

New Zealand: a prosperous but vulnerable nation

**Address to the
New Zealand Society of Actuaries Conference**

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Introduction

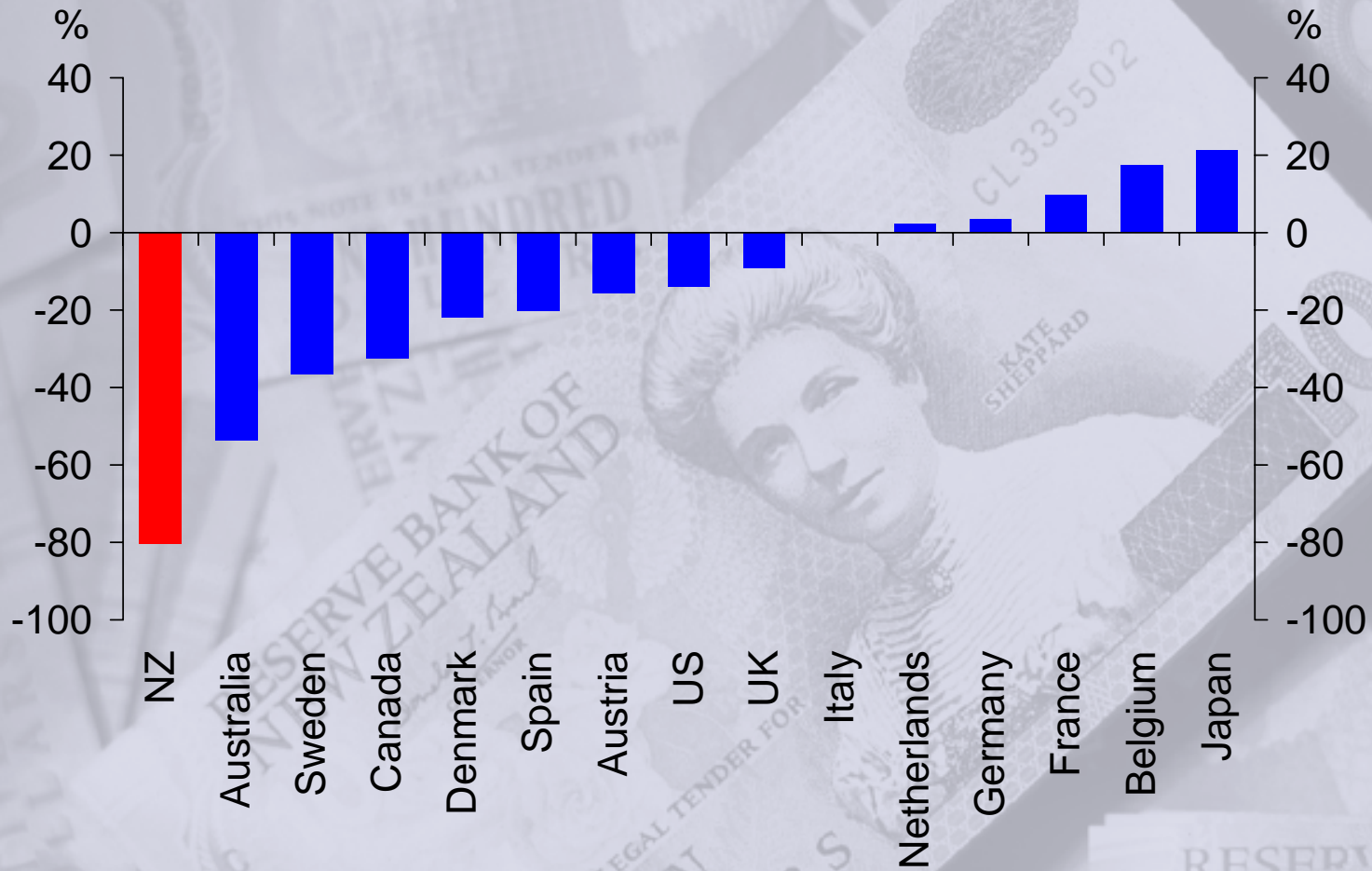
New Zealand's economy is in good shape

But we are vulnerable to shocks because of:

