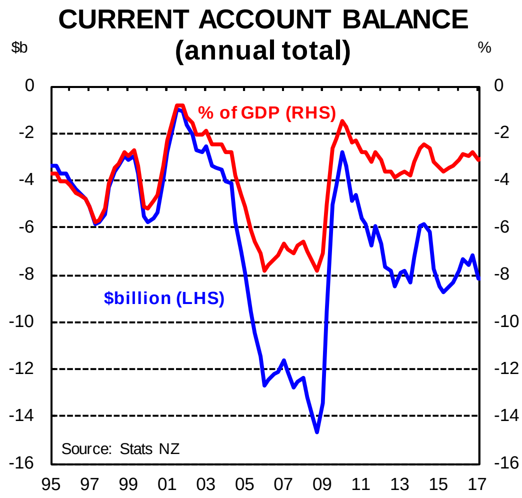
Current account pothole

- **Q1 current account deficit widens by more than expected.**
- **However, we expect this was largely due to temporary factors.**
- **Indeed, we expect the current account deficit to narrow steadily over 2017.**

Summary and Implications
The headline current account deficit surprised over Q1 by widening more than expected on an annual basis. However, **we expect that the current dip is more of the pothole variety as opposed to something deeper.** Indeed, there were several temporary factors weighing down the deficit over Q1.

First up, agricultural production (and thus exports) was weak over recent quarters and has since rebounded. Moreover, NZ's Terms of Trade are likely to set a record high this year. **The combination of these two factors should send the goods balance back towards surplus by year end, lifting the current account balance with it.**

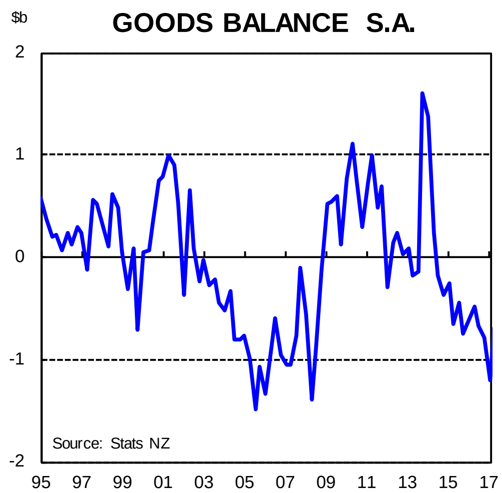
Meanwhile, there are no implications from this release for our GDP or our OCR view. We expect a 0.5% Q1 GDP increase at tomorrow's release.



Comments
The annual current account deficit widened to 3.1% of GDP in Q1 from a revised 2.8% in Q4. This result was larger than the market consensus and our forecast for deficits of 2.7% and 2.8%, respectively. In seasonally-adjusted terms, Q1 had the largest current account deficit since the end of 2008.

In particular, the goods balance was weak. The seasonally-adjusted Q1 deficit widened to $1.2bn from $0.4bn over Q4. Notably, imports of goods were at a record high over Q1.

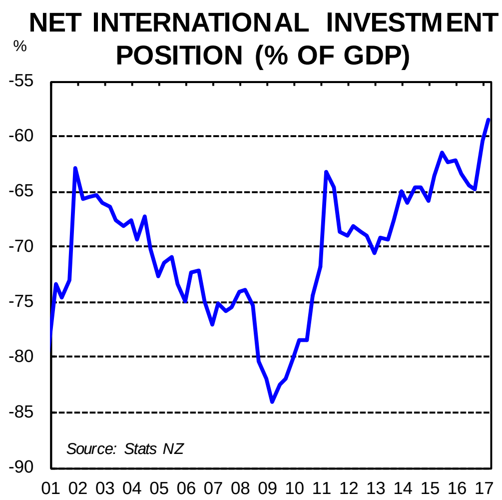
However, **we anticipate that the weakness in the goods balance will be temporary**. NZ's Terms of Trade are at their highest level since the 1970's and are expected to set a record high over 2017. Moreover, previously weak agricultural production is rebounding and will translate into higher export volumes over coming quarters.



Looking at the services balance, **the surplus softened a touch over the quarter**. However, with the Lions tour underway along with the earlier World Masters Games, we expect this weakness will also prove short-lived.

Meanwhile, NZ's net international liability position decreased over Q1 to its lowest recorded level as a % of GDP. The net liability position was $154.8bn (58.5% of GDP), down from a revised $157.5bn (60.4%) in Q4.

In addition, earthquake reinsurance inflows of $116m slowed from Q3. An estimated $516m of outstanding claims relating to the Christchurch earthquakes remain. Meanwhile, **November's Kaikoura earthquake reinsurance claims have been revised higher**. At this juncture, these claims have been estimated at $814m, up from an estimated $694m last quarter. So far just $19m of claims have been settled. As a result, combining claims from both earthquakes, gives a total of $1.311bn in outstanding claims.



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