the price-based system, which would incentivize the adoption of new technologies and methods needed to achieve the targeted reductions. That said, the authorities' assessment shows that the ETS is moderately regressive and has thus far mainly incentivized investment in afforestation, which by itself will not be a sustainable solution to climate mitigation. Complementary policies to address gross emissions, including investment in green technologies and infrastructure, supporting innovation, and regulatory actions to accelerate the uptake of low- and zero-emissions technologies may thus be needed, along with the use of ETS proceeds to compensate those adversely affected by carbon price increases, particularly vulnerable groups. It will also be important to find a price-based mechanism for agricultural emissions to incentivize emissions reductions in New Zealand's largest emissions source. By contrast, staff cautioned on the possible use of offshore offsets to meet climate goals given issues related to verifying emissions reductions and potential double counting. On adaptation, a robust dialogue should begin ahead of the release of the National Climate Adaptation Plan to ensure that the costs of adaptation are measured relative to potential losses from climate change.

Authorities' Views

44. The authorities agreed on the need to reignite productivity growth and close the infrastructure gap. They stressed their intention to promote innovation and indicated that the R&D tax credit would be a main vehicle. They also intended to promote digitalization and foster digital skills, in line with Digital Technologies Industry Transformation Plan to be finalized in mid-2022.

45. The authorities highlighted planned reforms to ensure inclusive growth. They stressed the benefits of the Income Insurance Scheme, which will close an important gap in social protection coverage. They indicated that the choice of a relatively short entitlement duration was motivated by New Zealand's flexible labor market, where unemployment episodes tend to be relatively short, while the relatively high replacement ratio was chosen to match that of accident compensation payments. They also agreed that active labor market policies would be important to achieve inclusive growth and stated that they would calibrate such policies along with the introduction of the Income Insurance Scheme, while strengthening the review framework of existing policy measures. While they had not seen any major impact from previous minimum wage increases on employment, they concurred that very large (real) future increases could potentially restrain employment growth and erode skill margins.

46. While the authorities agreed that there are potential efficiency benefits from tax reform, they noted that there were competing trade-offs that would require careful consideration. They also highlighted potential implementation challenges, including leakage from personal income tax to corporate income tax if corporate income tax is reduced.

47. The authorities reiterated strong commitment to their climate targets, building on the ETS as the key tool. The price increases in the ETS following liberalization in 2021 were seen as an important step, and further strengthening of price-based measures, along with complementary policies to facilitate emissions reductions, would be part of the forthcoming Emissions Reduction Plan. They also pointed to ongoing consultations toward instituting price-based measures to reduce agricultural emissions. On adaptation, the authorities intend to outline possible approaches to addressing identified risks as part of a public consultation process.

STAFF APPRAISAL

48. **New Zealand managed the transition to living with COVID well.** Strong health and economic policies supported quick recovery from lockdowns in 2021. Following a slow start, swift progress in the vaccination campaign has offered a pathway to a new normal. The expected border reopening will provide an additional economic boost to the tourism and education sectors. Still, economic growth is expected to moderate this year, reflecting policy tightening, global spillovers, and the ongoing Omicron wave. Amid commodity price pressures related to the war in Ukraine, continued supply chain disruptions, and a tight labor market, inflation is expected to remain high and stay well above the RBNZ's target range this year. Overall, the outlook remains highly uncertain, contingent on the trajectory of the pandemic and geopolitical developments.

49. **The path of macroeconomic policy normalization needs to be calibrated to evolving economic conditions.** With output above potential and stronger-than-expected inflation, the authorities are appropriately withdrawing fiscal and monetary support. Under baseline expectations for growth and inflation, the pace of planned policy support withdrawal is adequate. That said, the pace should be adjusted nimbly in case upside or downside risks materialize.

50. **Fiscal policy should remain agile amid continued uncertainty**. While the scheduled tightening of fiscal policy is appropriate, the authorities should calibrate the fiscal stance on the evolution of the pandemic and economic conditions, providing additional, targeted support where needed in case of renewed, COVID-related disruptions. Fiscal policy should also focus on promoting long-term growth while addressing emerging structural issues. As uncertainty related to the pandemic recedes, the authorities should update their fiscal targets, which were suspended during the pandemic, to provide an anchor for fiscal policy and manage long-term spending pressures.

51. **Monetary policy should remain data dependent, and continued, swift policy normalization will be appropriate under baseline conditions**. Given New Zealand's cyclical position, continued, significant increases in the OCR in the near term would signal the RBNZ's commitment to addressing inflation. In the event downside risks to growth materialize, more gradual tightening, coupled with a pause in reducing the RBNZ's balance sheet, can be considered, but elevated inflation suggests that room for additional monetary stimulus is limited.

52. **Raising bank capital requirements and enlarging the MPM toolkit will help the system weather future shocks.** Higher bank capital requirements will help insulate the banking system from future shocks, though the impact on lending rates should be monitored. The DTB is a step forward in adopting international good practices to strengthen financial regulation and supervision and enhance depositor protection, and opportunities for further strengthening the proposed law should be seized, including by addressing remaining FSAP recommendations.

53. **Continued focus is needed on addressing housing imbalances.** The macroprudential measures implemented last year should be maintained, and work to expand the macroprudential

toolkit is appropriate. Increasing the stock of social housing remains important in the near term as a durable solution to housing affordability is achieved over time by addressing supply constraints.

54. The external position is broadly consistent with economic fundamentals and desired policy settings. The assessment is subject to large uncertainty and assumes that the extraordinary impact of COVID-19 on the tourism and transportation sectors is temporary.

55. Stronger efforts are needed to meet GHG emissions goals. The recent rise in carbon prices is welcome, and the forthcoming Emissions Reduction Plan is an opportunity to further strengthen the price-based mechanism and lay out complementary policies. The planned introduction of prices on agricultural emissions will be important to include the largest emissions source in New Zealand's climate mitigation efforts, incentivizing the adoption of new technologies and methods to lower emissions. Proceeds of higher carbon prices should be used to invest in emissions reduction and to compensate those adversely affected by carbon price increases, particularly vulnerable groups.

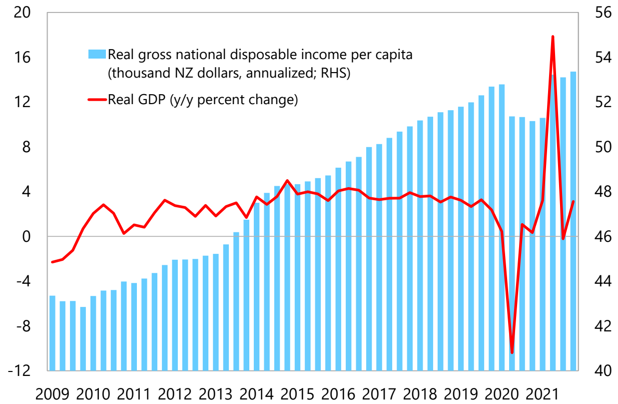
56. Structural policies should promote durable and inclusive growth. The authorities should promote innovation and digitalization, and tax reforms would support long-term growth. Infrastructure spending should aim at reducing the infrastructure gap and supporting the transition to a net zero carbon growth path. Unemployment insurance should be calibrated carefully to address trade-offs between insurance and disincentives, and minimum wage increases should be aligned with underlying labor productivity growth.

57. It is recommended that the next Article IV consultation be held on the standard 12-month cycle.

Figure 1. Rapid Recovery After the Pandemic's Initial Impact

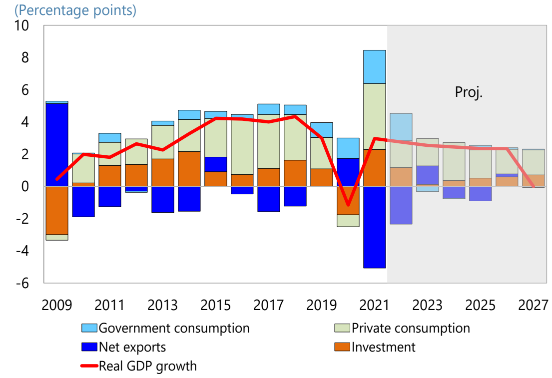
Real GDP growth bounced back rapidly after the initial pandemic impact, though real disposable income remains weak.

Growth Performance



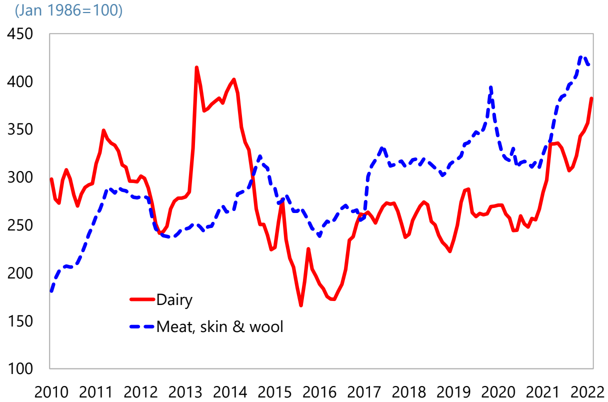
Government and private consumption supported activity in 2021.

Contribution to Growth
(Percentage points)



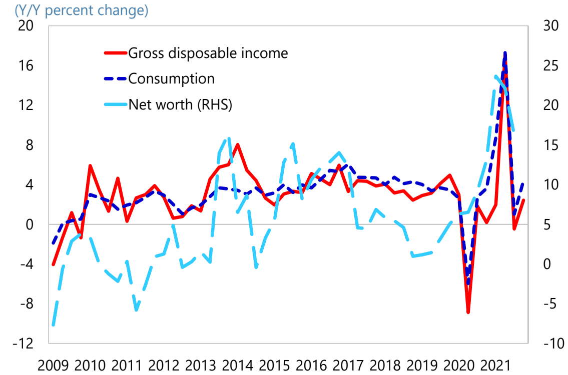
Export prices for major commodities remained firm.

Export Commodity Price Indices
(Jan 1986=100)



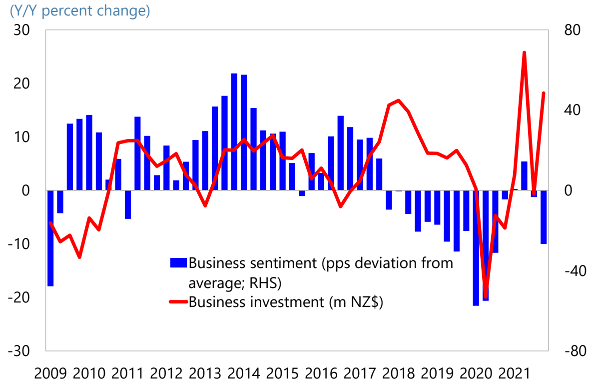
Rising house prices have improved household balance sheets even as income has been volatile.

Real Household Consumption, Income, and Wealth
(Y/Y percent change)



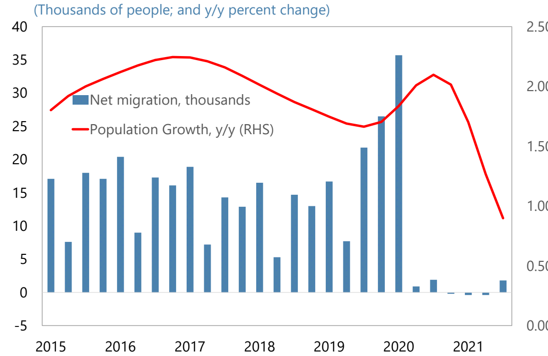
Business sentiment and investment have been volatile given COVID-19 related uncertainty.

Business Sentiment and Investment
(Y/Y percent change)



Migration flows have been weak due to border restrictions.

Migration and Population Growth
(Thousands of people; and y/y percent change)

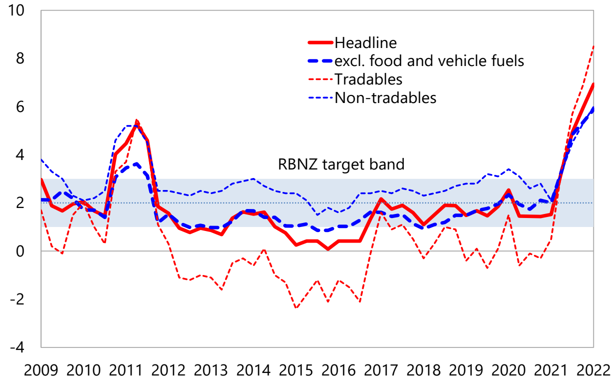


Sources: Stats NZ; Haver Analytics; and IMF staff calculations.

Figure 2. Monetary Stimulus Is Being Withdrawn

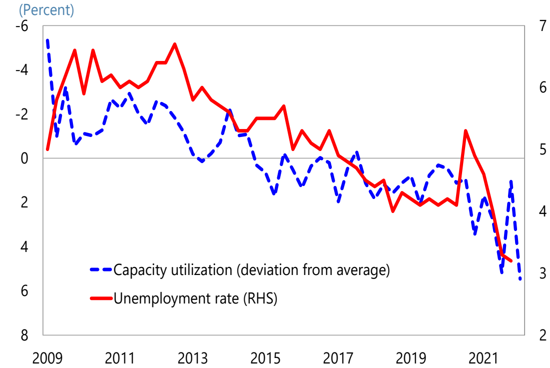
Headline inflation has risen rapidly, well above the target band.

CPI Inflation
(Y/Y percent change)



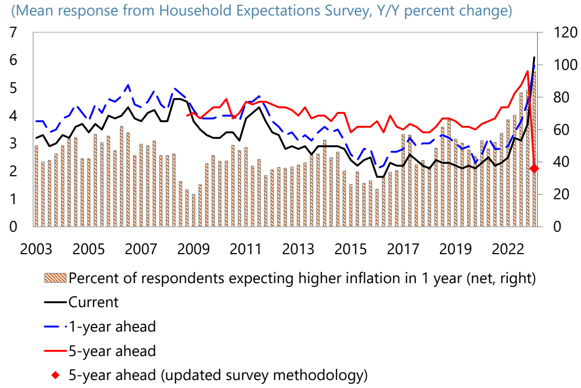
Unemployment continues to fall, signaling a tight labor market.

Indicators of Resource Pressure
(Percent)



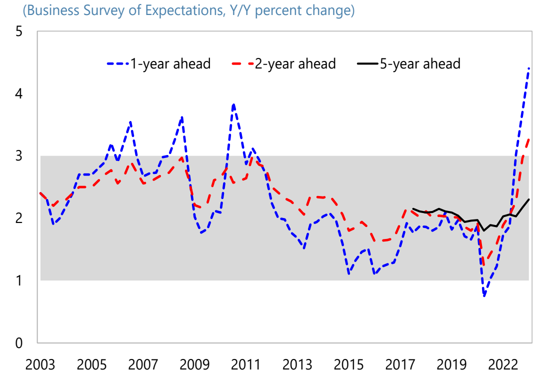
A majority of households expect inflation to rise in the near term…

Consumer Price Index Expectations
(Mean response from Household Expectations Survey, Y/Y percent change)



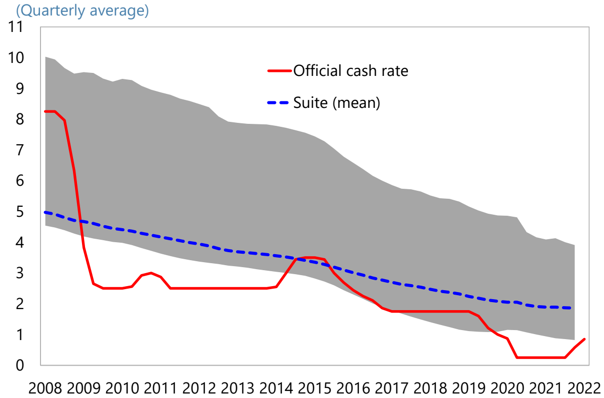
…as do firms, though medium-term expectations remain anchored

Consumer Price Index Expectations
(Business Survey of Expectations, Y/Y percent change)



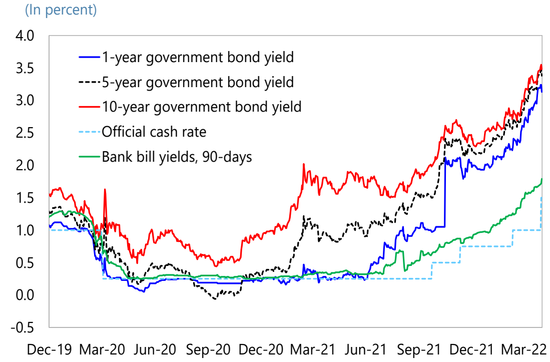
The official cash rate has been raised four times since 2021 but remains broadly accommodative.