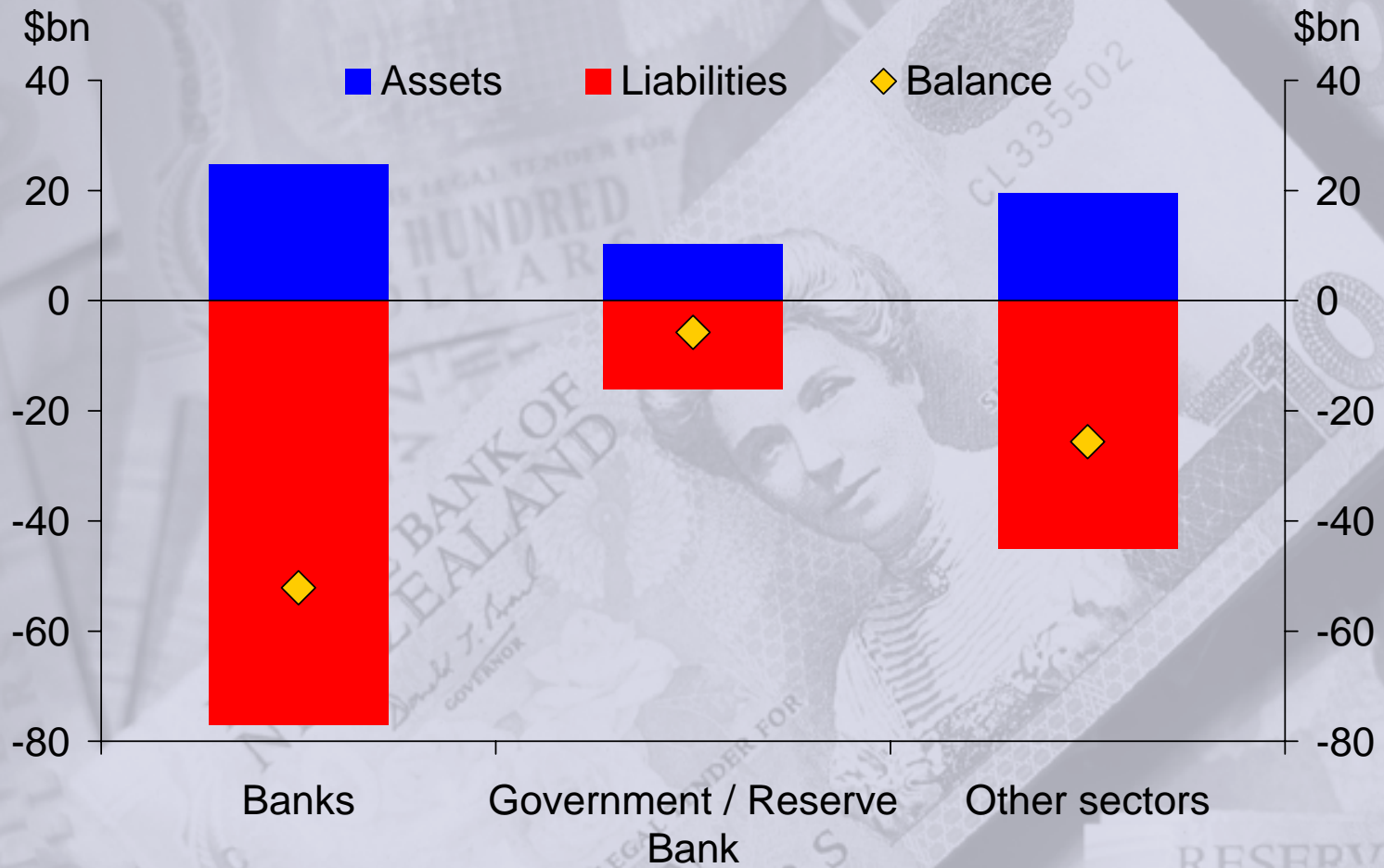
- **Heavy reliance on foreign capital**
- **Low household savings and concentrated wealth**

Net foreign assets

(As a percentage of GDP, 1995-2000 average)



