



TE TAI ŌHANGA
THE TREASURY

New Zealand Government Securities Overview

2019/2020: Edition 1

New Zealand Government Securities

New Zealand Government Securities are issued by the Treasury on behalf of the New Zealand Crown¹. These securities provide investors with exposure to a diverse and robust economy, a strong fiscal and institutional framework, a sovereign credit rating in the top twenty globally, and a yield above many peers.

This overview provides investors with insights into New Zealand's:

Economic Backdrop

Institutional Framework

Government Securities Market

It includes practical information on participating in the New Zealand Government Securities Market.

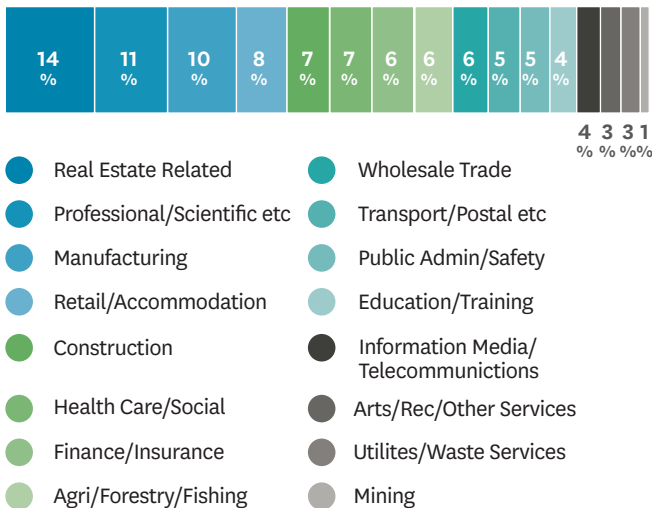
Economic Backdrop

New Zealand is a parliamentary democracy which operates on free market principles. It has a large services sector and a sizable manufacturing sector complementing an efficient export-oriented primary sector.

New Zealand's land size is similar to Japan and the UK but has a resident population of only 4.9 million. The climate is temperate, supporting agriculture, forestry and horticulture. It has abundant natural resources and makes wide use of hydroelectric power generation.

External trade is of fundamental importance to the New Zealand economy. Primary sector products, commodities, manufactured products and services are all important sources of export income. Tourism is the largest services export, as New Zealand is a popular destination for overseas visitors, with education services exports also substantial. Additional services exports include transport, financial and business services, and information technology. Raw materials, consumer goods and capital equipment for industry are important components of New Zealand's imports.

Chart 1: NZ GDP by Industry – Year Ended March 2019



Source: Stats NZ

New Zealand has had a freely floating exchange rate of its currency, the New Zealand Dollar (NZD), since March 1985. There are no exchange controls on foreign-exchange transactions undertaken in New Zealand. The NZD is one of the top 10 traded currencies on a global basis².

Economic Performance

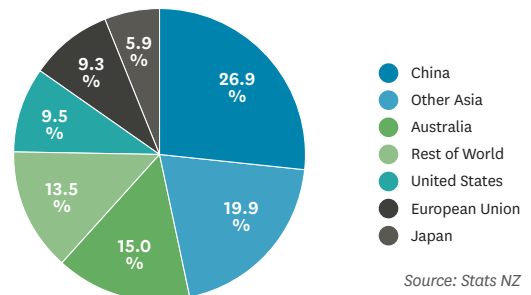
The New Zealand economy has been on a solid footing, with annual real Gross Domestic Product (GDP) growth averaging 3.4% over the past five years. More recently, the economy grew 2.4% in the year to 30 June 2019. This slower, but still solid, growth was driven by an easing in household consumption and business investment growth. Real GDP per capita grew 1.0% in the year. The economy is forecast to grow at an annual average rate of 2.5% over the forecast period (2019/20 to 2023/24) in real terms.

New Zealand generally runs a current account deficit. This has narrowed from almost 8.0% of GDP during the mid-2000s, and was most recently 3.4% in the year to June 2019. Over the same period, New Zealand's net international investment liability has improved from over 80% of GDP to 55%.

New Zealand's unemployment rate in the September 2019 quarter was 4.2%. It has remained around this rate since early 2018. Annual wage growth has accelerated to 3.7% in the September 2019 quarter, from a low of 1.7% in the December 2016 quarter. New Zealand has one of the highest labour participation rates in the OECD, measured at just over 70% by Statistics New Zealand (Stats NZ). The unemployment rate is forecast to remain around 4% throughout the forecast period.

Annual headline CPI inflation was 1.5% in the September 2019 quarter. The Reserve Bank has remained on hold since the official cash rate was lowered to 1.0% in August 2019, noting that economic developments since the August Statement do not warrant a change to already stimulatory monetary policy. Annual headline CPI inflation is forecast to return to 2.0% over the forecast period, supported by accommodative monetary policy and additional government support.

Chart 2: NZ Total Exports – Destination – Year Ended September 2019



Source: Stats NZ

1 The British Crown is the Head of State of New Zealand. New Zealand Government Securities are issued in the name of "Her Majesty the Queen in right of New Zealand".
 2 Bank for International Settlements, Triennial Survey, April 2019, percentage shares of average daily turnover.

