

# THE MYSTERY OF THE \$52 BILLION GIFT: DOES NEW ZEALAND HAVE A FAIRY GODMOTHER?

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Research Note

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The New Zealand Initiative is an independent public policy think tank supported by chief executives of major New Zealand businesses. We believe in evidence-based policy and are committed to developing policies that work for all New Zealanders.

Our mission is to help build a better, stronger New Zealand. We are taking the initiative to promote a prosperous, free and fair society with a competitive, open and dynamic economy. We develop and contribute bold ideas that will have a profound, positive, long-term impact.

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## Does anyone believe in a fairy godmother?

Imagine checking your credit card balance with well-founded trepidation. Unexpected costly events had pushed you over budget. You fear you might not be able to pay the debt you have run up.

But what do you think when you open your statement and find that your debt is *much* less than the sum of what you have bought? Is this a fairy godmother at work, a clerical error by the card company, a lottery win, or a hidden time bomb?

The question is pertinent – in a national context. According to SNZ, for decades New Zealanders have been spending more overseas on current account than we have been earning from exports and overseas investment income.<sup>1</sup> To fund the difference, we have had long to borrow more from overseas than we have invested overseas.

The advent of Covid-19 greatly increased the needed overseas borrowing. Export income from tourism and overseas students plummeted. The current account deficits in the Balance of Payments (BoP) were 8.3% and 7.6% of GDP respectively in the years ended September 2022 and 2023. The average annual ratio starting with the June quarter 2009 and ending with the September quarter 2023 is 3.5% of GDP.<sup>2</sup>

The scale of the cumulative funding need is large. Starting with the June quarter 2009 and ending with the September quarter 2023, it is \$158 billion. Of this \$62 billion occurred in the eight quarters to September 2023 (Table 1, first row).

Table 1: The puzzle - why did the Net International Investment position (NIIP) not decline by more?

	Period	
	June Qtr 2009- Sept Qtr 2023 (inclusive)	Dec Qtr 2021 to Sept 2023 (inclusive)
Required net capital to fund the current account deficit compared to the actual change in the NIIP		
	\$ million	
Cumulative current account deficit (+) in the BoP	\$158,134	\$61,715
Decline (-) in NIIP	-\$32,255	-\$25,379
Difference = apparent funding from other sources	\$125,879	\$36,336

The decline in New Zealand's Net International Investment Position (NIIP) (i.e. what we own overseas compared to what we owe overseas) has been much smaller – at \$32 billion for the full period and \$25 billion for the shorter period (Table 1, second row).

Apparently, New Zealanders have spent more overseas since March 2009 than we have earned, by \$158 billion, but our overseas “bank balance” has fallen by only \$32 billion. It is as if a fairy godmother has funded the extra \$126 billion. Or is it?

The difference is large but less striking for the shorter period shown in Table 1 (column 2). From the December quarter 2021 to the September quarter 2023, the cumulative current account deficit was \$62 billion, but the NIIP only declined by \$25 billion. Where did the extra capital of \$36 billion come from?

<sup>1</sup> See the current account deficit chart in Appendix 2.

<sup>2</sup> The sole reason for picking the end of March 2009 as the starting point is that the Net International Investment Position (NIIP) was then, at 84.3% of GDP, the most negative it has been relative to GDP in statistics going back to June 2000. At 30 September 2023, its estimated value is -47.9% of GDP. See the NIIP and net overseas debt chart in Appendix 2 for the full record.

## Statistics New Zealand's funding estimates

SNZ's capital account statistics in the BoP provide its best estimates of how past current account deficits have been funded (Table 2). It estimates two components directly. The third is a residual. The two estimated components comprise:

- the capital account balance, and
- the financial account balance.