OCR and Neutral OCR Indicator Suite 1/
(Quarterly average)



The market anticipated rising rates well ahead of the official announcements.

Interest Rates
(In percent)



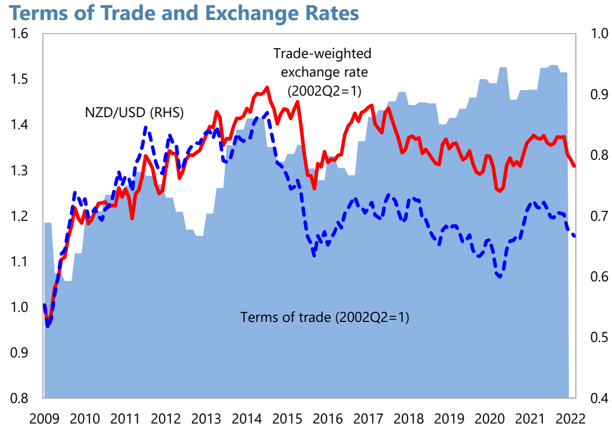
Sources: RBNZ; Haver Analytics; and IMF staff calculations.

1/ Shaded area indicates the range between the maximum and minimum values from a suite of neutral OCR indicators.

Figure 3. The External Sector Remains Stable

The nominal exchange rate has remained broadly stable…

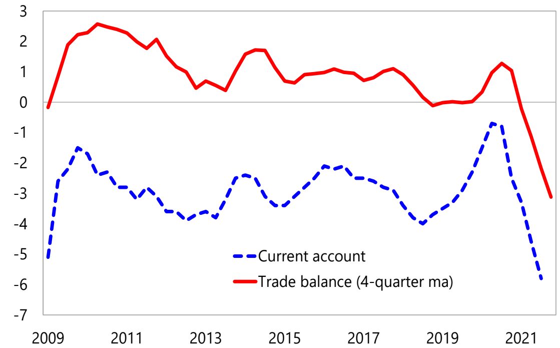
Terms of Trade and Exchange Rates



…although the current account widened sharply given strong domestic demand.

Current Account

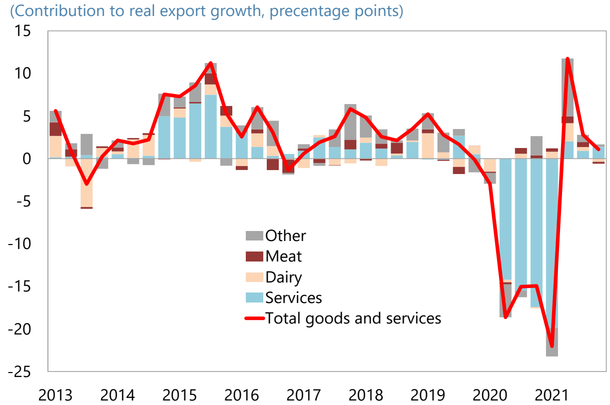
(Percent of GDP)



An uptick in food commodity exports only partially offset the continuing weak performance in service exports.

Export Composition

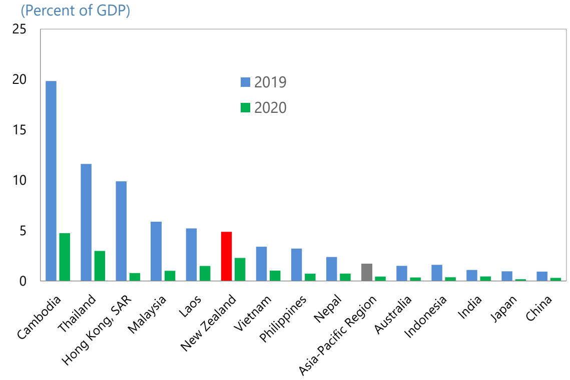
(Contribution to real export growth, precentage points)



With relatively high exposure to international tourism, services exports will lag until borders reopen.

International Visitor Spend

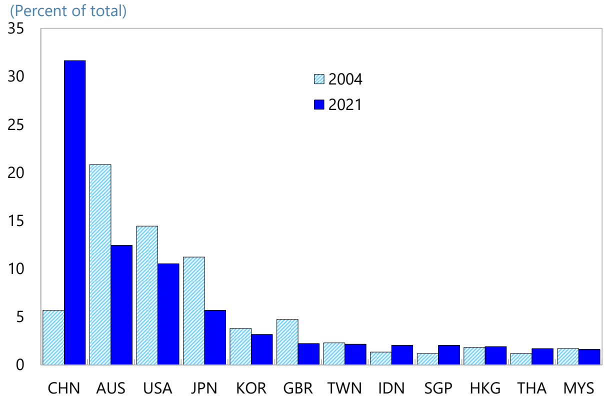
(Percent of GDP)



China remains the most important export market.

Exports by Destination

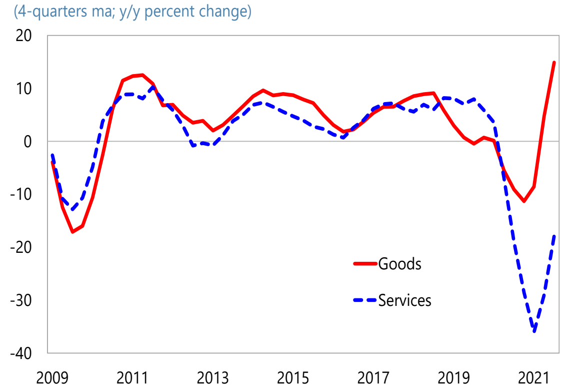
(Percent of total)



While service imports continue to be weak, imports of goods surged as the economy recovered.

Import Volume

(4-quarters ma; y/y percent change)

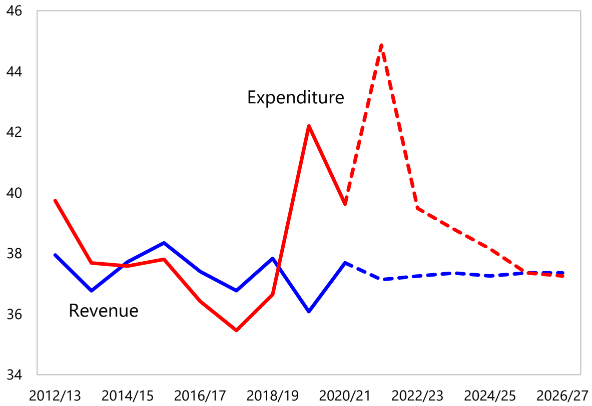


Sources: RBNZ; Haver Analytics; World Travel & Tourism Council; and IMF staff calculations.

Figure 4. The Fiscal Position Remains Resilient Despite Large Stimulus

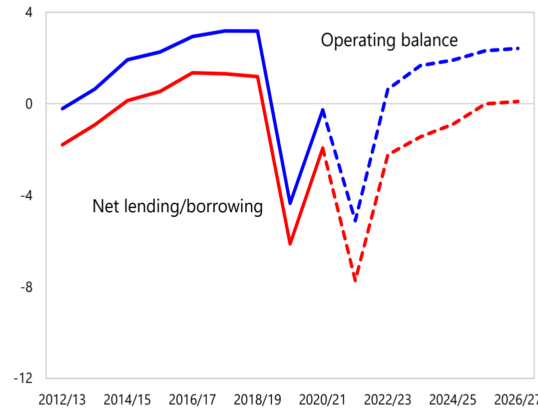
The government boosted spending again in response to the resurgence of the pandemic in 2021...

General Government Revenue and Expenditure
(Percent of GDP)



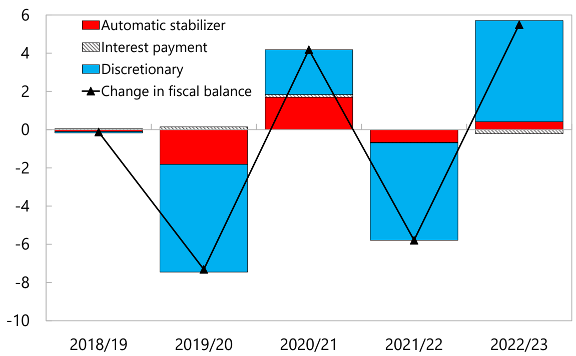
...which has led to a large expected fiscal deficit in FY2021/22.

Overall and Operating Balance
(Percent of GDP)



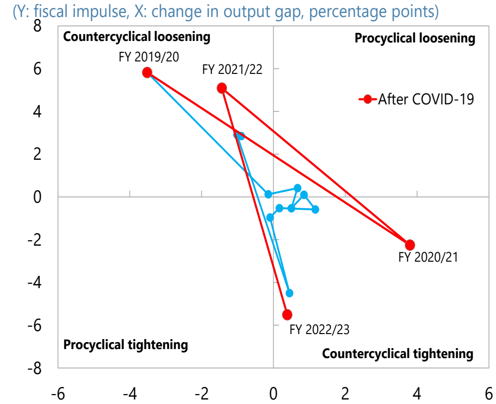
As discretionary COVID-related support measures expire, fiscal policy is expected to tighten.

Drivers of Changes in Fiscal Balances
(Percent of GDP, change from previous year)



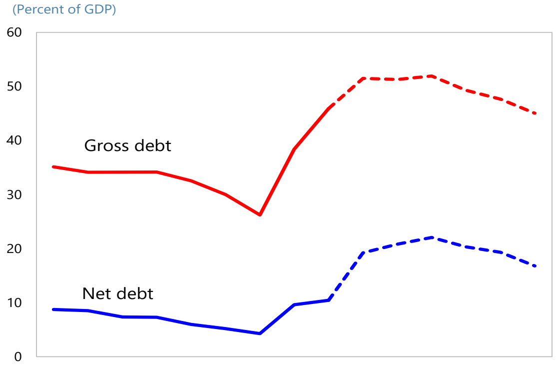
Expected tightening in FY2022/23 is appropriate given strong cyclical conditions.

Discretionary Fiscal Policy and Cyclical Conditions
(Y: fiscal impulse, X: change in output gap, percentage points)



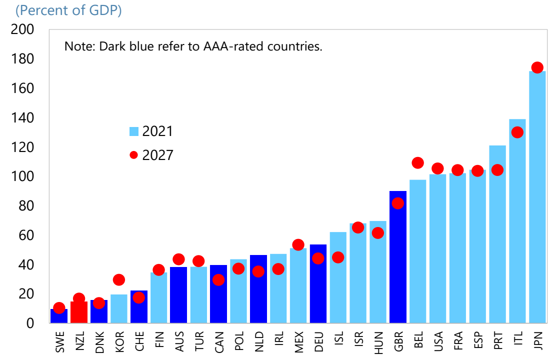
The government debt ratio is projected to stabilize after a large increase due to COVID-related spending...

General Government Debt
(Percent of GDP)



... and is expected to remain low compared to other advanced economies.

Net Public Debt
(Percent of GDP)



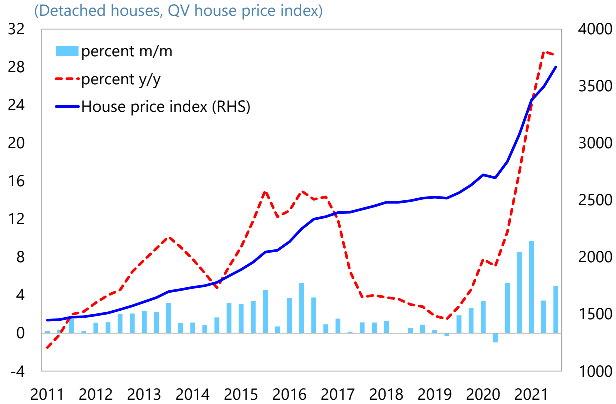
Sources: The Treasury New Zealand; Stats NZ; and IMF staff calculations.

Figure 5. The Housing Market Rebounded Strongly

House price inflation accelerated during the downturn…

House Prices

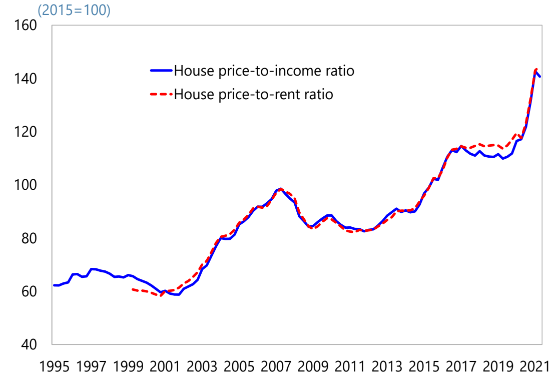
(Detached houses, QV house price index)



…resulting in a rapid decline in affordability…

Housing Affordability

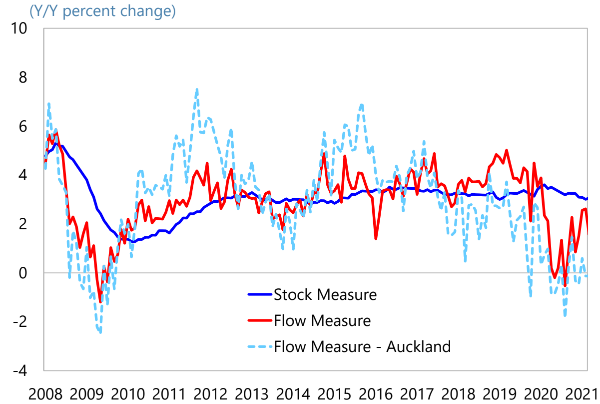
(2015=100)



…and rents began to recover after an initial decline.

Rental Price

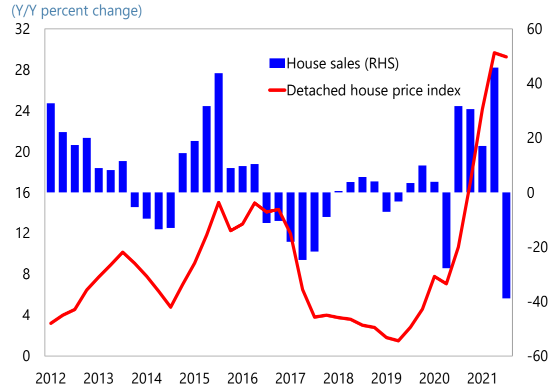
(Y/Y percent change)



A decline in sales suggests that the market has turned.

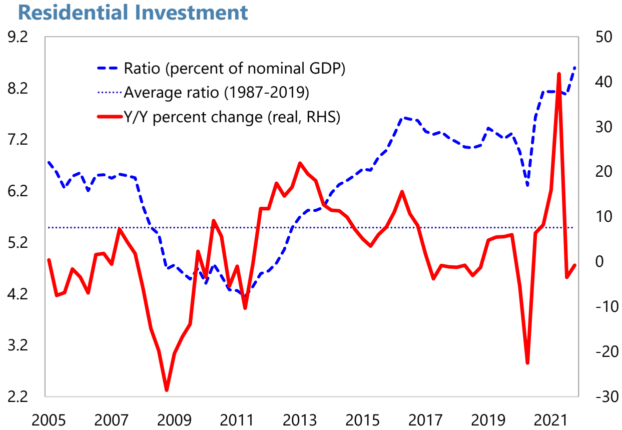
House Prices and Sales

(Y/Y percent change)



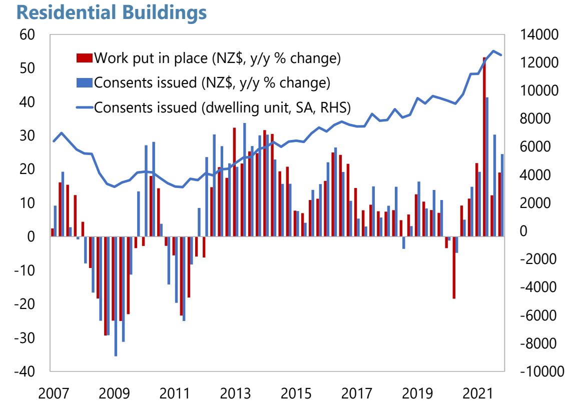
Residential investment has been volatile…

Residential Investment



…but there has been a significant increase in building consents issued.