External assets and liabilities

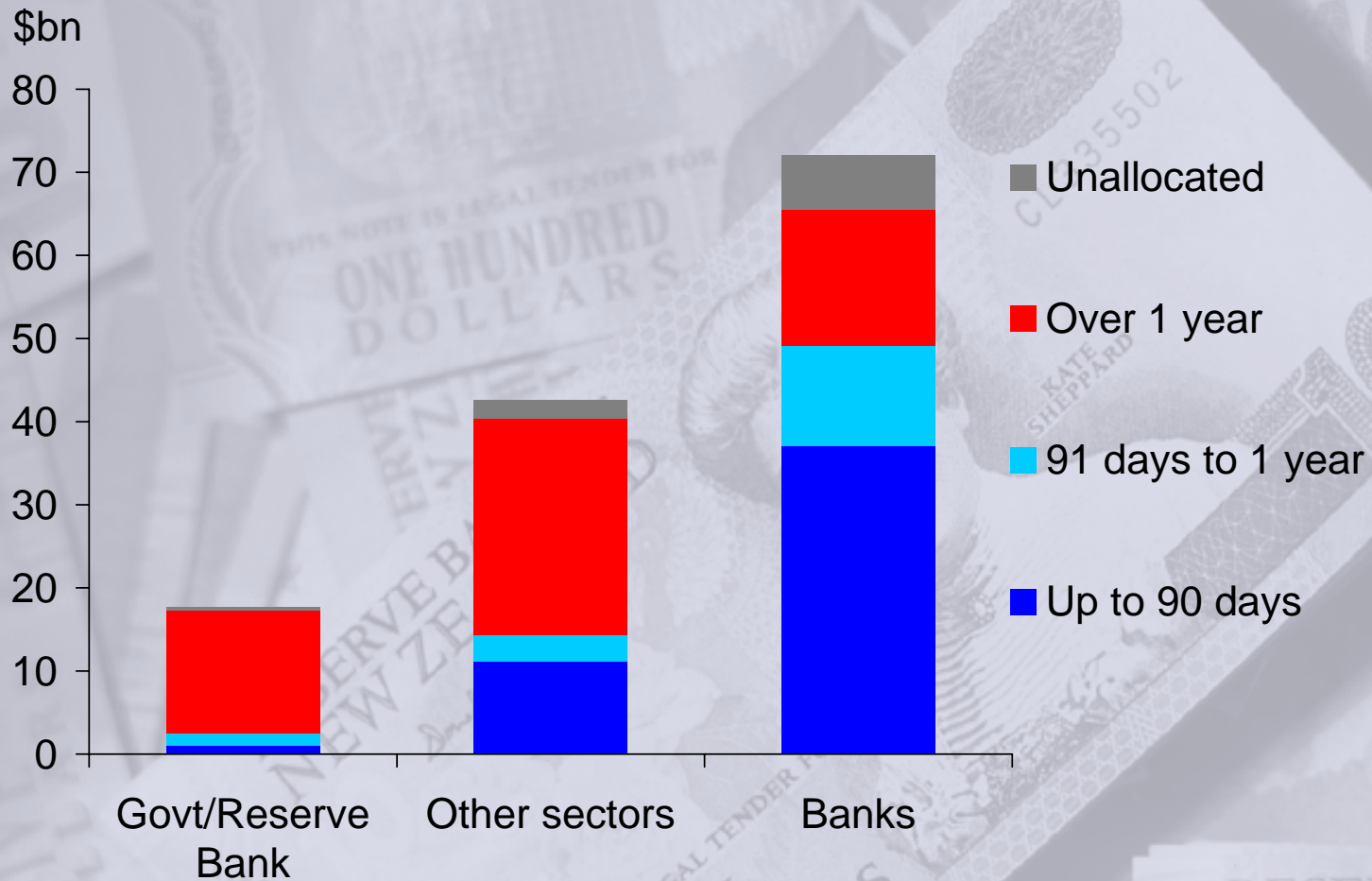


External position

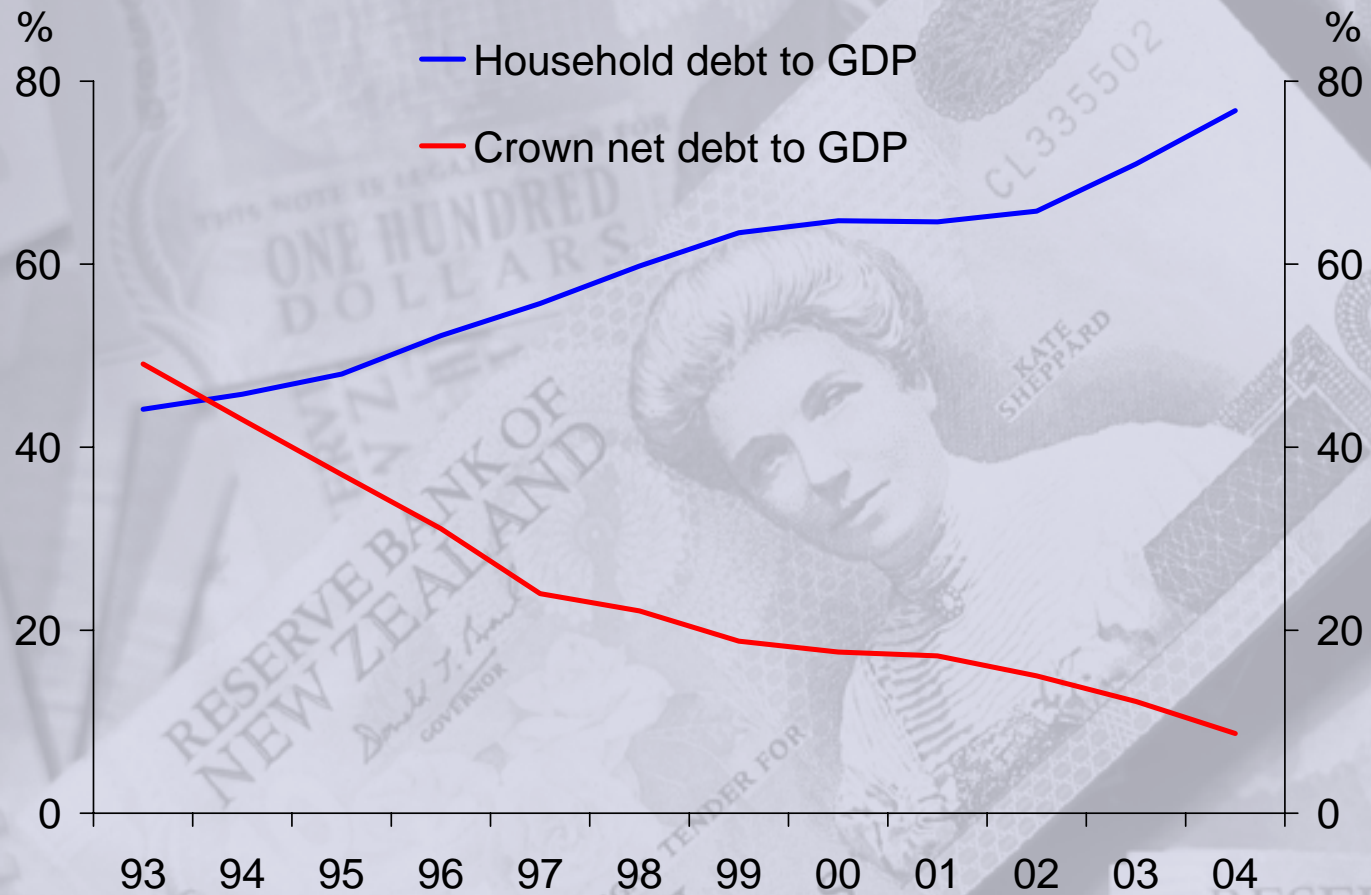
External liabilities present greater risks if they are:

- **Debt (as opposed to equity)**
 - Interest payments
 - Default
- **Short-term**
 - Rollover risk
- **Denominated in foreign currencies**
 - Exchange rate risk (largely hedged in NZ)