Table 2: SNZ's capital account BoP estimates

SNZ's estimates of the funding of the Current Account deficits		
	June Qtr 2009- Sept Qtr 2023 (inclusive)	Dec Qtr 2021 to Sept 2023 (inclusive)
	\$ million	
Cumulative current account deficits (+)	<b>\$158,134</b>	<b>\$61,715</b>
<i>Accounted for as follows:</i>		
BOP: Capital Account Balance	\$27,642	\$2,124
BOP: Financial Account Balance	\$78,871	\$29,821
BOP: Net Errors & Omissions	\$51,618	\$29,768
	<b>\$158,131</b>	<b>\$61,713</b>

The BoP *capital account* measures the net flow from one-time capital transfers of ownership of fixed assets, debt forgiveness, plus transactions in non-produced, non-financial assets such as patents, copyrights, leases and licenses, plus the purchase and sale of natural resources that have not outputs of production processes. This category includes payments by global reinsurers to New Zealand insurance companies in the event of major losses from natural disasters.<sup>3</sup>

The BoP *financial account* measures transactions in financial assets and liabilities. When New Zealand banks have to borrow offshore to get the foreign exchange to sell to New Zealand customers, the financial account records these and related transactions.

The third category is the mysterious residual item: *Net errors and omissions*.

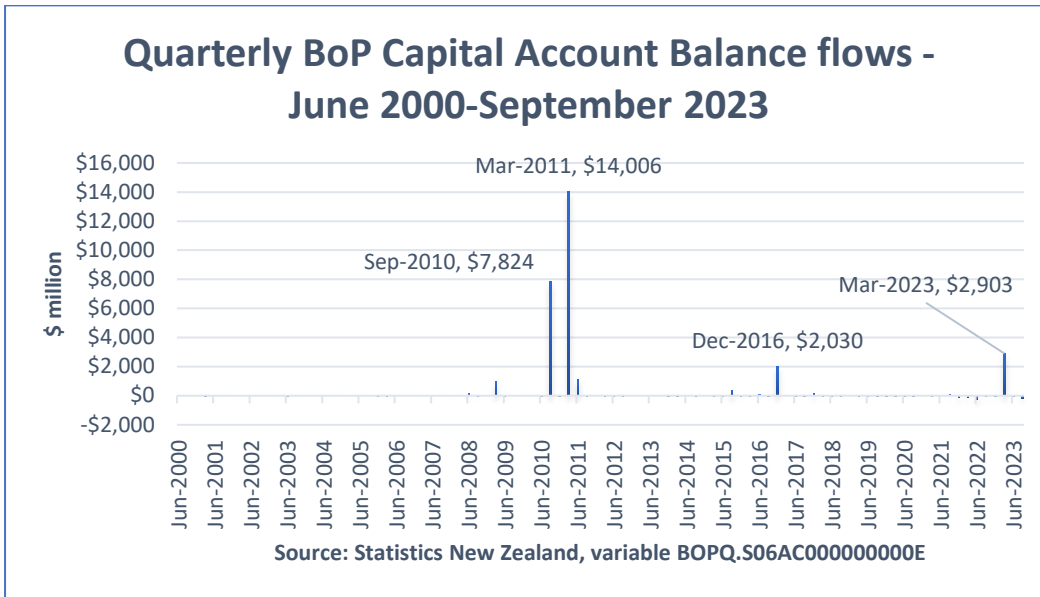
### The capital account

The capital account contributed \$28 billion to funding the \$158 billion needed since March 2009. But its contribution was small in the two years to September 2023 (Table 2, row 3).

The capital account flows during this period have been extremely lumpy (Figure 1). The notably big contributions in 2010 and 2011 will be due to inflows from global reinsurers in response to the Christchurch earthquakes. Reinsurers' payouts in the March quarter 2023 for the Auckland floods and cyclone Gabrielle were also significant. Smaller contributions likely occurred in response to the 2016 Kaikoura and 2017 Wellington earthquakes.

<sup>3</sup> For example, see the discussion under "Capital account" here <https://www.stats.govt.nz/information-releases/balance-of-payments-and-international-investment-position-march-2023-quarter/>

Figure 1: Net capital account balances quarterly June 2000 to September 2023



Perhaps some large capital inflows of recent origin are escaping Statistics New Zealand’s information sources.