Residential Buildings



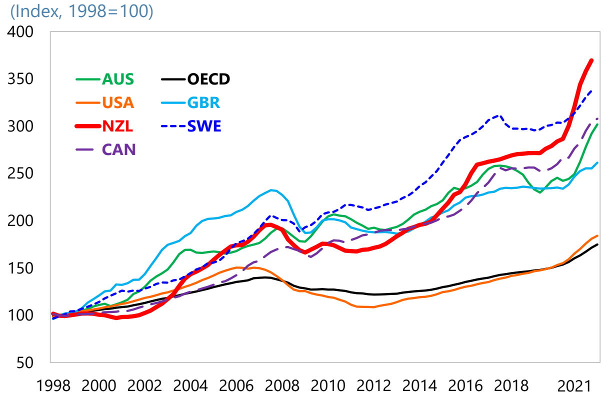
Sources: RBNZ; Haver Analytics; and IMF staff calculations.

Figure 6. Household Debt and Balance Sheet Risks Are Elevated

House price increases are well above the OECD…

Real House Prices in Selected OECD Countries

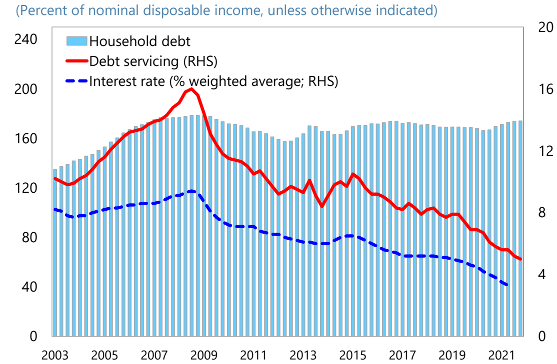
(Index, 1998=100)



…with household debt remaining elevated.

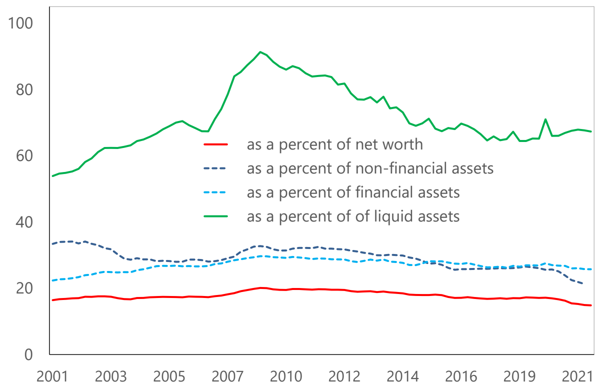
Household Debt and Debt Service

(Percent of nominal disposable income, unless otherwise indicated)



Household debt as a percentage of liquid assets has edged up again.

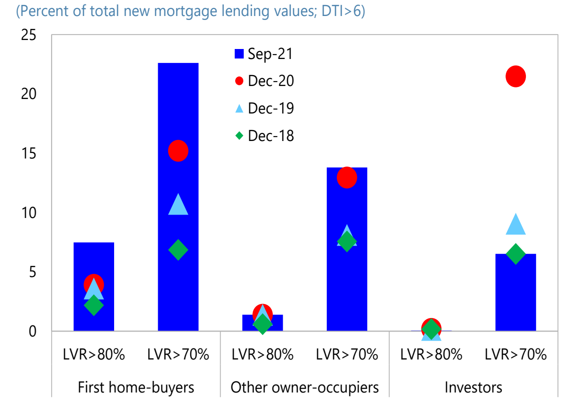
Household Debt



High debt-to-income loans now account for a smaller share of new loans among investors.

Share of High DTI Loans

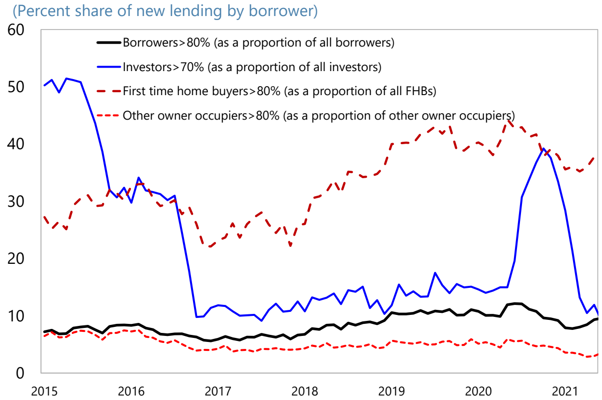
(Percent of total new mortgage lending values; DTI>6)



High loan-to-value ratio lending has moderated following macroprudential tightening, particularly among investors…

New Residential Mortgage Lending by High LVR

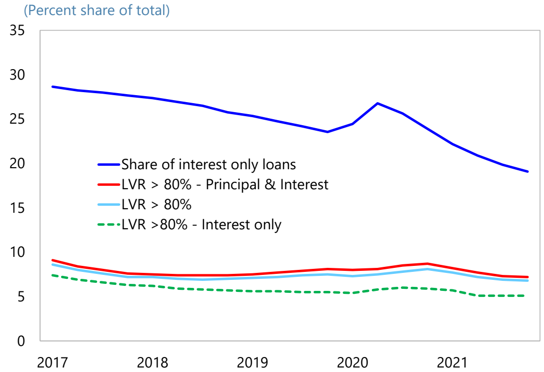
(Percent share of new lending by borrower)



… and the share of outstanding interest-only loans has gradually declined.

Existing Residential Mortgage Lending

(Percent share of total)

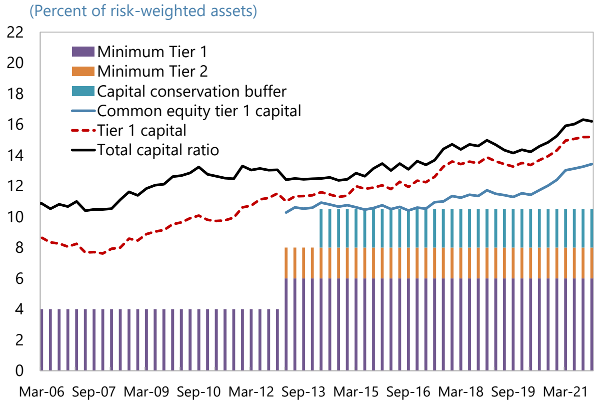


Sources: RBNZ; Stats NZ; OECD; and Haver Analytics.

Figure 7. The Banking Sector Weathered the COVID-19 Crisis Well

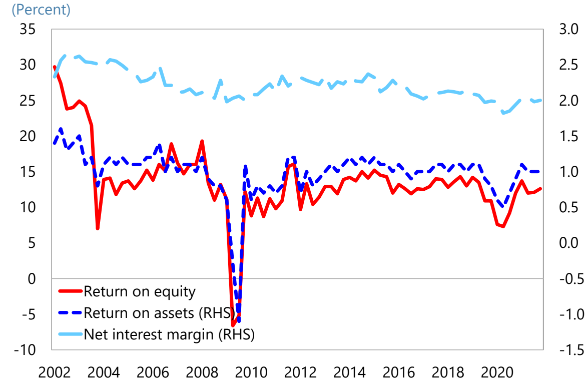
Banks are well capitalized…

Capital Ratios of Registered Banks
(Percent of risk-weighted assets)



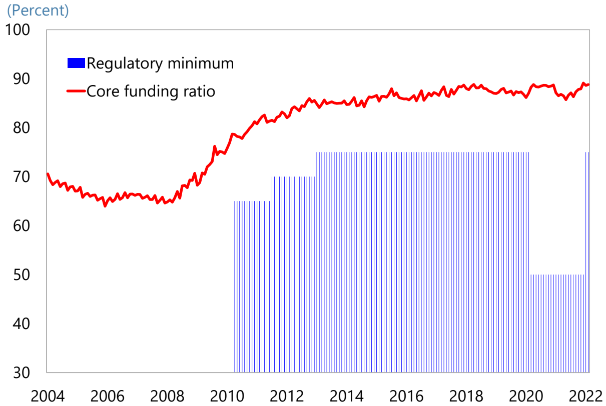
…while profitability has bounced back strongly after the initial lockdown

Profitability
(Percent)



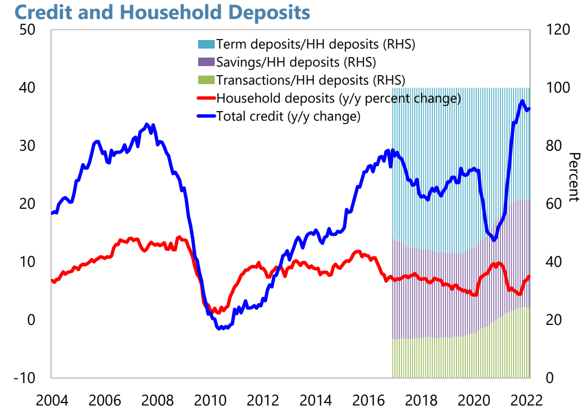
The core funding ratio is well above the regulatory minimum.

Core Funding Ratio
(Percent)



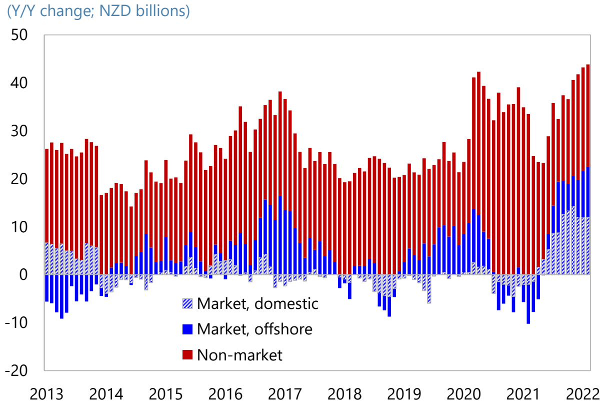
Household credit growth accelerated while low returns prompted a shift from term deposits.

Credit and Household Deposits



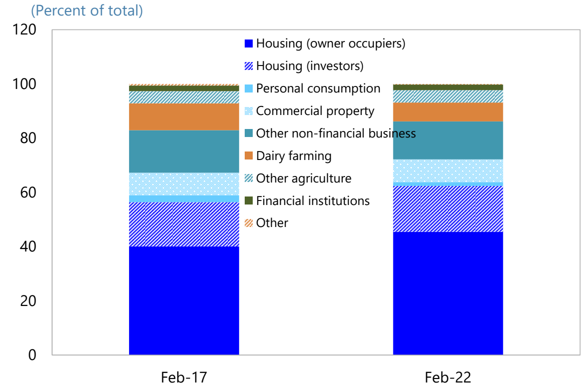
After relying on the RBNZ, banks are increasingly returning to market sources for wholesale funding.

Total Funding
(Y/Y change; NZD billions)



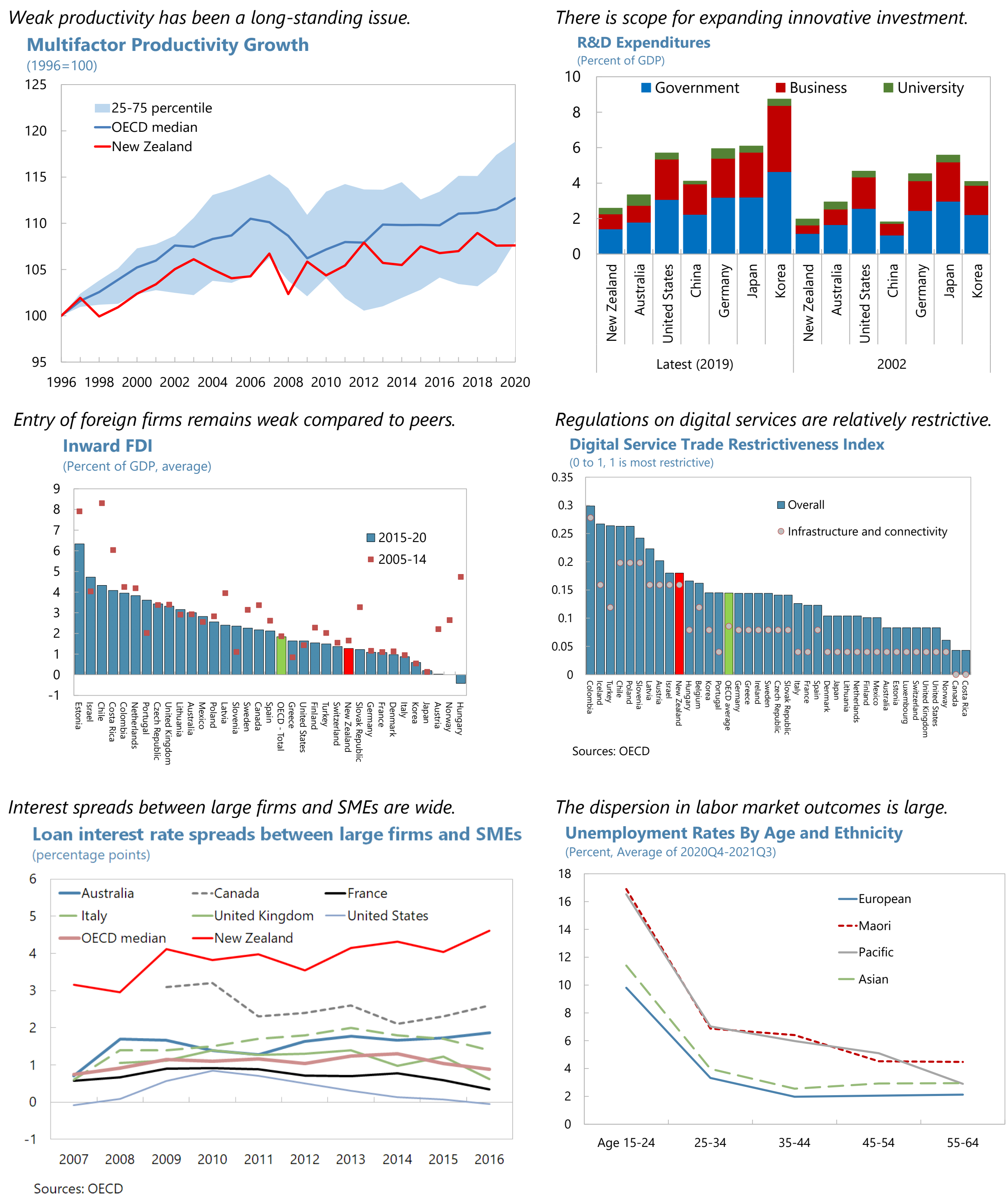
Banks' exposure to the housing sector continued to increase.

Loans by Purpose
(Percent of total)



Source: RBNZ.

Figure 8. Macro-Structural Opportunities



Sources: Stats NZ; OECD; and IMF staff calculations.