External debt tends to be short-term

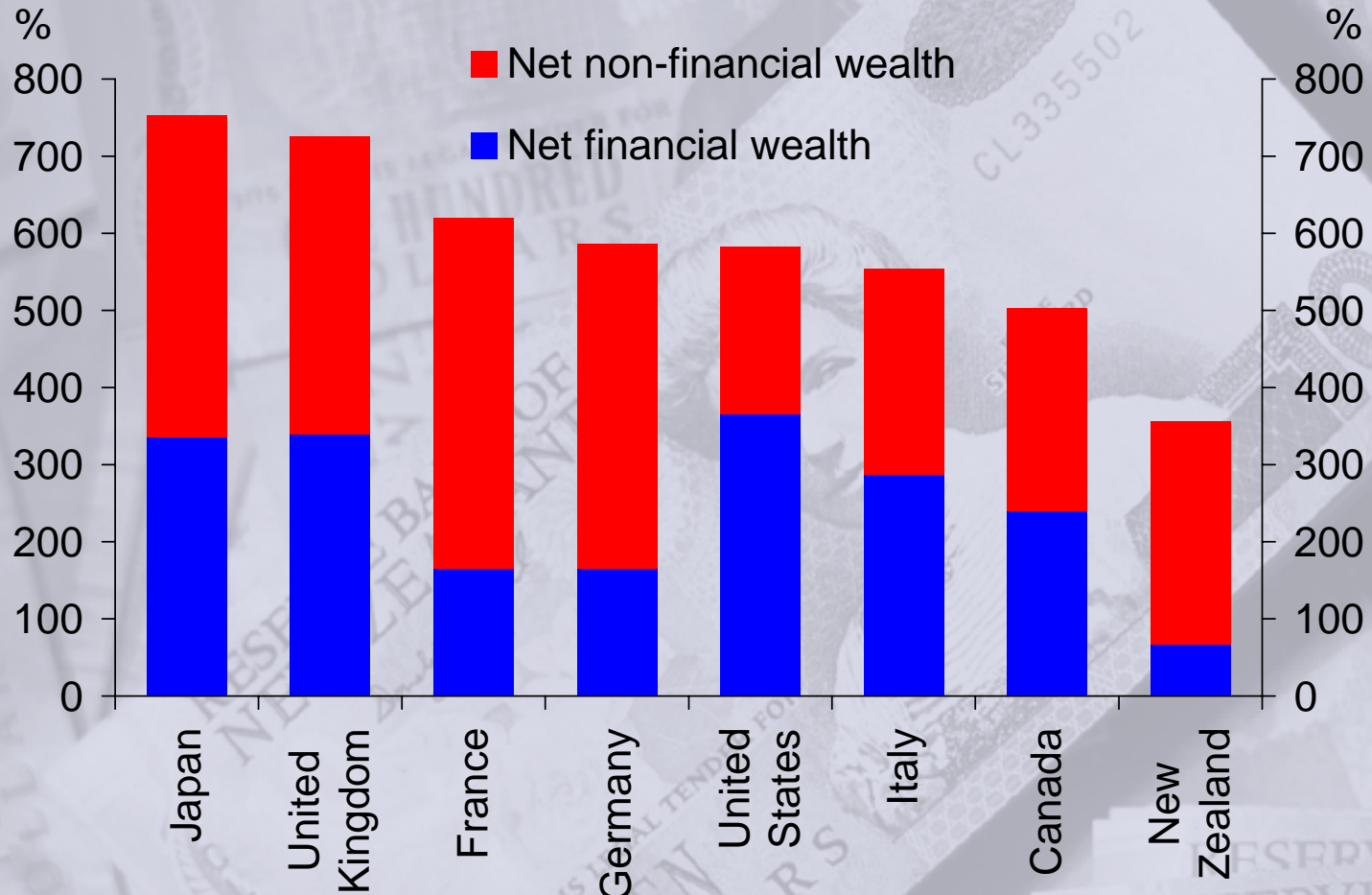


Households are the biggest borrowers