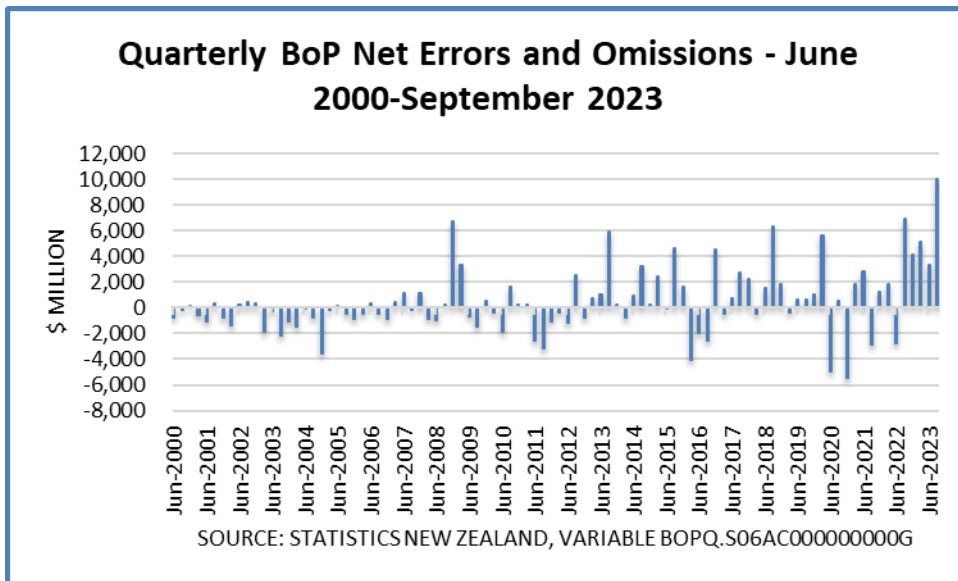
**Errors and Omissions – a fairy godmother or a time bomb?**

The scale of the amounts of \$52 billion and \$30 billion for “errors and omissions” in Table 2 (row 5) must be a real concern to Statistics New Zealand. Zero overall would be its ideal.

Net errors and omissions can only arise from measurement errors in the other items. Either the estimated current account deficits are too large, or the estimated capital and financial balance inflows are too small in aggregate.

In Appendix 1 below, we check to see if Australia’s statistical measures have the same problem. They do not. Its net errors and omissions are smaller and had the opposite sign for the period since 2009.

Figure 2: Errors and Omission quarterly June 2000 to September 2023



### The large financial imbalance from 2009 relative to the modest fall in the NIIP

For the 2009-2023 period, in Table 1 the \$32 billion decline in the NIIP accounts for less than half of the \$79 billion contribution of the financial balance shown in Table 2. Table 3 accounts for the difference.

Table 3: Valuation gains for New Zealanders have been large

	June Qtr 2009- Sept Qtr 2023 (inclusive)	Dec Qtr 2021 to Sept 2023 (inclusive)
	\$ million	
<b>Cumulative Financial Balance (+ = inflow)</b>	<b>\$78,871</b>	<b>\$29,821</b>
Breakdown of contributions		
NIIP: Net Exchange Rate Changes	\$8,234	\$974
NIIP: Net Financial Derivative Valuation Changes	\$5,454	\$646
NIIP: Net Market Price Changes	\$32,031	\$15,399
NIIP: Net Other Valuation Changes	\$900	-\$12,574
Decline (+) in the NIIP	\$32,252	\$25,379
<b>Sum of the above</b>	<b>\$78,871</b>	<b>\$29,824</b>

The \$25 billion decline in the NIIP in the 2021-2023 period in Table 1 accounts for most of the \$30 billion contribution made by the financial account balance in Table 2.

Net market price gains of \$32 billion for the longer period owe much to the gain of \$15 billion in the last seven quarters to September 2023.

Overall, valuation gains of \$47 billion in the longer period reduced the decline in the NIIP from a potential \$79 billion to \$32 billion.