Table 1. New Zealand: Main Economic Indicators, 2017-27
(Annual percent change, unless otherwise indicated)

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
						Projections					
NATIONAL ACCOUNTS											
Real GDP (production)	3.5	3.4	2.9	-2.1	5.6	2.7	2.6	1.9	1.7	2.4	2.3
Real GDP (expenditure)	4.0	4.3	3.3	-0.9	5.0	1.9	2.6	1.9	1.6	2.4	2.2
Domestic demand	5.2	5.2	3.2	-1.9	9.6	3.8	1.3	2.4	2.3	2.0	2.1
Private consumption	5.5	4.6	3.2	-1.2	6.6	2.6	2.6	3.7	2.7	2.4	2.4
Public consumption	3.5	3.3	5.1	6.8	10.4	7.9	-1.4	-0.2	1.3	0.4	0.2
Investment	5.5	8.0	2.4	-10.1	16.6	0.7	0.5	1.5	2.1	2.4	2.9
Public	7.4	2.2	2.0	-6.8	6.9	-0.9	0.6	3.0	4.4	4.7	4.8
Private	3.8	8.0	5.1	-7.2	10.6	5.7	0.5	1.1	1.5	1.7	2.3
Private business	6.5	13.0	5.0	-8.9	10.5	6.6	0.1	1.3	1.3	1.5	3.1
Dwelling	-1.1	-1.6	5.4	-3.3	11.0	4.1	1.2	0.7	1.8	2.2	0.7
Inventories (contribution to growth, percent)	0.2	0.3	-0.5	-0.8	1.6	-1.0	0.0	0.0	0.0	0.0	0.0
Net exports (contribution to growth, percent)	-1.6	-1.2	0.0	1.7	-5.1	-2.3	1.1	-0.7	-0.9	0.2	-0.1
Real gross domestic income	5.4	3.7	3.3	-0.6	4.2	4.4	2.4	3.9	2.4	1.9	2.0
Investment (percent of GDP)	23.3	24.3	24.1	21.7	24.5	24.4	24.0	23.4	23.4	23.3	23.2
Public	5.5	5.4	5.3	5.0	5.1	5.0	4.9	4.9	5.0	5.0	5.1
Private	17.9	18.9	18.8	16.7	19.5	19.4	19.1	18.6	18.4	18.2	18.1
Savings (gross, percent of GDP)	20.5	20.3	21.2	20.8	18.7	17.9	18.6	19.2	19.2	19.1	18.9
Public	1.3	1.3	-2.5	-4.0	-4.9	-4.9	-1.8	-1.2	-0.4	0.1	0.1
Private	19.2	19.0	23.6	24.9	23.7	22.8	20.4	20.4	19.6	19.0	18.8
Potential output	3.0	3.0	3.1	1.6	1.5	1.9	2.5	2.5	2.5	2.5	2.5
Output gap (percent of potential)	0.5	0.9	0.7	-3.0	0.9	1.7	1.9	1.3	0.4	0.3	0.0
LABOR MARKET											
Employment	4.2	2.9	1.3	1.3	2.4	1.7	1.0	1.4	1.2	1.2	1.3
Unemployment (percent of labor force, ann. average)	4.7	4.3	4.2	4.6	3.8	3.6	3.9	3.9	4.1	4.3	4.4
Wages (nominal percent change)	2.6	3.0	3.4	3.8	3.8	4.9	4.6	3.7	3.5	3.7	3.3
PRICES											
Terms of trade index (goods and services, % change)	5.0	-1.4	0.1	1.2	-1.2	8.3	-2.0	5.2	1.2	-2.1	-1.6
Terms of trade index (goods, % change)	7.3	-1.8	0.4	2.3	1.7	9.1	-3.3	2.5	-1.4	-4.5	-5.1
Consumer prices (avg, % change)	1.9	1.6	1.6	1.7	3.9	5.9	3.5	2.4	2.2	2.1	2.0
GDP deflator (avg, % change)	3.3	1.3	2.4	2.2	2.9	5.7	4.1	3.4	3.0	2.8	2.5
MACRO-FINANCIAL											
Official cash rate (policy rate, percent, avg)	1.8	1.8	1.4	0.4	0.4	1.7	3.3	3.5	3.0	2.5	2.5
Credit to the private sector (percent change)	4.9	5.4	5.6	3.9	6.1	2.7	1.1	4.0	4.5	4.2	4.1
Interest payments (percent of disposable income)	8.0	8.0	8.0	6.0	6.2	8.4	8.6	8.5	8.3	8.0	7.9
Household savings (percent of disposable income)	3.3	3.2	3.4	3.6	3.6	3.2	2.7	2.5	2.4	2.3	2.3
Household debt (percent of disposable income)	171	169	169	170	174	165	156	155	154	152	151
GENERAL GOVERNMENT (percent of GDP) 1/											
Revenue	37.4	36.8	37.8	36.1	37.7	37.1	37.3	37.4	37.3	37.4	37.4
Expenditure	36.1	35.5	36.6	42.2	39.6	44.9	39.5	38.8	38.2	37.4	37.3
Net lending/borrowing	1.3	1.3	1.2	-6.1	-1.9	-7.7	-2.2	-1.4	-0.9	0.0	0.1
Operating balance	2.9	3.2	3.2	-4.3	-0.3	-5.1	0.6	1.7	1.9	2.3	2.4
Cyclically adjusted balance 2/	1.3	1.0	0.9	-4.8	-2.4	-7.5	-2.2	-1.8	-0.2	0.1	0.6
Gross debt	32.5	30.0	26.2	38.4	45.9	51.5	51.3	51.9	49.3	47.7	45.0
Net debt	6.0	5.2	4.3	9.6	10.4	19.2	20.8	22.1	20.3	19.3	16.8
Net worth	88.2	91.4	93.2	83.6	92.0	80.5	77.3	77.0	76.8	78.4	80.3
BALANCE OF PAYMENTS											
Current account (percent of GDP)	-2.8	-4.0	-2.9	-0.8	-5.8	-6.5	-5.3	-4.2	-4.2	-4.2	-4.3
Export volume	2.7	3.2	2.4	-12.9	-2.5	7.3	9.1	6.4	6.0	5.7	5.7
Import volume	7.3	6.4	2.1	-15.9	15.4	12.6	3.1	6.8	6.8	3.7	4.4
Net international investment position (percent of GDP)	-52.3	-56.2	-53.6	-55.6	-46.1	-49.2	-51.4	-53.0	-54.9	-56.3	-58.1
Gross official reserves (bn US$)	20.3	17.6	17.0	13.0	...	...	...	...	...	...	...
MEMORANDUM ITEMS											
Nominal GDP (bn NZ$)	286	303	320	324	350	377	403	425	444	468	490
Percent change	7.4	5.7	5.8	1.3	8.0	7.8	6.8	5.4	4.7	5.3	4.8
Nominal GDP per capita (US$)	42,271	42,767	42,321	41,418	48,413	49,835	52,957	54,996	56,324	58,227	60,042
Real gross national disposable income per capita (NZ$)	51,235	52,213	53,601	52,710	54,387	55,769	56,572	57,879	58,463	58,813	59,135
Percent change	2.3	1.9	2.7	-1.7	3.2	2.5	1.4	2.3	1.0	0.6	0.5
Population (million)	4.8	4.9	5.0	5.1	5.1	5.2	5.2	5.3	5.4	5.4	5.5
US$/NZ$ (average level)	0.711	0.693	0.659	0.650	0.708	...	...	...	...	...	...
Nominal effective exchange rate	111.1	106.8	105.2	103.8	109.0	...	...	...	...	...	...
Real effective exchange rate	107.4	102.9	101.4	100.6	107.2	...	...	...	...	...	...

Sources: Authorities' data and IMF staff estimates and projections.

1/ Fiscal year.

2/ In percent of potential GDP.

Table 2. New Zealand: Fiscal Accounts, 2016/17-2026/27 1/

(In percent of GDP, unless otherwise indicated)

	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27
						Projections					
GENERAL GOVERNMENT 2/											
Revenue	**37.4**	**36.8**	**37.8**	**36.1**	**37.7**	**37.1**	**37.3**	**37.4**	**37.3**	**37.4**	**37.4**
Tax revenue	31.0	30.6	31.7	30.4	32.6	32.4	32.7	32.3	32.2	32.2	32.2
Direct taxes	20.0	19.7	20.5	19.6	21.0	21.2	21.3	21.1	21.0	21.2	21.2
Individual and withholding	12.4	12.2	12.6	12.8	13.2	13.6	13.3	13.1	13.1	13.2	13.2
Corporate	5.6	5.5	6.0	4.8	5.8	5.7	6.1	6.0	5.9	6.1	6.1
Property	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Indirect taxes	11.0	10.9	11.2	10.8	11.6	11.2	11.4	11.2	11.1	11.0	11.0
Of which: GST	7.5	7.4	7.5	7.2	7.9	7.7	7.8	7.7	7.7	7.6	7.6
Non-tax revenue	6.4	6.2	6.1	5.7	5.1	4.7	4.5	5.0	5.1	5.2	5.2
Expenditure	**36.1**	**35.5**	**36.6**	**42.2**	**39.6**	**44.9**	**39.5**	**38.8**	**38.2**	**37.4**	**37.3**
Expense	34.5	33.6	34.7	40.4	38.0	42.2	36.6	35.7	35.4	35.0	34.9
Employee expenses	8.5	8.3	8.7	9.1	8.9	9.2	9.0	8.8	8.8	8.7	8.7
Other operating expenses (excl. depreciation)	5.4	5.3	5.5	5.6	5.8	7.3	6.2	5.7	5.6	5.5	5.5
Social benefits	13.6	13.3	13.9	14.7	15.2	15.4	14.4	14.3	14.4	14.4	14.3
Other transfers	3.2	3.1	3.0	7.4	4.5	6.8	3.3	3.1	2.8	2.8	2.8
Interest	1.5	1.4	1.4	1.2	1.1	1.1	1.3	1.3	1.4	1.3	1.3
Other	2.3	2.2	2.3	2.4	2.3	2.5	2.5	2.4	2.3	2.3	2.3
Net acquisition of nonfinancial assets	1.6	1.9	2.0	1.8	1.7	2.6	2.9	3.1	2.8	2.3	2.3
Of which: Gross fixed capital formation	3.7	3.7	4.0	3.9	3.9	4.6	4.0	3.8	3.4	3.3	3.3
Operating balance	2.9	3.2	3.2	-4.3	-0.3	-5.1	0.6	1.7	1.9	2.3	2.4
Primary balance	2.0	1.9	1.8	-5.5	-1.3	-7.0	-1.2	-0.4	0.1	1.0	1.1
Net lending (+)/borrowing (-)	**1.3**	**1.3**	**1.2**	**-6.1**	**-1.9**	**-7.7**	**-2.2**	**-1.4**	**-0.9**	**0.0**	**0.1**
GENERAL GOVERNMENT BALANCE SHEET 2/											
Liabilities	**60.7**	**57.3**	**57.6**	**73.1**	**76.4**	**81.9**	**79.3**	**79.0**	**75.1**	**72.7**	**68.8**
Gross debt	32.5	30.0	26.2	38.4	45.9	51.5	51.3	51.9	49.3	47.7	45.0
Other liabilities 3/	28.2	27.4	31.4	34.7	30.5	30.4	28.0	27.1	25.8	25.0	23.7
Assets	**148.9**	**148.7**	**150.9**	**156.7**	**168.4**	**162.4**	**156.6**	**156.1**	**151.9**	**151.1**	**149.0**
Financial assets	66.5	65.4	65.4	69.8	81.3	77.3	74.8	75.5	73.1	73.2	72.9
Debt relevant	26.6	24.8	22.0	28.8	35.5	32.3	30.5	29.9	29.0	28.3	28.2
Other	39.9	40.6	43.4	41.0	45.9	45.1	44.4	45.6	44.1	44.8	44.7
Nonfinancial assets	82.4	83.3	85.5	86.9	87.1	85.0	81.8	80.6	78.8	77.9	76.1
Net financial worth	**5.8**	**8.0**	**7.8**	**-3.3**	**4.9**	**-4.5**	**-4.4**	**-3.6**	**-2.0**	**0.5**	**4.2**
Net debt 4/	**6.0**	**5.2**	**4.3**	**9.6**	**10.4**	**19.2**	**20.8**	**22.1**	**20.3**	**19.3**	**16.8**
Central government	2.4	1.9	0.8	5.7	6.8	15.8	17.6	19.0	17.5	16.6	14.2
Local government	3.6	3.3	3.5	3.9	3.6	3.4	3.2	3.0	2.9	2.7	2.6
Net worth	**88.2**	**91.4**	**93.2**	**83.6**	**92.0**	**80.5**	**77.3**	**77.0**	**76.8**	**78.4**	**80.3**
Central government	44.5	49.0	50.6	40.0	50.0	40.4	39.7	40.9	42.3	44.9	48.2
Local government	43.7	42.3	42.6	43.6	42.0	40.1	37.7	36.1	34.4	33.5	32.1
MEMORANDUM ITEMS											
Cyclically adjusted balance (percent of potential GDP)	1.3	1.0	0.9	-4.8	-2.4	-7.5	-2.2	-1.8	-0.2	0.1	0.6
Fiscal impulse (change in CAB; in percent of potential GDP	-0.6	0.3	0.1	5.6	-2.3	5.1	-5.3	-0.4	-1.6	-0.3	-0.5
Change in real revenue (percent)	5.3	3.9	6.1	-3.8	10.2	-2.0	3.8	3.0	3.3	2.3	3.4
Change in real primary expenditure (percent)	3.1	4.2	6.9	17.2	-0.8	12.9	-9.8	0.9	1.6	0.0	3.1
New Zealand Superannuation Fund											
Budget transfers (+ = receipts)	0.0	0.2	0.3	0.5	0.6	0.7	0.5	0.5	0.5	0.5	0.5
Net assets	12.5	13.2	13.6	13.9	17.3	17.7	17.9	18.5	18.9	19.1	19.2
Contributed capital	5.4	5.2	5.3	5.6	5.8	6.2	6.2	6.4	6.5	6.7	6.8
Central government											
Revenue	34.1	33.4	34.4	32.7	34.5	34.2	34.3	34.4	34.3	34.4	34.4
Expenditure	32.6	32.0	33.0	38.4	36.5	41.9	36.6	35.9	35.2	34.4	34.3
Net lending (+)/borrowing (-)	1.5	1.4	1.4	-5.7	-2.0	-7.7	-2.2	-1.4	-0.9	0.0	0.1
Local government											
Revenue	3.9	4.0	4.0	4.1	3.9	3.9	3.9	3.9	3.9	3.9	3.9
Expenditure	4.1	4.1	4.3	4.5	3.9	3.9	3.9	3.9	3.9	3.9	3.9
Net lending (+)/borrowing (-)	-0.2	-0.1	-0.2	-0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
GDP (in billion NZ$)	276	296	310	319	343	362	390	412	437	455	480

Sources: Authorities' data and IMF staff estimates and projections.

1/ The fiscal year runs from July to June.

2/ Accrual basis; GFS. Comprises Core Crown (excludes RBNZ), Crown entities, and local governments. Includes New Zealand Superannuation Fund.

3/ "Other liabilities" include government pension liabilities, and the Accident Compensation Corporation (ACC) liabilities.

4/ "Net debt" is gross debt less debt-relevant financial assets - cash and equivalents, marketable securities, etc. (often held to cover pension liabilities).

Table 3. New Zealand: Balance of Payments, 2017-27
(In percent of GDP, unless otherwise indicated)