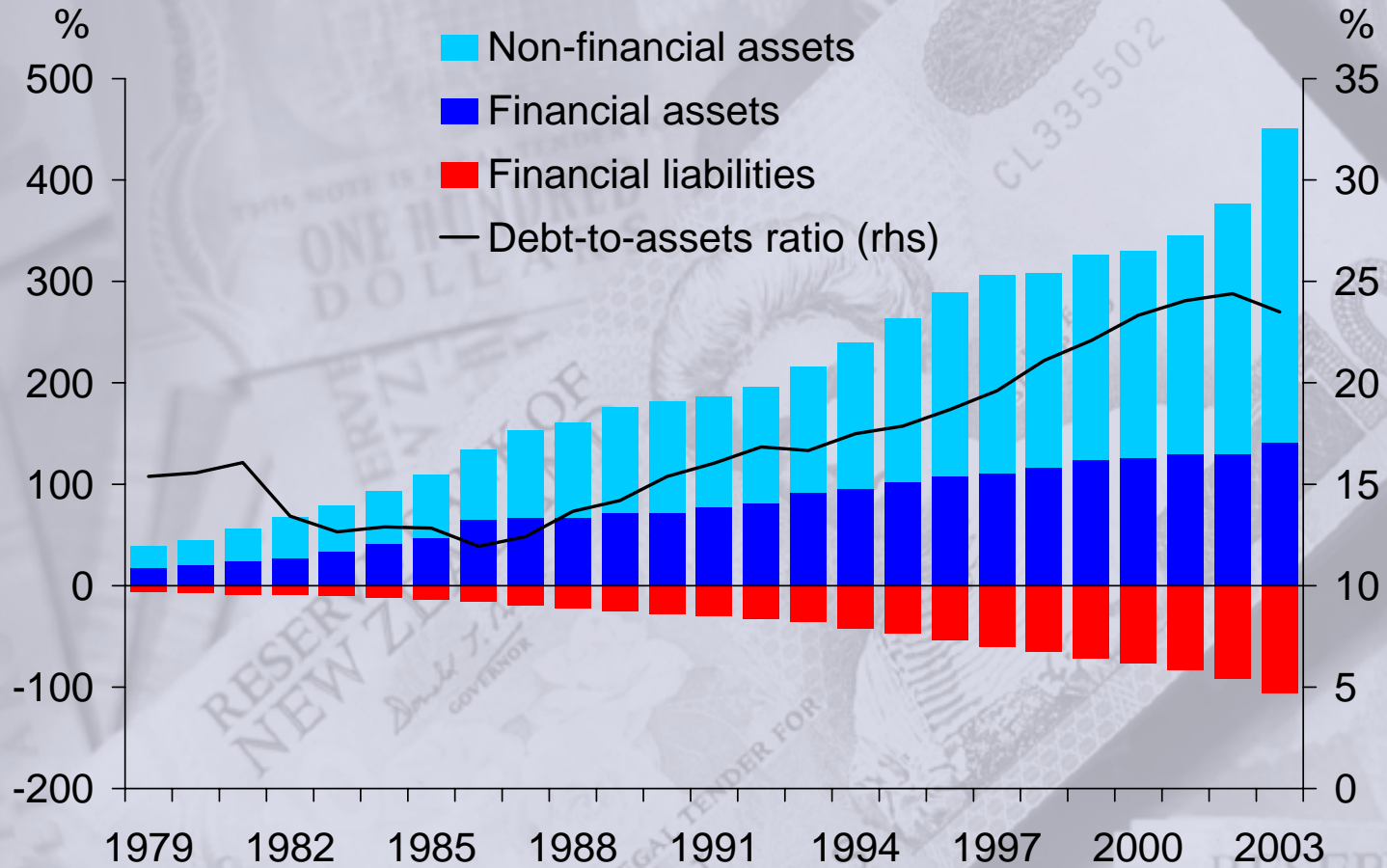
NZ household wealth is relatively low

(As a percentage of disposable income, 2000 data)