The rise in global interest rates will be a major cause of the recent market price gains. New Zealand's NIIP position is largely a net external debt position. (See the chart in the Appendix 2.) Higher interest rates lower the market value of debt whose interest payments are fixed rather than floating.

A final point is that although the NIIP has become more negative (by \$32 billion or 20%) since March 2009, annual nominal GDP has increased by 112%. That explains why the NIIP is now much smaller relative to GDP – as reported in footnote 1 above.

[Might any clues concerning these mysteries be revealed by a comparison with Australia?](#)

A detailed table in Appendix 1 compares Australia and New Zealand's statistics for the 2009-2023 period. It suggests that the small decline in NZ's NIIP relative to the scale of its current account deficits has been significantly fortuitous. Australia funded its current account deficits from financial balance surpluses to a much greater extent. This was because its funding contributions from other sources were negative, whereas they were positive for New Zealand.

## Conclusions

The mystery of the relatively small decline in the NIIP since 2009 reflects the following fortuitous circumstances:

- The advent of large inflows of capital from global reinsurers to fund losses from natural disasters in New Zealand. This is not a reliable source of future funding.
- Large holding gains from the recent large increases in global interest rates in response to higher inflation. This is not a reliable source of future gain either.
- SNZ's inability to date to ascertain where \$52 billion of its estimated needed funding has come from. Perhaps the NIIP has fallen by much more than it has been able to measure. Substantial revisions to the historical NIIP statistics are on the cards.

In short, if New Zealand continues to run sizeable current account deficits in its balance payments in, in future we should expect New Zealand's NIIP to fall more in line with those deficits than it did in the period between 2009 and 2023. Data revisions could see our NIIP fall by a lot more during the 14 years to 2023.



## Appendix 1: Comparison with Australia 2009-2023

New Zealand's NIIP experience since March 2009 is compared with Australia's in Table 4 below.

Australia has had a smaller funding task, relative to GDP. From the June quarter 2009 to the September quarter 2023 inclusive, Australia's current account deficit in its balance of payments averaged 2.0% of GDP. New Zealand's deficits averaged 3.5% of GDP.

The contribution of "errors and omissions" to funding those deficits was *negative* A\$24 billion for Australia as against positive NZ\$52 billion for New Zealand. That is a big difference -- and a likely impermanent one.

In contrast to New Zealand's large funding inflow on capital account, due to natural disaster reinsurance, Australia had a small A\$9 billion net outflow on capital account.

Table 4: Comparison Between New Zealand and Australia March 2009-September 2023

Table 4: Comparison Between New Zealand and Australia March 2009-September 2023				
	New Zealand		Australia	
	NZ \$ million	% of GDP	A\$ million	% of GDP
NIIP 31 Mar 2009	-\$159,685	-84.3%	-\$710,839	-56.7%
NIIP 30 Sept 2023	-\$191,940	-47.9%	-\$814,685	-31.4%
<b>Dedine</b>	<b>-\$32,255</b>	<b>36.4%</b>	<b>-\$103,846</b>	<b>25.2%</b>
	20%		15%	
<b>Contributions to those declines</b>				
NIIP: Net Financial Account Flows	-\$78,871		-\$411,990	
NIIP: Net Exchange Rate Changes	\$8,234		-\$86,320	
NIIP: Net Financial Derivative Valuation Changes	\$5,454			
NIIP: Net Market Price Changes	\$32,031		\$288,657	
NIIP: Net Other Valuation Changes	\$900		\$105,798	
	<b>-\$32,252</b>		<b>-\$103,855</b>	\$9m discrep.
<b>Relationship between Net Financial Account Flow and Current Account Balance</b>				
Cumulative current account balance in the BoP June quarter 2009-Sept Qtr 2023	<b>-\$158,134</b>		<b>-\$379,513</b>	
Funded by the following capital account cumulative flows:				
BOP: Capital Account Balance	\$27,642		-\$8,632	
BOP: Financial Account Balance	\$78,871		\$411,988	\$2m discrep.
BOP: Net Errors & Omissions	\$51,618		-\$23,843	
	<b>\$158,131</b>		<b>\$379,513</b>	
<b>Conclusion:</b>				
The cumulative deficits in the current account of the balance of payments of	-\$158,134		-\$379,513	
have been funded as follows:				
BOP: Capital Account Balance	\$27,642		-\$8,632	
BOP: Net Errors & Omissions	\$51,618		-\$23,843	
Plus the following components of the Cumulative Financial Account Balances of:	<b>\$78,871</b>		<b>\$411,990</b>	
NIIP: Net Exchange Rate Changes	\$8,234		-\$86,320	
NIIP: Net Financial Derivative Valuation Changes	\$5,454			
NIIP: Net Market Price Changes	\$32,031		\$288,657	
NIIP: Net Other Valuation Changes	\$900		\$105,798	
Dedine in the NIIP	<b>\$32,252</b>		<b>\$103,855</b>	
	<b>\$78,871</b>		<b>\$411,990</b>	