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
								Projections			
Current account	-2.8	-4.0	-2.9	-0.8	-5.8	-6.5	-5.3	-4.2	-4.2	-4.2	-4.3
Balance on goods and services	1.1	-0.2	0.0	1.3	-3.3	-3.2	-2.4	-1.0	-1.0	-1.0	-1.1
Exports of goods and services	27.4	27.8	27.4	24.1	22.1	26.6	27.2	27.6	27.9	28.0	28.3
Exports of goods	18.8	19.1	18.8	18.4	18.2	22.5	22.2	21.3	20.6	19.8	18.8
Exports of services	8.6	8.7	8.6	5.7	4.0	4.1	5.1	6.3	7.3	8.2	9.5
Imports of goods and services	26.3	27.9	27.4	22.8	25.4	29.9	29.6	28.6	28.9	29.1	29.4
Imports of goods	19.6	20.8	20.0	17.4	19.9	23.1	22.8	22.1	22.3	22.4	22.7
Imports of services	6.8	7.1	7.4	5.4	5.5	6.7	6.8	6.6	6.6	6.7	6.7
Primary income, net	-3.7	-3.6	-2.6	-1.6	-2.0	-3.2	-2.8	-3.0	-3.1	-3.0	-3.1
Inflows	3.0	2.9	2.9	2.7	2.9	2.8	2.8	2.8	2.8	2.8	2.8
Outflows	6.7	6.5	5.5	4.3	4.9	5.9	5.6	5.8	5.9	5.8	5.9
Secondary income, net	-0.1	-0.1	-0.2	-0.3	-0.3	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Inflows	0.8	0.9	0.8	0.6	0.5	0.8	0.7	0.6	0.7	0.6	0.6
Outflows	0.9	1.0	1.0	0.9	0.9	0.9	0.8	0.8	0.8	0.8	0.7
Capital and financial account											
Capital account, net	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account, net	-0.9	-1.1	-2.2	-2.3	-3.4	-6.5	-5.3	-4.2	-4.2	-4.2	-4.3
Direct investment	-1.2	-0.9	-2.1	-1.6	-2.2	-3.1	-2.6	-2.1	-2.0	-2.1	-2.0
Equity	-1.6	-0.4	-2.5	-1.6	-2.1	-2.3	-2.0	-1.6	-1.5	-1.6	-1.5
Debt	0.3	-0.5	0.4	0.1	0.0	-0.8	-0.6	-0.5	-0.5	-0.5	-0.5
Portfolio investment	0.1	0.0	1.8	4.4	-2.7	-2.2	-1.8	-1.4	-1.5	-1.4	-1.5
Equity	0.7	-0.2	1.2	1.4	3.4	1.5	1.3	1.1	0.9	1.1	0.9
Debt	-0.7	0.2	0.6	3.1	-6.0	-3.7	-3.1	-2.5	-2.4	-2.5	-2.4
Financial derivatives	0.4	1.0	-0.6	-2.4	0.0	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1
Other investment	-1.0	-0.1	-1.1	-0.6	0.2	-1.5	-1.2	-1.0	-0.9	-1.0	-1.0
Reserve assets	0.9	-1.1	-0.2	-2.1	1.3	...	...	...	...	...	...
Net errors and omissions	1.9	2.9	0.8	-1.4	2.4	0.0	0.0	0.0	0.0	0.0	0.0
BALANCE SHEET											
Net international investment position	-52.3	-56.2	-53.6	-55.6	-46.1	-49.2	-51.4	-53.0	-54.9	-56.3	-58.1
Equity, net	-1.0	-4.6	-5.8	-8.4	3.8	2.6	1.8	1.2	0.6	0.0	-0.6
Assets	40.2	37.7	42.6	47.2	56.6	56.6	56.6	56.6	56.6	56.6	56.6
Liabilities	41.2	42.3	48.4	55.6	52.9	54.0	54.8	55.4	56.1	56.6	57.2
Debt, net	-61.6	-60.2	-56.1	-53.1	-56.6	-58.6	-60.0	-61.0	-62.2	-63.1	-64.2
Assets	39.9	40.0	40.1	45.0	35.8	35.8	35.8	35.8	35.8	35.8	35.8
Liabilities	101.5	100.3	96.2	98.1	92.4	94.4	95.8	96.8	98.0	98.9	100.0
External assets (gross)	90.3	86.4	91.0	98.0	99.2	99.2	99.2	99.2	99.2	99.2	99.2
Equity	40.2	37.7	42.6	47.2	56.6	56.6	56.6	56.6	56.6	56.6	56.6
Debt	39.9	40.0	40.1	45.0	35.8	35.8	35.8	35.8	35.8	35.8	35.8
External liabilities (gross)	142.6	142.6	144.6	153.7	145.3	148.4	150.6	152.2	154.1	155.5	157.3
Equity	41.2	42.3	48.4	55.6	52.9	54.0	54.8	55.4	56.1	56.6	57.2
Debt	101.5	100.3	96.2	98.1	92.4	94.4	95.8	96.8	98.0	98.9	100.0
Of which: NZ$ denominated	57.0	52.5	51.2	52.0	49.2	50.3	51.0	51.6	52.2	52.7	53.3
FX denominated	44.6	43.8	43.3	53.3	43.2	44.1	44.8	45.2	45.8	46.2	46.8
Short-term	29.7	34.2	29.5	33.5	30.2	30.8	31.3	31.6	32.0	32.3	32.7
MEMORANDUM ITEMS											
Gross official reserves (bn NZ$)	20.3	17.6	17.0	13.0	16.4	...	...	...	...	...	...
In months of prospective imports	4.1	3.6	4.3	2.6	2.5	...	...	...	...	...	...
In percent of short-term external debt	34.3	25.4	28.0	17.5	22.3	...	...	...	...	...	...

Sources: Authorities' data and IMF staff estimates and projections.

Table 4. New Zealand: Monetary and Financial Sector, 2017-27
(In billions of NZ$, unless otherwise indicated)

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
						Projections					
CENTRAL BANK											
Net foreign assets	24	22	19	11	14	16	17	18	19	19	21
Net domestic assets	-9	-8	-4	27	39	22	2	-5	-5	-6	-8
Net domestic claims	-1	-4	0	31	43	26	6	-1	-1	-2	-3
Claims on Central government (net)	-2	-5	-1	29	34	21	5	-1	-1	-2	-3
Claims on Other Depository Corporations	0	0	1	2	9	5	1	0	0	0	0
Other items net	-8	-3	-4	-3	-4	-4	-4	-4	-4	-5	-5
Monetary base	15	15	15	38	54	38	19	13	13	13	13
DEPOSITORY CORPORATIONS											
Net foreign assets	-76	-80	-91	-100	-109	-119	-126	-133	-140	-147	-155
Net domestic assets	369	391	417	466	498	532	543	565	594	623	654
Net domestic claims	436	459	489	544	576	619	634	661	695	730	767
Claims on Central government (net)	7	7	12	49	50	41	25	19	19	18	17
Claims on State and Local Government	6	7	8	10	7	8	9	9	10	10	11
Claims on Public Nonfinancial Corporations	1	1	1	2	2	2	2	2	2	3	3
Claims on Private Sector	412	434	459	473	505	555	585	617	649	684	720
of which: Private Sector Credit	410	432	456	469	504	555	585	617	649	684	720
Claims on Other Financial Corporations	9	9	10	12	11	13	13	14	15	16	16
Other items net	-67	-67	-72	-79	-79	-87	-91	-96	-101	-107	-113
Broad money	293	311	326	366	389	413	417	432	454	476	499
MEMORANDUM ITEMS											
Private sector credit 2/	429	452	477	496	526	556	562	584	611	637	663
Housing loans 1/	242	256	274	296	326	338	337	354	373	390	409
Business loans 1/	103	108	115	109	116	132	138	143	150	157	162
Household deposits	167	177	185	203	217	239	252	265	278	290	309
					In percent of GDP						
Private sector credit 2/	150	149	149	153	150	144	138	136	136	135	132
Housing loans 1/	84	85	85	91	93	87	83	82	83	83	82
Business loans 1/	36	36	36	34	33	34	34	33	33	33	32
Household deposits	58	59	58	63	62	62	62	62	62	62	62
					Percentage change						
Private sector credit 2/	4.9	5.4	5.6	3.9	6.1	5.6	1.1	4.0	4.5	4.2	4.1
Housing loans 1/	5.5	5.9	6.9	8.2	10.1	3.8	-0.4	5.1	5.3	4.6	5.1
Business loans 1/	6.1	5.0	6.5	-5.3	5.8	14.0	5.0	3.4	4.6	4.9	3.4
Household deposits	7.1	6.2	4.4	9.8	6.7	10.1	5.5	5.3	4.7	4.6	6.4

Sources: RBNZ and IMF staff calculations.
1/ Registered banks.
2/ Depository corporations.

Table 5. New Zealand: Financial Soundness Indicators, 2017-21

	2017	2018	2019	2020	2021
Interest rates (percent end-year)					
90-day bank bill rate	2.0	1.9	1.5	0.5	0.5
90-day bank bill rate, real	0.1	0.3	-0.1	-1.2	-3.3
Stock market index (percent change, end-year)	22.0	4.9	30.4	13.9	-0.7
Liquidity and funding (in percent)					
Liquid assets to total assets	13.3	13.3	13.5	17.0	16.8
Liquid assets to short-term liabilities	20.0	19.8	20.4	25.1	24.2
1-month maturity mismatch	7.4	7.2	6.7	6.8	7.4
Core funding ratio	88.7	87.0	86.8	88.5	89.1
Asset composition (percentage share of total)					
Agricultural	14.1	13.9	13.2	12.7	11.7
Business	25.1	25.0	25.2	23.5	23.2
Households	60.7	61.1	61.5	63.8	65.1
Of which: Housing	56.9	57.3	58.0	60.8	62.5
Asset quality (in percent)					
Non-performing loans to total loans	0.5	0.5	0.6	0.6	0.4
Non-performing loans net of provisions to capital	n.a.	0.7	2.3	-0.1	-0.8
Non-performing loans (in millions of NZ$)	2,296	3,686	4,483	4,827	3,603
Capital adequacy (in percent)					
Regulatory capital to risk-weighted assets	14.7	15.0	14.4	15.2	16.2
Tier I capital to risk-weighted assets	13.6	13.9	13.5	14.3	15.2
Common equity tier 1 to risk-weighted assets	11.4	11.7	11.5	12.4	13.4
Capital to assets	7.7	7.7	7.7	7.6	7.8
Profit Ratios (in percent)					
Return on assets	1.1	1.0	0.8	0.9	1.0
Return on equity	13.9	13.0	10.9	12.0	12.6
Net interest margin	2.1	2.1	2.0	1.9	2.0

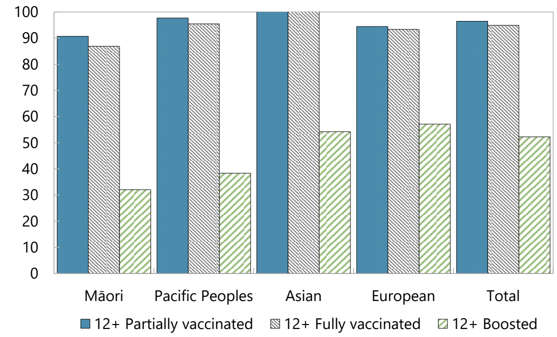
Sources: RBNZ; and IMF staff estimates.

Note: Capital adequacy measures, NPLs net of provisions to capital, liquid assets, 1-month mismatch ratio, core funding ratio, and return on equity are calculated for locally incorporated banks only.

Annex I. Reopening Strategy

1. New Zealand has transitioned to the COVID-19 protection framework to manage outbreaks without needing to rely on hard lockdowns. New Zealand was initially successful at completely eliminating the virus through strict lockdowns. However, with the arrival of the more contagious Delta variant, even a protracted lockdown in Auckland starting in August 2021 was not successful at extinguishing the virus completely. As a result, the authorities abandoned their strict elimination policy in December 2021, in favor of a living-with-COVID strategy, enabled by the rapid progress with vaccinations (more than 95 percent of the 12+ population is fully vaccinated, albeit with some gaps, particularly among the Māori).

Vaccinations by Ethnicity
(Percent of 12+ population)



Source: New Zealand Ministry of Health.

2. The framework is designed to minimize the impact and provide protection from COVID-19 through a "traffic light" system. The goal is to keep the spread and hospitalizations low by containing and controlling outbreaks. Protection emphasizes vaccination (including use of vaccine passes), infection prevention and control, and general public health measures such as contact tracing, case management, and testing. The system's three settings are designed to ensure that cases do not get to a point where they would stress the health system. A green designation imposes few restrictions, orange requires mask wearing and distancing, while red entails limits to gathering sizes even with vaccination certificates. Under the framework, localized lockdowns and protections can be used to control high rates of transmission.

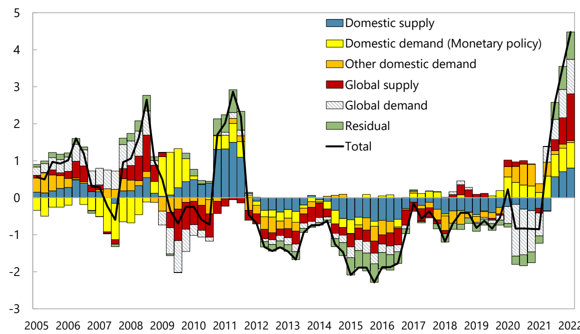
3. The border has begun reopening after having been closed to non-residents since March 2020. Since March 4, arriving citizens no longer need to go through managed isolation facilities. On April 12, the border re-opened for permanent residents, international students, and Australian citizens. On May 1, the border will reopen for travelers from visa-waiver countries such as the large tourist markets of the UK, US, Japan, Germany, Korea and Singapore. It is also expected that the reopening date for non-visa waiver travelers (currently October) will be brought forward.

Annex II. Drivers Behind the Surge in New Zealand's Inflation[1]

1. **New Zealand's inflation has been elevated above the target range, with inflation expectation increased.** Inflation in New Zealand stood at 6.9 percent in 2022Q1, well above the RBNZ's inflation 1-3 percent target range. Inflation expectations by households and firms have increased, particularly in the short-term, potentially feeding back into actual inflation.

2. **Both domestic and global factors have been affecting inflation.** An empirical study finds that the large increase in inflation reflects the combination of both global and domestic inflationary pressure, with global factors playing a larger role in recent quarters.[2] On global factors, intensified supply disruptions and a recovery in global demand have contributed to a recent sharp increase in inflation. In addition, domestic supply disruptions due to the resurgence of the pandemic and prolonged border restrictions have added inflationary pressure, while domestic demand fueled by accommodative monetary policy also has played a role.

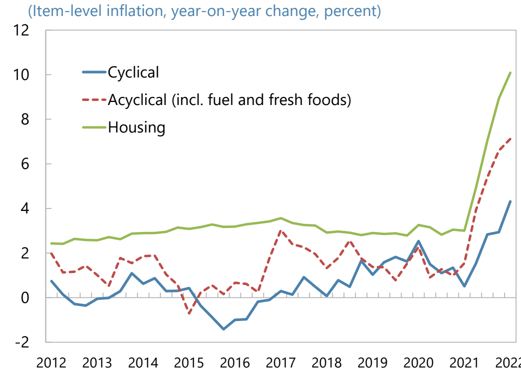
Both Global and Domestic Factors are Affecting Inflation
(Y-on-y inflation, deviation from trend, percentage point)



Source: IMF Staff estimates.

3. **At the item level, both acyclical and cyclically sensitive items have been contributing to high inflation.** As price increases for some categories of goods and services are relatively more responsive to the business cycle, a closer look at granular item-level inflation sheds light on drivers of inflation and underlying economic conditions. In this episode, housing and less cyclically sensitive items have been the chief factors contributing to high inflation, although prices for cyclically sensitive items also rose, reflecting the tight labor market and strong economic recovery.

Both Cyclical and Acyclical Inflation Are Rising
(Item-level inflation, year-on-year change, percent)



Source: IMF Staff estimates.

4. **Monetary policy should be calibrated carefully to anchor expectations.** With both cyclically sensitive inflation and acyclical inflation picking up, the ongoing normalization of monetary policy is appropriate. Going forward, the feedback effects from actual inflation to inflation expectations should be carefully monitored. A tightening at a faster pace would be warranted if risks of de-anchoring of inflation expectations increased.

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[1] Based on an accompanying Selected Issues Paper.

[2] The historical decomposition is based on a theoretically motivated structural vector autoregression model with sign and zero restrictions similar to Forbes and others (2020).

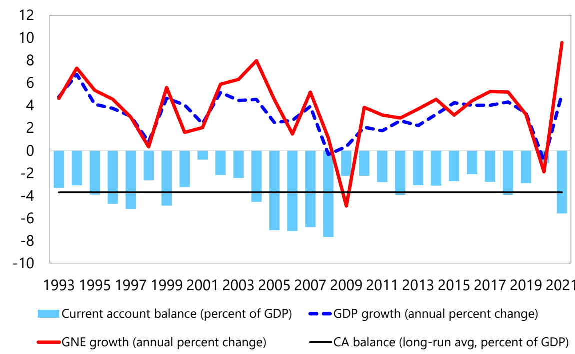
Annex III. External Sector Assessment

Based on preliminary estimates, New Zealand's external position in 2021 was broadly in line with fundamentals and desired policy settings, after accounting for the extraordinary impact of the pandemic on the tourism sector. The real effective exchange rate (REER), however, remains above its long-term average.

1. New Zealand has historically run current account (CA) deficits, averaging close to 4 percent of GDP over the past few decades. These deficits reflected a long-standing structural savings-investment imbalance and have resulted in a sizable negative net international investment position (NIIP). New Zealand's NIIP stood at -46.1 percent at the end of 2021, contracting from -55.7 percent of GDP at the end of 2020.

2. The economic rebound led to an increase in the CA deficit in 2021. Both real exports and imports had declined during the initial phase of the pandemic in 2020, with imports declining more than exports, reining in the current account deficit to an abnormally low level. However, the rebound in domestic demand in 2021, coupled with a precautionary inventory buildup as a result of global supply chain disruptions, led to a surge in imports. Despite supportive international prices and an improvement in the terms of trade, exports remained subdued, given growth setbacks in trading partners and unfavorable weather conditions. Tourism suffered in particular, given continuing border closures. The primary income deficit also widened as portfolio flows increased. Overall, this resulted in a widening of the current account deficit to 5.8 percent of GDP.