Household assets and liabilities

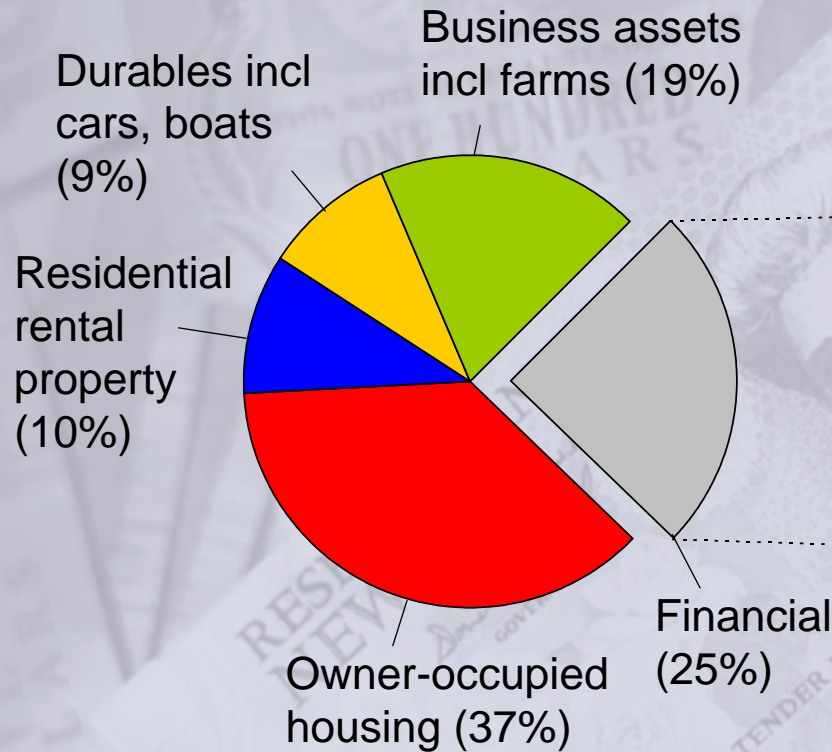
(As a percentage of disposable income)



Composition of household assets

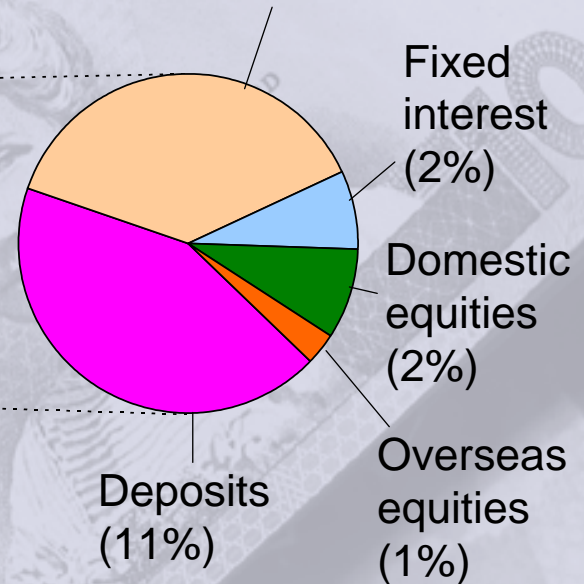
(RBNZ estimates)

Total household assets



Financial assets

Life, super and managed funds (9%)



What is saving? Gratification deferred

Saving = Income – Current Expenditure

- Current expenditure: goods that deliver immediate benefit
- Capital expenditure delivers benefits later

Saving is the mirror image of investment

- Significant definitional concerns

Why is saving so important?

- **Individual level: life-cycle, precautionary, retirement, bequest, target, irrational**
- **Economy-wide: saving is investment (physical and human), and hence economic growth**
- **Financial system vulnerability**

Does NZ lack savings?

Shortage?

- Income flow measures
- Debt levels
- Price of capital
- Household balance sheets
- Ownership of profits