Australia's cumulative valuation gains of A\$308 billion (=412-104) were much higher relative to its A\$711 billion NIIP in March 2009 than were New Zealand's cumulative gains of \$47 billion relative to its \$160 billion NIIP in March 2009.

Australia's valuation gains to NIIP were also much larger than New Zealand's in proportion to their respective net financial account inflows. Australia's valuation gains reduced its A\$412 billion

cumulative financial account inflow to a A\$104 billion decline in its NIIP. New Zealand's valuation gains of \$47 billion were a smaller proportion of its \$79 billion cumulative financial account balances.

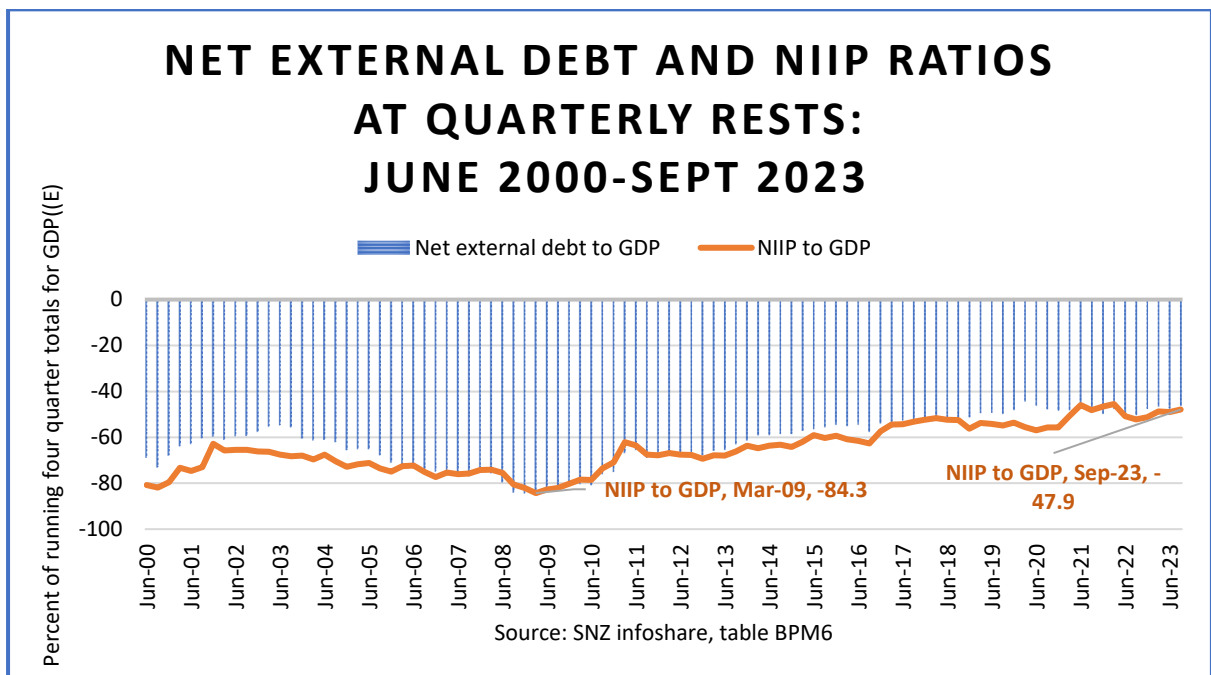
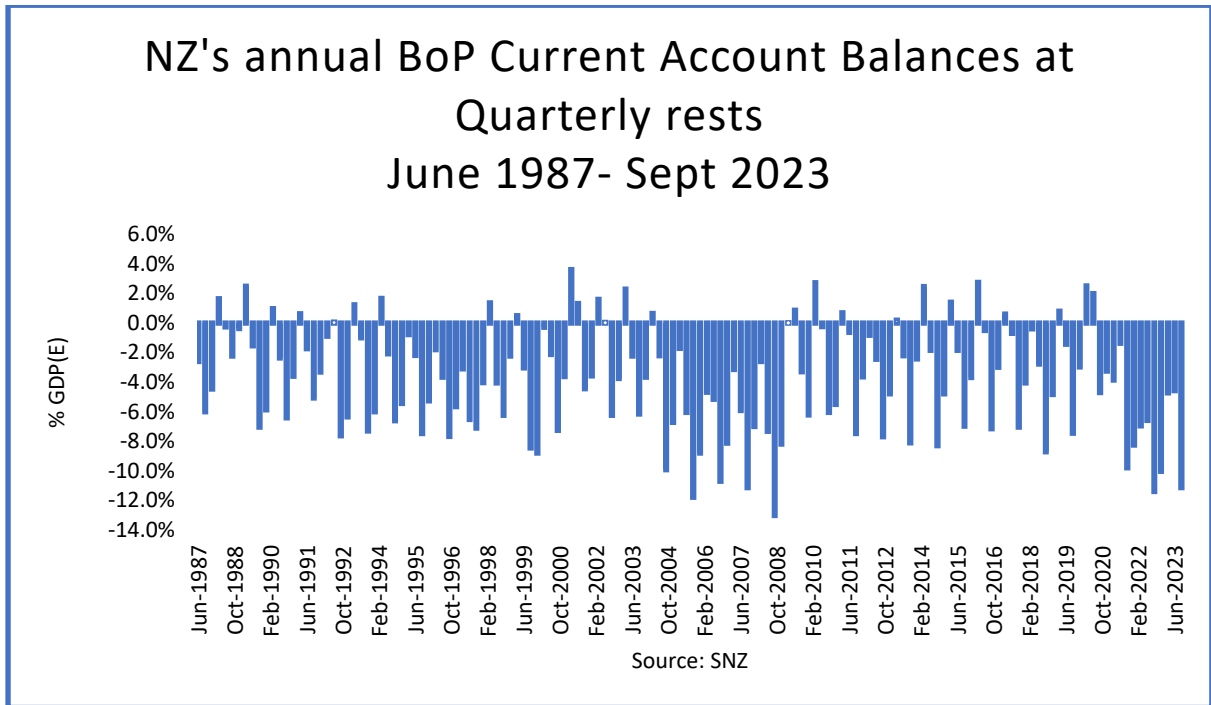
Overall, these differences meant Australia had to fund a much larger proportion of its current account deficits from financial balance surpluses. Partly, as a result, between March 2009 and September 2023, New Zealand's negative net international investment position 'improved' by 37% of GDP. Australia's position 'improved' by only 25% of GDP.

### Concluding observations on the comparison with Australia

The reasons for Australia's larger relative valuation gains might be worthy of further research. The RBNZ or the Treasury's DMO have already looked into this.

Compared to Australia, New Zealand has been fortunate, statistically speaking. First, our NIIP did not fall by a lot more because the lottery we lost on natural disasters was a winner for funding the balance of payments. Second, SNZ has not been able to measure much of how our deficits have been funded. Data revisions could see our NIIP fall by a lot more during the 14 years to 2023.

Appendix 2: Two summary charts



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