Current Account Balance and Growth

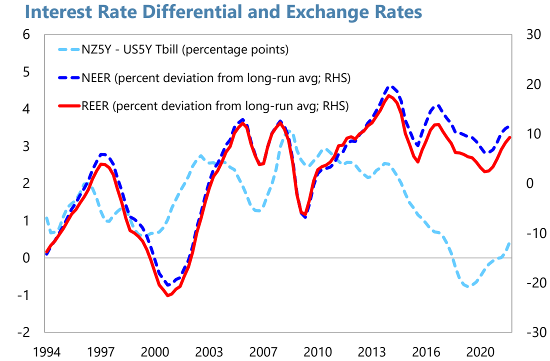


Sources: Haver Analytics; and IMF staff calculations.

3. Model estimates suggest that New Zealand's external position in 2021 was broadly in line with fundamentals and desirable policies.

- **New Zealand's REER appreciated to around 10 percent above its long-term average in 2021, consistent with the rebound in the domestic economy.** The REER reversed its depreciating trend witnessed over the last few years and appreciated in 2021 to reach levels last seen during 2017. The trend mirrors the increase in the interest differential and the fast economic rebound.

Interest Rate Differential and Exchange Rates



Sources: Haver Analytics; and IMF staff calculations.

- **The EBA current account regression suggests that the current account deficit in 2021 was at about the level implied by fundamentals and desired policy settings.** The estimated cyclically adjusted CA norm for 2021 was -1.6 percent of GDP. The estimated underlying, cyclically adjusted CA balance was -2.6 percent, taking into consideration the temporary compression in tourism inflows (1.7 percent), an increase in transportation and shipping costs (0.5 percent), a shift in consumption patterns towards durables (0.2 percent), increase in medical imports (0.2 percent) and cyclical factors (0.6 percent). This gives an estimated CA gap of -1.0 percent of GDP. Applying the EBA-estimated elasticity of the current-account-to-GDP ratio with respect to the REER of -0.2 to this gap results in an estimated currency overvaluation of less than 5 percent (text table).

- **The EBA REER index and level regressions suggest that the New Zealand dollar was overvalued in real effective terms in 2021.** The models imply that, in real effective terms, the dollar was overvalued by 15.6 percent and 9.2 percent respectively.

EBA Real Exchange Rate Assessments

	2019	2020	2021
REER index regression	8.2	6.5	15.6
REER level regression	0.3	-2.8	9.2
Current account regression 1/	9.0	1.4 [2/]	5.0 [2/]
External sustainability 1/	1.9	-6.4 [2/]	-3.0 [2/]
Summary			
Mean	4.9	-0.3	6.7
Median	5.1	-0.7	7.1

Note: figures show percent deviation from level implied by fundamentals and desired policy settings. +ve sign indicates actual REER is stronger than the predicated level.

1/ The underlying current account balance was also lowered by 2.6 percent to account for the temporary impact of the COVID-19 pandemic, largely reflecting the transitory impact of lower tourism inflows (1.7 percent), increase in transportation costs (0.5 percent), an increase in imports of tradeables due to a change in expenditure patterns (0.2 percent), and increase in medical imports (0.2 percent).

2/ CA/GDP to REER elasticity is estimated to be -0.2.

- **The NIIP level and trajectory are on course to narrow over the medium term**. The External Stability approach suggests that the NIIP would be stabilized at current levels with a CA deficit of 3.2 percent of GDP, which when compared with the cyclically adjusted CA deficit for 2021 (see above), gives an estimated gap of 0.6 percent. This implies that the currency is estimated to be undervalued by around 3 percent. The structure of New Zealand's external balance sheet reduces the vulnerability associated with its large negative NIIP. Since external NIIP liabilities are mainly in New Zealand dollars and there is a net foreign currency asset position, a nominal depreciation tends to strengthen the external balance sheet, all else equal. The banking sector has a net foreign currency liability position, but it is fully hedged. Further, the temporary provision of significant domestic funding to commercial banks from the RBNZ as a response to the pandemic significantly reduced banks' near-term needs for external financing.

4. **There is an unusually high level of uncertainty surrounding the current assessment, but overall results indicate that the external position is broadly in line with fundamentals and desired policy settings.** The results from the various approaches indicate an average overvaluation of around 6.7 percent, close to the results of the current account model. On balance, the current account model likely provides a reliable assessment of the external position, especially with the use of multilaterally consistent adjustors to account for the temporary but extraordinary impact of the pandemic. However, it is possible that the pandemic may have lasting effects on the tourism industry and consumption patterns, requiring adjustments over the medium term.

5. **Other considerations**. The New Zealand dollar has been floating since 1985. The central bank undertook a brief but large intervention in 2007–08 when the market for New Zealand dollars became illiquid following banking sector disruptions in the United States. The authorities are strongly committed to a floating regime, which reduces the need for reserve holdings.

Annex IV. Risk Assessment Matrix[1]

	Source of risks	Likelihood	Time horizon	Impact	Policies to reduce impact
	COVID-Related Risks				
	Outbreaks of lethal and highly contagious COVID-19 variants, either domestic or global, lead to resurgence of the pandemic and subpar/volatile growth and increased divergence across countries	**H**	Short to medium term	**H** Setbacks to the recovery from economic disruptions related to domestic containment measures or from a longer-than-expected border closure affecting tourism and education exports and migration flows.	In addition to using available policy space to deliver monetary and fiscal relief, calibrate reopening strategy in light of international developments.
	Milder COVID-19 outbreak, faster containment or economic impact as households and businesses learn to live with the virus	**M**	Short to medium term	**M** Stronger-than-expected private consumption and investment, together with early resumption of tourism and migration, will boost growth.	Speed up unwinding of stimulus.
	Other Risks: External				
	Extended global supply chains disruptions caused by COVID-19 lockdowns and logistical bottlenecks	**H**	Short to medium term	**H** Disruptions and bottlenecks could continue until 2023, resulting in shortages of intermediate and final consumer goods, growth slowdown, and price surges.	Encourage private sector to build inventories and calibrate policy mix to adjust.
	Further increase in level and volatility of food and energy prices amid pent-up demand and supply disruptions, or conflicts.	**H**	Short to medium term	**M** This would put additional pressure on inflation, interacting with other global risks such as supply chain disruptions and geopolitical tensions.	In case of a large shock, assess the need for policies to mitigate the adverse social impact. Assess impacts on inflation expectations and adjust monetary policy accordingly.
	Abrupt growth slowdown in China, either due to financial strains in the real estate market or COVID-19 outbreaks	**M**	Short to medium term	**M** China has emerged as a dominant export destination and an abrupt growth slowdown there will result in significant spillovers.	Reduce pace of unwinding monetary and fiscal policy stimulus.
	Other Risks: Domestic				
	De-anchoring of inflation expectations given tight labor markets and rising and volatile global food and energy prices	**L**	Short to medium term	**H** De-anchoring of inflation expectations could lead to costly price-wage spiral	Speed up monetary tightening if inflation expectations show signs of de-anchoring
	Large decline in housing prices	**M**	Short to medium term	**M** This could have severe effects on growth, residential investment, private consumption, and balance sheets, considering macrofinancial spillovers and interactions with higher mortgage rates.	A moderation in the pace of monetary tightening and relaxation of some MPMs, coupled with close monitoring of bank capital.

[1] Based on the January 2022 Global Risk Assessment Matrix (G-RAM).

	Source of risks	**Likelihood**	**Time horizon**	**Impact**	**Policies to reduce impact**
	Higher frequency and severity of natural disasters related to climate change	**M/L**	Medium term	**H** Stronger and more frequent economic disruptions. Larger fiscal costs related to disaster recovery and adaptation.	Combined monetary, fiscal policy easing; review medium-term fiscal framework to explicitly build in buffers.

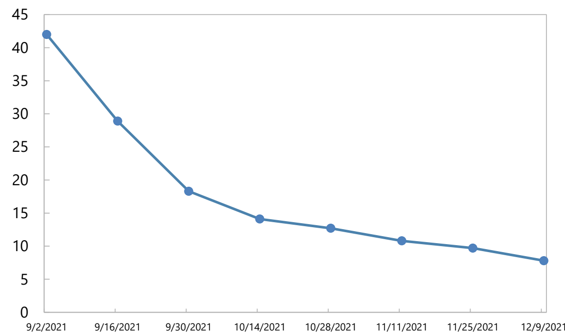
Annex V. New Zealand's Fiscal Support Measures in Response to the Resurgence of COVID-19

1. **New Zealand responded to initial waves of COVID-19 in 2020 utilizing its ample fiscal space.** The government's initial support measures centered on the large-scale wage subsidy program, which was part of a NZ$62.1 billion (19.2 percent of 2020 GDP) fiscal package. The scheme covered more than 60 percent of workers during the lockdowns in 2020.

2. **The government deployed contingency support measures in response to the resurgence of COVID-19 in 2021.** The contingency measures announced in December 2020 allowed the government to respond swiftly to the resurgence of COVID-19 in 2021:

- **Wage Subsidy Scheme.** In December 2020, the government introduced a new wage subsidy scheme linked to its health alert system. Firms experiencing or projected to experience at least a 40 percent decline in revenue during lockdowns were eligible. The payment was initially provided to more than 40 percent of workers at the beginning of the 2021 lockdowns, with the total fiscal cost in FY2021/22 amounting to NZ$5.4 billion

Wage Subsidy Scheme Cushioned Impact of COVID-19
(Proportion of workers received wage subsidies, percent)



Source: MSD.

- **Resurgence Support Payment.** The payment provided support to firms which experienced a sharp revenue loss due to a change in the government's health alert level. Businesses were eligible if they experienced a 30 percent drop in revenue after New Zealand's health alert level increase. The total fiscal cost in FY2021/22 amounts to NZ$3.2 billion.

- **Leave Support Scheme and Short-Term Absence Payment.** The schemes provide a payment to businesses to pay their workers who have to self-isolate (due to COVID-19 infections or waiting for test results) and cannot work from home.

3. **With a rise in the vaccination rate and shift to new health framework, the government has shrunk its support measures appropriately.** The government has terminated the Wage Subsidy Scheme and Resurgence Support Payment along with the COVID-19 Protection Framework. Although these shifts are appropriate as the need for large scale policy has waned at the current conjecture, the authorities should stand ready to act swiftly and provide targeted additional support if COVID-related downside risks materialize. In this respect, the recent introduction of temporary COVID Support Payments targeted to businesses severely affected by the resurgence of COVID-19 triggered by the Omicron variant was appropriate.

Annex VI. Public Debt Sustainability Analysis

Figure 1. New Zealand Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

(in percent of GDP unless otherwise indicated)

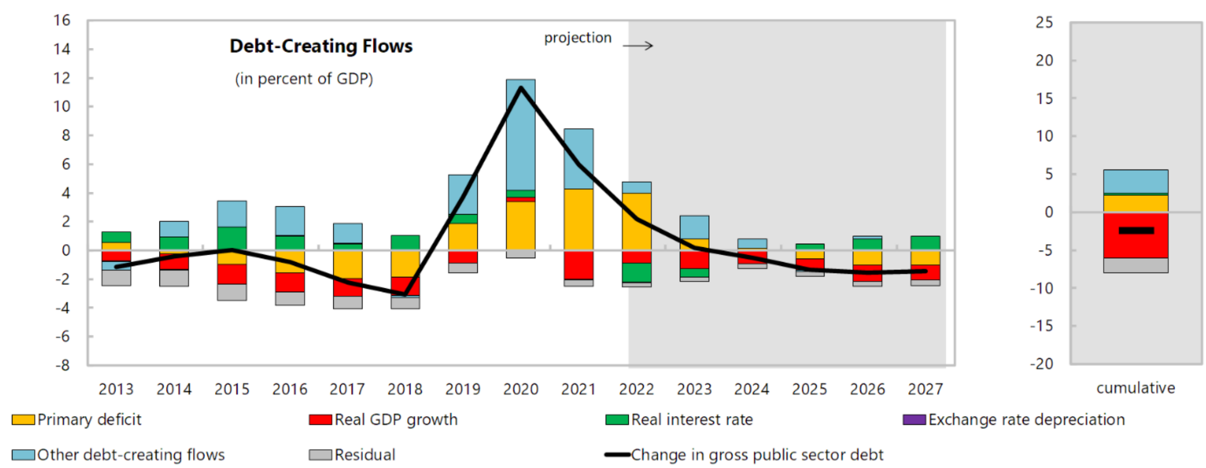
Debt, Economic and Market Indicators [1]

	Actual			Projections					
	2011-2019 [2]	2020	2021	2022	2023	2024	2025	2026	2027
Nominal gross public debt	33.1	43.1	49.1	51.3	51.5	51.0	49.6	48.1	46.7
Public gross financing needs	1.0	4.1	5.1	5.4	8.9	6.5	8.6	4.1	5.0
Net public debt	7.0	10.2	15.0	20.1	21.5	21.6	20.9	19.8	18.3
Real GDP growth (in percent) [4]	3.3	-0.9	5.0	1.9	2.6	1.9	1.6	2.4	2.2
Inflation (GDP deflator, in percent)	1.9	2.2	2.9	5.7	4.1	3.4	3.0	2.8	2.5
Nominal GDP growth (in percent)	5.3	1.3	8.0	7.8	6.8	5.4	4.7	5.3	4.8
Effective interest rate (in percent) [5]	5.3	3.8	2.8	2.9	2.9	3.5	4.0	4.6	4.8

As of March 30, 2022		
Sovereign Spreads		
Bond Spread (bp) 3/	-64	
5Y CDS (bp)	19	
Ratings	Foreign	Local
Moody's	Aaa	Aaa
S&Ps	AA+	AAA
Fitch	AA	AA+

Contribution to Changes in Public Debt

	Actual			Projections							
	2011-2019	2020	2021	2022	2023	2024	2025	2026	2027	cumulative	debt-stabilizing primary balance [10]
Change in gross public sector debt	0.2	11.3	6.0	2.2	0.2	-0.5	-1.3	-1.5	-1.4	-2.4	0.0
Identified debt-creating flows	1.2	11.8	6.4	2.5	0.5	-0.2	-1.0	-1.2	-1.1	-0.4	
Primary deficit	0.1	3.4	4.2	4.0	0.8	0.1	-0.6	-1.0	-1.1	2.2	
Primary (noninterest) revenue and grants	36.3	37.1	37.2	36.8	36.8	36.9	37.1	37.0	36.2	220.8	
Primary (noninterest) expenditure	36.4	40.5	41.5	40.7	37.6	37.1	36.5	36.0	35.2	223.1	
Automatic debt dynamics [6]	0.0	0.8	-2.1	-2.2	-1.9	-0.9	-0.3	-0.3	0.0	-5.8	
Interest rate/growth differential [7]	0.0	0.8	-2.1	-2.2	-1.9	-0.9	-0.3	-0.3	0.0	-5.8	
Of which: real interest rate	1.0	0.5	-0.1	-1.4	-0.6	0.0	0.5	0.8	1.0	0.3	
Of which: real GDP growth	-1.0	0.3	-2.0	-0.9	-1.3	-0.9	-0.8	-1.1	-1.0	-6.0	
Exchange rate depreciation [8]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	1.0	7.7	4.2	0.8	1.6	0.6	-0.1	0.2	0.0	3.1	
Residual, including asset changes [9]	-1.0	-0.5	-0.4	-0.3	-0.3	-0.3	-0.3	-0.4	-0.3	-2.0	



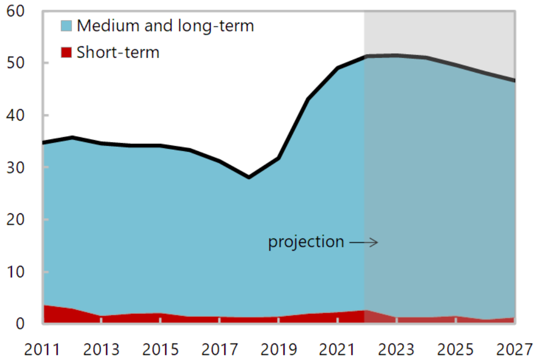
Source: IMF staff.
1/ Public sector is defined as general government.
2/ Based on available data.
3/ Long-term bond spread over U.S. bonds (bp).
4/ Based on expenditure GDP.
5/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.
6/ Derived as [r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ) times previous period debt ratio, with r = effective nominal interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).
7/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.
8/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).
9/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.
10/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 2. New Zealand Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