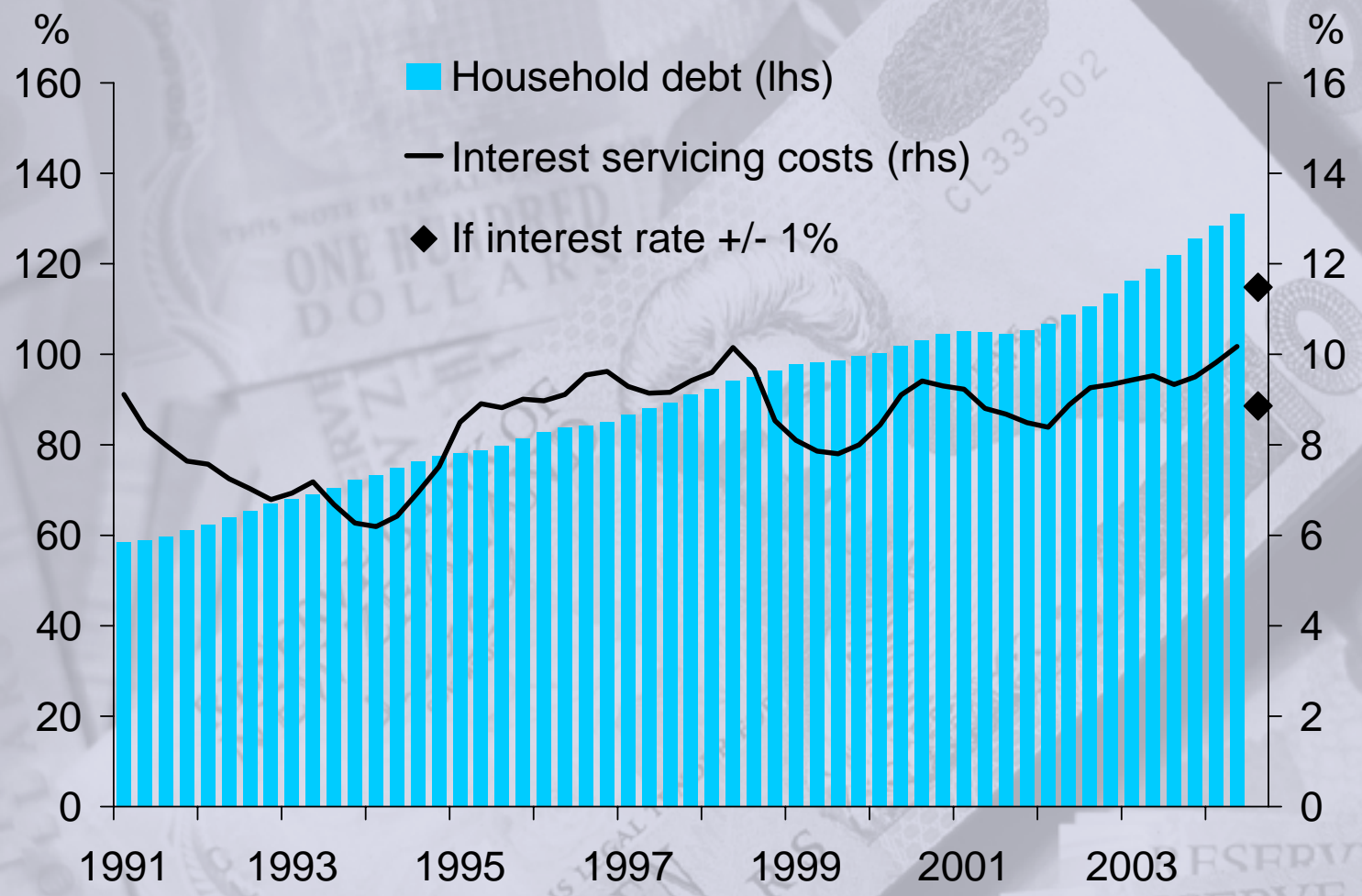
No shortage?

- Stock of wealth
- Open capital market
- Investment levels
- Whole of government

But financial vulnerability is undoubted

Household debt and interest servicing

(As a percentage of disposable income)



Potential financial system shocks

Banking sector

- Balance sheet fragility
- Operational risk
- Major fraud

Macroeconomy

- Recession
- Housing market collapse

Environmental

- Biosecurity, e.g. foot-and-mouth
- Natural, e.g. earthquakes, drought

Other

- Political crisis
- Terrorism

Financial Sector Assessment Programme

- **IMF team reviewed New Zealand's financial system**
 - **Concluded that the financial system is generally in a strong position**
 - **Noted some areas where regulation could be strengthened**
- **IMF also regularly assesses external vulnerabilities in Article IV reviews**

The Reserve Bank's role

Enhancing public awareness

- First *Financial Stability Report* published in October

Developing and extending crisis management capabilities

- Enhanced home-host supervision
- Local incorporation and outsourcing polices

Examining further stress testing

Bolstered foreign reserves