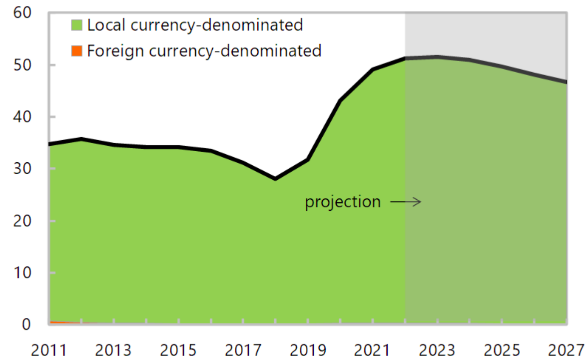
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

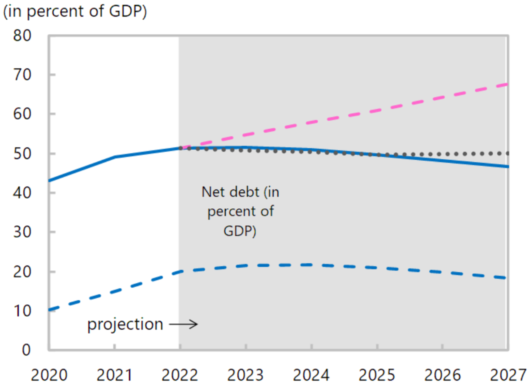


Alternative Scenarios

Baseline   Historical   Constant Primary Balance

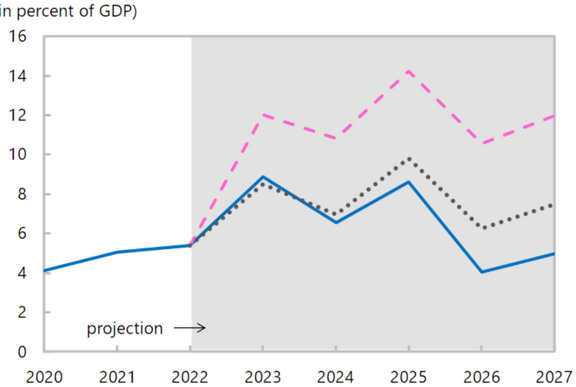
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

Baseline Scenario	2022	2023	2024	2025	2026	2027
Real GDP growth	1.9	2.6	1.9	1.6	2.4	2.2
Inflation	5.7	4.1	3.4	3.0	2.8	2.5
Primary Balance	-4.0	-0.8	-0.1	0.6	1.0	1.1
Effective interest rate	2.9	2.9	3.5	4.0	4.6	4.8
Constant Primary Balance Scenario						
Real GDP growth	1.9	2.6	1.9	1.6	2.4	2.2
Inflation	5.7	4.1	3.4	3.0	2.8	2.5
Primary Balance	-4.0	-4.0	-4.0	-4.0	-4.0	-4.0
Effective interest rate	2.9	2.9	3.5	3.9	4.4	4.5

Historical Scenario	2022	2023	2024	2025	2026	2027
Real GDP growth	1.9	3.2	3.2	3.2	3.2	3.2
Inflation	5.7	4.1	3.4	3.0	2.8	2.5
Primary Balance	-4.0	-0.5	-0.5	-0.5	-0.5	-0.5
Effective interest rate	2.9	2.9	4.0	4.8	5.8	6.1

Annex VII. Deposit Takers Bill

1. **The Deposit Takers Bill (DTB) is part of the second phase of the RBNZ Act Review and aims to strengthen the RBNZ's financial stability mandate.** By strengthening the bank supervision and resolution frameworks and introducing deposit insurance, the Bill aims at promoting the safety and soundness of deposit takers and ensuring public confidence in the financial system. The DTB also addresses various recommendations from the 2017 Financial Sector Assessment Program (FSAP) report for New Zealand, particularly in meeting the Basel Core Principles (BCP) for effective banking supervision. The RBNZ released an exposure draft to seek input from stakeholders, which will be considered before submission to Parliament. Once introduced into Parliament, further stakeholder feedback will be sought during the select committee process scrutinizing the Bill.

2. **The DTB seeks to provide the legal basis on which to build an intensive prudential supervisory approach and strengthens the bank resolution framework.** In particular, the DTB will provide the legal basis for developing regulatory requirements and introducing independent on-site verification work by the RBNZ. It also strengthens the resolution framework by adopting some key elements of international resolution standards.

3. **The DTB proposes to set up a Depositor Compensation Scheme (DCS).** The DCS, to be fully funded by fees from its members, would insure deposits up to NZ$100,000, covering an estimated 93 percent of depositors. As is typical for deposit insurance schemes elsewhere, participation of all licensed deposit takers will be mandated under the proposed law.

4. **These proposals are expected to strengthen the financial safety net.** Some improvements are particularly useful, such as the removal of the need to receive the consent of the Minister of Finance for the application of early intervention measures, the adoption of some missing elements of the FSB's Key Attributes of Effective Resolution Regimes, and the general scope and design of the DCS.

5. **Proposals related to the crisis resolution framework, implementing consolidated supervision, related party framework and clarifying governance arrangements could be strengthened further.** The crisis resolution framework should be improved by granting statutory bail-in powers and reducing the risk of resolutions that do not immediately recapitalize the bank, as these could lead to adverse effects on public confidence in the financial system. Further, provisions that affect the autonomy of the RBNZ should be reviewed. The Minister's role in initiating resolution should be limited to cases where public funds are needed and fiscal risks are entailed. The RBNZ's potential ownership of bridge banks and asset management companies could give rise to concerns over financial autonomy and conflicts of interest. It will also be important to ensure that the DCS has its own independent governance framework, and that its balance sheet is clearly separated from the RBNZ. Some aspects of the resolution funding framework need to be clarified. On supervision, enabling clauses to support consolidated supervision would be helpful, while the perimeter of persons and transactions under the related party framework could usefully be expanded. On enforcement, pecuniary sanctions without court process should be considered, to the extent

permitted within the broader legal framework, while making the RBNZ's power to issue infringement notices more efficient. There may be some overlaps in early intervention and resolution triggers, which should be avoided.

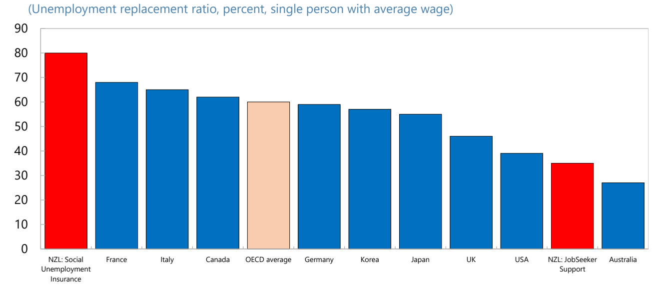
6. **The authorities see scope to address some of these issues through other channels including implementing regulations, civil arrangements, and administrative measures.** The authorities continue to think the open bank resolution framework could work well in New Zealand and does not stand in the way of swift resolution in many cases. The absence of a statutory bail-in requirement could be addressed through civil (contractual) bail-in procedures. Fiscal support for resolution will be enabled by an amendment to the Public Finance Act, though this could leave open questions of consistency of treatment of shareholders and other stakeholders. On improving the framework for supervision, the remaining elements identified in the BCP assessment could be clarified when implementing regulations and enforceable commitments on directors of banks.

7. **The DTB is a paradigm shift in regulating and supervising the financial system, and its effective implementation calls for significantly more resources.** While New Zealand's approach to financial regulation rests on three pillars—self, market and regulatory discipline—the first two have been especially critical given the dominance of foreign banks in the system. The DTB strengthens the regulatory pillar, building on work undertaken since the FSAP. Building capacity to effectively implement the DTB will need to be a priority, and the authorities have begun work to significantly increase the number of supervisors employed at the RBNZ, in part in anticipation of the new powers and responsibilities from the passage of the Act. The RBNZ's funding has been increased to enable this. Included in this is separating the existing Supervision Department in two to ensure that the appropriate management spans of control are maintained as the number of supervisors is increased. In addition to the growth in staff numbers, efforts are underway to strengthen the supervisory framework through entity proximity (the creation of a significant supervisory presence in Auckland, where the majority of regulated entities' New Zealand operations are headquartered) and enhanced technology, processes, and capability. A separate bank resolution department, which will be responsible for compiling resolution plans, assessing their adequacy, and, if the need arises, overseeing the bank resolution process, is in the process of being set up. This will help avoid conflicts of interest between supervision and resolution.

Annex VIII. Income Insurance Scheme in New Zealand

1. **New Zealand is one of a few advanced economies which do not have a formal unemployment insurance scheme.** New Zealand has a tax-financed unemployment benefit called Jobseeker Support. The coverage of the benefit is small, with only one third of workers with family income receiving benefits due to means testing. In addition, the generosity of the benefit is low compared to other advanced economies, and the flat benefit of the scheme suggests that particularly higher-income earners face a significant and sudden loss of income if they lose their job.

New Zealand's Unemployment Benefits Are Less Generous
(Unemployment replacement ratio, percent, single person with average wage)



Sources: OECD, New Zealand Treasury.

2. **The authorities are working towards establishing an unemployment insurance scheme.** In the awake of COVID-19, the government has indicated its intention to establish an Income Insurance Scheme by 2023, largely replacing the existing Jobseeker Support scheme.[1] The scheme will be financed through a levy on salary and wages and likely generate only limited additional fiscal costs.

Income Insurance Scheme vs. Jobseeker Support

	Income Insurance Scheme	Jobseeker Support
Replacement ratio	80 percent	35 percent (2019)
Duration	7 months	Unlimited
Means tested	No	Yes
Finance	Social security contribution	Tax

Sources: Employment New Zealand, OECD.

3. **While the introduction of an unemployment insurance is welcome, the scheme should be calibrated carefully to address trade-offs between insurance and incentives.** Unemployment insurance would promote consumption smoothing and strengthen macroeconomic automatic stabilizers. At the same time, overly generous support could undermine workers' job search incentives. In the current plan, the unemployment replacement ratio is expected to be 80 percent of workers' former earnings, among the highest in advanced economies, although its duration, at 7 months, is relatively short.

4. **Some alternative approaches may alleviate trade-offs.** Given potential disincentive effects, one option would be to start the scheme with a lower replacement rate and assess trade-offs as the data accumulate. Recent studies suggest that state dependent unemployment insurance, which tops up unemployment insurance during downturns, would alleviate trade-offs (Shmieder and others, 2012, Landais and others, 2018). Other studies argue that unemployment insurance should be adjusted for financial conditions (Kroft and Notwidigdo, 2016). On duration, providing support for a longer period with a gradual decline of the replacement ratio could support better job matching quality while limiting disincentive effects (Nekoei and Weber, 2017).

[1] Jobseeker Support will remain available for eligible people after expiration of Income Insurance payments.

Annex IX. The Minimum Wage in New Zealand

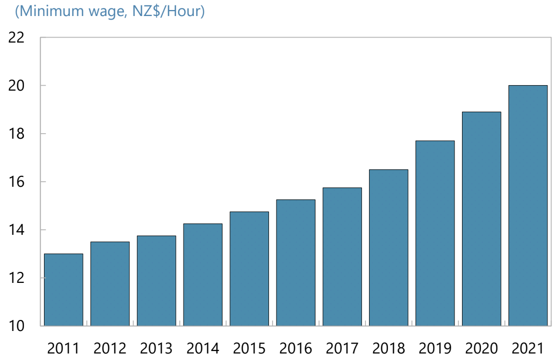
1. The minimum wage has been rising to relatively high levels. The government has increased the minimum wage at a pace faster than underlying labor productivity growth in recent years. In April 2022, the minimum wage was increased to NZ$21.20 per hour, from NZ$20 in 2021. As a result of the significant increase in recent years, the minimum wage, when put in relation to the median wage, is among the highest in advanced economies.

2. In general, the impact of an increase in a minimum wage depends on labor market structure. In a competitive market, some firms may reduce employment if the minimum wage is set above the prevailing level. On the other hand, a minimum wage could boost employment if the labor market structure is more monopsonistic, where small number of firms hold wages down by hiring too few workers. More broadly, minimum wages can be used to address inequality if disadvantaged workers have weaker bargaining power, while too high rates could affect firms' competitiveness.

3. As the minimum wage in New Zealand is already high, a further rapid increase could have unintended impacts on labor market. As the minimum wage is already about 65 percent of the median wage, a further increase in the minimum wage may be increasingly binding and erode New Zealand's competitiveness. It may have an adverse impact on job opportunities for low-skilled workers who work at or near the minimum wage. In the long run, a minimum wage close to a median wage may disincentivize human capital accumulation, with potential negative effects on growth. A too high minimum wage could also undermine labor market flexibility and hinder needed wage adjustments during downturns. Given those potential unintended impacts, future minimum wage adjustments should be calibrated carefully, and an increase in the minimum wage should be linked to underlying labor productivity growth. To address inequality, other tools, such as cash transfers and active labor market policies, can be considered.

The Minimum Wage Has Increased At a Fast Pace

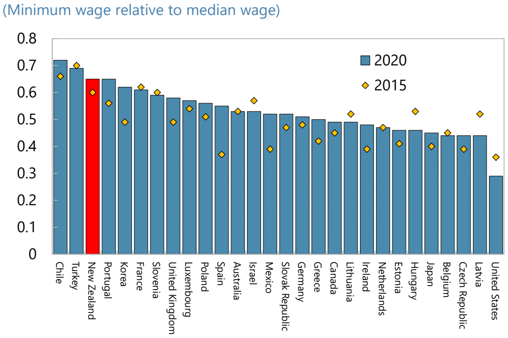
(Minimum wage, NZ$/Hour)



Source: New Zealand authorities.

New Zealand's Minimum Wage is Among the Highest in AEs

(Minimum wage relative to median wage)



Source: OECD.

Annex X. Follow-Up on Key Recommendations of the 2017 FSAP

Recommendation	Time Frame	Update and Implementation
Financial Stability and Financial Sector Resilience		
Increase RBNZ resources for the supervision and regulation of banks, insurance companies, and FMIs.	ST	**In process.** A new funding agreement signed with the Minister of Finance in June 2020 provides the RBNZ with an average of NZ$115 million a year (an increase of about NZ$35 million) for its operations over five years from July 2020, to support a more intensive supervisory model. Staff numbers have increased significantly in the financial policy area over the past several years, with a significant supervisory and a smaller policy footprint now established in Auckland, where many of the NZ operations of RBNZ-regulated entities are headquartered. This process is ongoing.
Strengthen cooperation and collaboration arrangements with Australian authorities.	ST	**In process**. With ongoing interaction, completed a hypothetical bank crisis simulation exercise in September 2017, and a follow-up exercise on communications coordination in 2019. There is continuing coordination between NZ and Australian communications teams across multiple agencies by a dedicated working group. This Trans-Tasman cooperation is explicitly coordinated with the wider TTBC (Trans-Tasman Council on Banking Supervision) work. (Note the TTBC remit covers insurers and other entities in addition to banks.) The RBNZ Act contains a new cooperation function for the RBNZ that includes 'overseas central banks and relevant international institutions'. The trans-Tasman cooperation provision in the current Act (s.68A) will be carried across to the deposit takers sectoral legislation under the forthcoming Deposit Takers Act (DTA).
Clarify responsibilities of the Treasury and RBNZ on financial sector issues to reinforce the role of RBNZ as prudential regulator and supervisor.	ST	**In process.** Governance and prudential regulation options have been examined in Phase 2 Review of the RBNZ Act. A new financial stability objective for the RBNZ was introduced in the RBNZ Act 2021. A Financial Policy Remit to be issued by the Minister of Finance will outline matters that the RBNZ will have to have regard to in pursuing its financial stability objectives, prudential standards and its implementation. The RBNZ Act designates a government department as the formal monitor of the RBNZ on behalf of the Minister of Finance (replacing the role played by the current board). The Minister has appointed the Treasury in the monitor role. The DTA will further clarify the role of the Minister in the prudential framework (e.g., role in the crisis management and bank resolution frameworks).

Recommendation	Time Frame	Update and Implementation
Issue enforceable standards on key risks, governance, risk management, and controls to make RBNZ's supervisory expectations more transparent and support supervisory preventive action.	ST	**In process.** As laid out in the exposure draft of the DTA, prudential requirements for deposit takers will be set through 'standards' as a secondary legislative instrument. The DTA will clearly set out the areas where the RBNZ can set standards. The scope of standard-setting broadly aligns with those areas expected by the Basel Core Principles (BCPs). Within the scope permitted by legislation, the RBNZ will still choose in what areas to set standards, supported by guidance where appropriate. IPSA already uses standards as the means to set prudential requirements for licensed insurers. The legislation is being reviewed to take account of experience and to follow up on the recommendations of independent reports in recent years. While the RBNZ will continue to use standards to regulate the sector, the areas in which it can issue a standard will be looked at as part of the review.
Review and extend the enforcement regime to promote preventive action and enhance sanctions powers, including by eliminating ministerial consent for directions, and making compliance with RBNZ policy documents evidence of prudent practice.	MT	**In process.** The DTA exposure draft expands the current enforcement toolkit (e.g. with the inclusion of enforceable undertakings and remedial notices) and removes the requirement for Ministerial consent to issue directions, thereby removing the current high threshold for using this tool to take corrective action.
Initiate on-site programs to test the foundation of the three-pillar approach and directors' attestations and increase supervisory engagement with institutions in order to require appropriate action.	ST	**In process**. A team has been formed for the purposes of performing deep dive onsite thematic reviews. These are performed across both the deposit taking and insurance sectors and focus on a range of risk, governance and compliance matters. The exposure draft of the DTA empowers the RBNZ to undertake on-site inspections of deposit takers. How this power is operationalized will be a matter for the RBNZ (e.g., frequency and scope of inspections across large and small deposit takers). The current review of IPSA will consider the design of a similar on-site inspection power for the insurance sector.
Refine Financial Markets Authority (FMA) supervision by a) direct monitoring of aspects of asset management relevant to financial stability;	I	a) **In process.** The FMA published findings of a thematic review of liquidity risk management practices in July 2021. Supplementing the FMA good practice guide of April 2020, the FMA is now preparing industry guidance, based on IOSCO recommendations, for consultation later in 2022. The FMA is also taking a more direct oversight role of the Managed Investment Scheme (MIS) sector, including a sector risk assessment which will guide FMA and supervisor efforts, and thematic projects/ guidance related to demonstrating

Recommendation	Time Frame	Update and Implementation
		value for money and maturing the industry approach to better articulating and substantiating ESG labels and claims.
b) ensuring quality of Financial Markets Supervisors; and		b) **In process.** The relicensing process for supervisors has commenced and will continue through 2022. The current license duration is five years, and this is the second such re-licensing round. The FMA highlighted the expected areas of focus in 2018 and will be examining those items closely as part of relicensing. The FMA continues to have strong engagement with Supervisors including through regular operational meetings, sector forums, chief executive and senior management relationship meetings and attending Board meetings. In 2020 and 2021, the FMA required supervisors to undertake and identify risks in the MIS sector and report back to the FMA. The process of evaluating these Sector Risk Assessments is now underway, with the FMA intending to provide formal feedback to Supervisors in the coming months.
c) enhancing insurance intermediary and conduct regulation and supervision.		c) **In process.** The new financial advice regime, which came into effect on March 15, 2021, continues to be successfully embedded and operationalized. This includes ongoing market engagement, guidance, and informational material to support entities full-license application. In anticipation of the Conduct of Financial Institutions Bill and the Insurance Contracts Bill (that reforms and updates the Insurance Contract Law) passing into law, the FMA has established a program for implementation.
Expand the FMA's regulatory perimeter to include licensing and supervision of custodians and appropriate oversight of wholesale asset managers.	ST	**In process.** The FMA has received its outsourced thematic on custodial arrangements and is progressing work to consider whether there is a case for recommending the establishment of a regulatory regime for custodians.
Adopt and implement proposed Financial Market Infrastructures (FMI) legislation on regulation, oversight, and enforcement powers.	I	**Completed**. The Financial Market Infrastructures Act (FMI Act) was enacted in May 2021. Work on the designation of FMIs and issuance of standards under the Act is currently underway and is expected to be complete by around March 2023.
Adopt the CPSS-IOSCO Principles for Financial Market Infrastructures (PFMI) through detailed requirements in secondary legislation; change the frequency of FMI self-assessments in the proposed regime from three to two years; and enhance compliance of the designated FMIs with PFMI requirements.	ST	**In process**. The FMI Act provides the ability for the PFMI to be implemented via legally binding standards. The RBNZ is currently drafting the relevant standards and expects that this work will be complete by around March 2023. The frequency of FMI self-assessments is intended to be changed from three to two years once these standards are set.

Recommendation	Time Frame	Update and Implementation
Ensure that designated nonfinancial businesses and professions are subject to AML/CFT requirements, particularly company service providers, lawyers, and accountants.	MT	**Completed**. The *AML/CFT Amendment Act 2017,* which extends the coverage of the AML/CFT laws, has come fully into effect. The legislation now covers lawyers, conveyancers and businesses that provide trust and company services (from July 1, 2018); accountants (from October 1, 2018); and real estate agents (from January 1, 2019).
Expand data collection and modeling efforts to develop structural models for credit risk in commercial real estate (CRE) and corporate portfolios.	MT	**In process**. Current focus is on embedding stress testing within the prudential framework. Consideration of enhancements will follow.
Macroprudential Framework		
Strengthen arrangements for macroprudential policy by increasing communication efforts; by increasing the transparency of the process to adjust the framework; and by maintaining an accountability framework that does not jeopardize the integrity and independence of the macroprudential decision-making process.	C	**In process.** In 2019, the RBNZ published a review of experience with its loan-to-value ratio policy and a framework document providing more clarity on the purpose and strategy for using macroprudential tools. The RBNZ is currently updating this framework and developing guidance notes on individual macroprudential tools. The Financial Policy Remit (see above) will enable the Minister to articulate government's policy priorities that are relevant to how the RBNZ goes about addressing systemic risk (that is, macro-prudential policy). The exposure draft of the DTA subjects macro-prudential powers to the same general framework as other standard-setting powers, with the exception that the scope of lending-standard tools in relation to property lending (e.g. LVRs and DTIs) needs to be empowered through regulation. The current Macro-Prudential Policy MoU will be superseded in the new prudential framework for deposit takers by the role played by the Financial Policy Remit and the process around the setting of standards (including lending standards).
Introduce DTI measures in the macroprudential toolkit.	I	**Completed.** Following advice from the RBNZ in 2021 on measures to address unsustainable house prices, the Minister of Finance agreed to add DTI restrictions to the macroprudential toolkit.
Implement DTI measures if the changes to the LVR do not reduce the risks in the housing sector.	I	**In process.** The RBNZ is consulting with stakeholders on the possible introduction of DTI limits and floors on serviceability test rates used to assess debt servicing capacity of borrowers. If required, the likely timeframes for being able to implement these restrictions would be Q2 2022 for a test rate floor and Q4 2022 for a DTI limit. Whether an intervention is needed will depend on the assessment of financial stability risks at the time.

Recommendation	Time Frame	Update and Implementation
Increase capital buffer requirements to reflect the concentration of the financial sector in four banks.	I	**Completed.** The 2019 Capital Review, required banks to raise their minimum capitalization from 10.5 percent of risk-weighted assets to 18 percent for the four large banks and 16 percent for the remaining smaller banks in seven years, starting from by July 2020. In the context of the COVID-19 response, the start date was pushed out to July 2022, when the first step up in capital requirements will commence with the part introduction of the D-SIB capital requirement.
Crisis Readiness, Management, and Resolution		
Strengthen domestic crisis management arrangements by reaching ex-ante agreement on roles, responsibilities, and processes; prepositioning, mobilization, logistics, and communications plans; and testing through simulation exercises.	MT	**In process.** Phase 2 Review of the RBNZ Act examined options to enhance the crisis management regime, most of which have been developed with reference to the 2017 FSAP recommendations. The DTA exposure draft designates the RBNZ as the Resolution Authority, with a broader range of powers. A Depositor Compensation Scheme (DCS) will be introduced. The DTA will also clarify the role of the Minister in the crisis management and bank resolution frameworks. An amendment to the Public Finance Act 1989 will be introduced in order to address a gap in the current arrangements, enabling the Government to act quickly and use public funds in a financial crisis.
Reconsider the merits of deposit insurance, or in the absence of policy support, introduce a limited depositor preference to provide legal certainty for the *de minimis* exemption in OBR.	MT	**Partially done.** Key decisions adopted as a part of the Phase 2 Review of the RBNZ Act, include to introduce a depositor compensation with a NZ$100,000 limit per person per institution, and to be funded by a levy on deposit takers, with a Government backstop.
Revise the RBNZ Act to provide greater clarity and certainty in resolution, by inserting objectives in resolution including protection of depositors and the public interest and requiring accountability reporting against these objectives; by clarifying that the RBNZ is the sole resolution authority and inserting an express requirement for ministerial consent for resolutions with fiscal or systemic implications only.	MT	**In process.** The Phase 2 Review of the RBNZ Act examined options to enhance the crisis management regime, most of which have been developed with reference to the 2017 FSAP recommendations. The DTA exposure draft provides the RBNZ with the powers to act as the resolution authority, includes clear objectives and functions, aims to widen resolution powers and includes "no creditor worse off" provisions.
C = continuous; I (immediate) = within one year; ST (short-term) = 1–3 years; MT (medium-term) = 3–5 years.		
Sources: IMF (2017), *New Zealand, Financial Sector Assessment Program—Financial System Stability Assessment*; and New Zealand authorities.		

INTERNATIONAL MONETARY FUND

NEW ZEALAND

STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

April 28, 2022

Prepared By

Asia and Pacific Department
(In consultation with other departments)

CONTENTS

FUND RELATIONS

(As of March 31, 2022)

Membership Status: Joined: August 31, 1961; Article VIII

General Resources Account:	SDR Million	Percent Quota
Quota	1,252.10	100.00
Fund Holdings of Currency	906.44	72.39
Reserve position in Fund	346.36	27.66
Lending to the Fund		
New Arrangements to Borrow	8.04	

SDR Department:	SDR Million	Percent Allocation
Net cumulative allocation	2,053.84	100.00
Holdings	2,119.73	103.23

Outstanding Purchases and Loans: None

Financial Arrangements: None

Projected Payments to Fund (SDR Million; based on existing use of resources and present holdings of SDRs) [1/]

	Forthcoming				
	2022	2023	2024	2025	2026
Principal					
Charges/Interest	0.03	0.03	0.03	0.03	0.03
Total	**0.03**	**0.03**	**0.03**	**0.03**	**0.03**

[1/] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Exchange Arrangement:

The New Zealand dollar has floated independently since March 1985. The de facto exchange rate arrangement is free floating, and the de jure exchange rate arrangement is free floating. New Zealand accepted the obligations under Article VIII, Sections 2, 3, and 4 on August 5, 1982 and maintains an exchange system that is free of multiple currency practices and restrictions on the making of payments and transfers for current international transactions, other than restrictions notified to the Fund in accordance with Decision No. 144-(52/51).

Article IV Consultation:

New Zealand is on the 12-month consultation cycle. The 2021 Article IV consultation was concluded by the Executive Board on May 5, 2021.

FSAP Participation and ROSCs:

New Zealand has participated in two FSAPs to date.

- The FSSA from the 2003 FSAP mission and the Detailed Assessments of Observance of IOSCO Objectives and Principles of Securities Regulation and FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism were published under Country Reports No. 04/126, No. 04/417, and No. 05/284, respectively.

- New Zealand participated again in 2016, with one FSAP mission in August 2016 and another FSAP mission in November 2017. The FSSA was discussed by the Executive Board at the time of the discussion of the Staff Report for the 2017 Article IV Consultation with New Zealand.

Technical Assistance:

- A monetary and financial statistics (MFS) technical assistance (TA) mission visited New Zealand during October 1-12, 2018. The *TA report* was published on June 14, 2019.

STATISTICAL ISSUES

(As of March 31, 2022)

I. Assessment of Data Adequacy for Surveillance
General. Data provision is adequate for surveillance. The authorities are continuing to enhance data quality and expand the range of data available, and are making progress towards subscribing to the IMF's Special Data Dissemination Standard (SDDS).
Real Sector. Annual estimates of GDP are compiled for production, expenditure and income, in nominal and chained volume terms. Estimates are fully reconciled via supply and use tables and make use of annual enterprise and household surveys to update benchmarks. The authorities compile quarterly estimates of GDP for both production and expenditure, based on appropriate indicators. Quarterly production GDP is compiled only on a chained volume basis while quarterly expenditure GDP is compiled on both nominal and chained volume terms. National accounts data are released around 11 weeks after the close of the reference quarter. New Zealand only produces a quarterly rather than monthly consumer price index (CPI), which has national coverage and a contemporary weight reference period (2018/2019). CPI data is released three weeks after the close of the reference quarter. Data collection methods are appropriate, and include web-scraping and the use of scanner data.
Fiscal Sector. Stats NZ provides annual data (operating statement, balance sheet, government expenses by function, taxation revenue and non-financial assets reconciliation) on the general government and its central and local government subsectors following the *Government Finance Statistics Manual 2014* (*GFSM 2014*) recommendations for data beginning from 2009 on a fiscal year (July-June) basis. It is published roughly five months following the fiscal year end, preceded by data on a provisional basis at the time of the budget (usually in May). The authorities also report detailed central government debt data to the IMF / World Bank Quarterly Public Sector Debt Database. The Treasury also provides data on a timely basis for the central government that complies with New Zealand equivalents of the GAAP Public Sector Public Benefit Entity (PBE) Standards from 2005 onwards. They are provided on a monthly basis (with a one-month lag), with an annual statement published within 4 months of the fiscal year end. The provided data enable adequate assessment of the impact of fiscal policy measures on New Zealand's economic performance.
Monetary and Financial Sectors. The Reserve Bank of New Zealand (RBNZ) publishes monthly and quarterly data on a broad range of monetary and financial variables. Monetary statistics compiled by the RBNZ are consistent with the methodology of the *2016 Monetary and Financial Statistics Manual and Compilation Guide (MFSMCG)*. New Zealand reports high quality monetary

statistics regularly to STA for publication in *International Financial Statistics*. There is room for improving the timeliness of the data for other financial corporations. RBNZ also reports some data and indicators of the Financial Access Survey (FAS), including the two indicators (commercial bank branches per 100,000 adults and ATMs per 100,000 adults) adopted by the UN to monitor Target 8.10 of the Sustainable Development Goals (SDGs).
Financial Sector Surveillance: New Zealand currently does not report Financial Soundness Indicators (FSIs) for dissemination on the Fund website. The authorities should develop an action plan to submit the FSI data and metadata to the IMF for posting.
External Sector. Stats NZ provides timely information on the balance of payments and the international investment position (IIP) on a quarterly frequency. The data are released around 11 weeks after the close of the reference quarter. The IIP and international financial assets and liabilities measures of New Zealand's international balance sheet position are complemented with data on external lending and debt in total and by sector and the ownership relationship between the New Zealand-resident party and the non-resident counterparty of external lending and debt positions. This follows the IMF's external debt methodology in excluding values for financial derivative asset and liability positions. RBNZ provides monthly data on official international reserves and in the Data Template on International Reserves and Foreign Currency Liquidity. Stats NZ also participates in the Coordinated Direct Investment and Portfolio Investment Surveys conducted by the IMF's Statistics Department.

New Zealand: Table of Common Indicators Required for Surveillance
(As of March 31, 2022)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of Publication[6]
Exchange Rates	3/30/2022	3/30/2022	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	2/2022	3/14/2022	M	M	M
Reserve/Base Money	2/2022	3/14/2022	M	M	M
Broad Money	2/2022	3/31/2022	M	M	M
Central Bank Balance Sheet	2/2022	3/14/2022	M	M	M
Consolidated Balance Sheet of the Banking System	2/2022	3/31/2022	M	M	M
Interest Rates[2]	3/30/2022	3/30/2022	D	D	D
Consumer Price Index	Q4 2021	1/27/2022	Q	Q	Q
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	2020/21	12/7/2021	A	A	A
Stocks of Central Government and Central Government-Guaranteed Debt[4]	2020/21	12/7/2021	A	A	A
External Current Account Balance	Q4 2021	3/16/2022	Q	Q	Q
Exports and Imports of Goods and Services	Q4 2021	3/17/2022	Q	Q	Q
GDP/GNP	Q4 2021	3/17/2022	Q	Q	Q
Gross External Debt	Q4 2021	3/16/2022	Q	Q	Q
International Investment Position[5]	Q4 2021	3/16/2022	Q	Q	Q

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes, and bonds.
[3] Foreign, domestic bank, and domestic non-bank financing.
[4] Including currency and maturity composition.
[5] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[6] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).