Institutional Framework

New Zealand is globally recognised for its robust institutional framework. It ranks highly in all of the World Bank's Governance indicators, illustrating its institutional strength, as shown in Chart 3.

Form of Government

New Zealand is a sovereign state with a democratic parliamentary government based on the Westminster system. Its constitutional history dates back to the signing of the Treaty of Waitangi in 1840, between the British Crown and the indigenous Māori people.

The New Zealand Constitution Act 1852 provided for the establishment of a Parliament with an elected House of Representatives. Universal suffrage was introduced in 1893. New Zealand has the British monarch as titular Head of State. The Queen is represented in New Zealand by the Governor-General, appointed by her on the advice of the New Zealand Government.

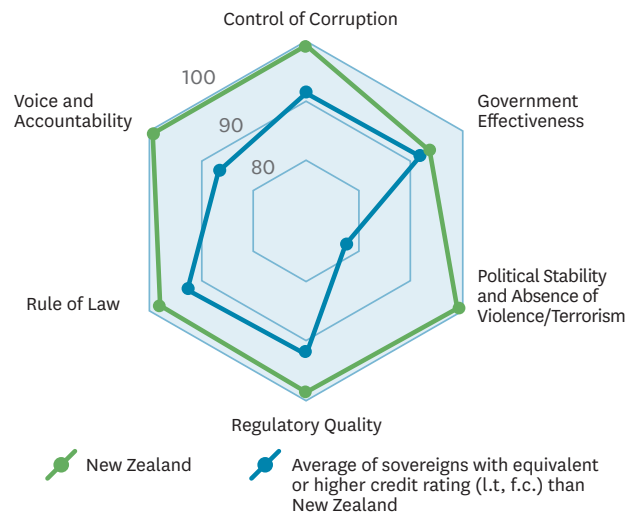
As in the United Kingdom, constitutional practice in New Zealand is an accumulation of convention, precedent and tradition. As such, there is no single document that can be termed the New Zealand constitution. The Constitution Act 1986 however, updated, clarified and combined in one piece of legislation the most important constitutional provisions that had been enacted in various statutes. It provides for a legislative body, an executive and administrative structure and specific protection for the judiciary.

Legislative power is vested in Parliament, a single chambered body titled the House of Representatives. The 120 members are elected for three-year terms through general elections. Eligible residents over 18 years of age may vote in general elections.

The executive Government of New Zealand is carried out by the Executive Council. This is a formal body made up of the Cabinet and the Governor-General, who acts on the Cabinet's advice. The Cabinet itself consists of the Prime Minister and her/his Ministers, who must be chosen from among elected Members of Parliament. Each Minister supervises, and is responsible for, particular areas of government administration. Collectively, the Cabinet is responsible for all decisions of the Government.

As a result of a referendum held in conjunction with the 1993 election, New Zealand changed from a "First Past the Post" (FPP) system of electing Members of Parliament to a "Mixed Member Proportional" (MMP) system of proportional representation. Under MMP, the total number of seats each party has in Parliament is proportional to that party's share of the total list vote. This change was implemented in the 1996 election. The judicial system in New Zealand is based on the British model. By convention and the Constitution Act 1986, the judiciary is independent from the executive.

Chart 3: Percentile Ranking on Key Governance Indicators



Source: World Bank Worldwide Governance Indicators - 2018

Monetary Policy Framework

The Reserve Bank of New Zealand (RBNZ), was established as a Central Bank in 1934. The Reserve Bank of New Zealand Act 1989 (the Act) cemented its independence. It is responsible for monetary policy and financial stability policy.

On 1 April 2019, amendments to New Zealand's monetary policy framework, under the Act, came into effect. Previously, New Zealand's monetary policy was directed towards maintaining stability in the general level of prices. The amended Act includes 'supporting maximum sustainable employment' as an economic objective alongside price stability.

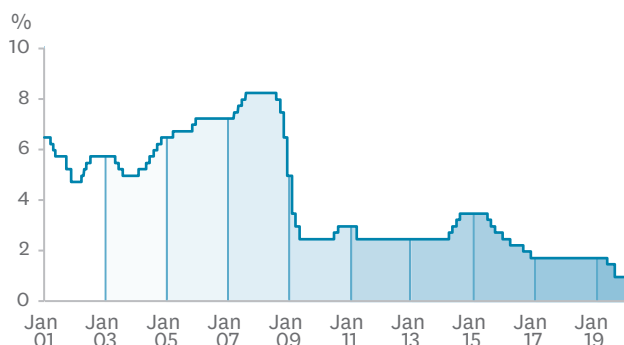
The amended Act also introduces a committee decision-making model for monetary policy, the Monetary Policy Committee (MPC). In addition, the Policy Targets Agreement that had previously been signed by the Governor of the RBNZ and Minister of Finance, is replaced by a remit issued by the Minister of Finance to the MPC.

For the purpose of the remit, issued in May 2019, the MPC's operational objectives are "to keep future annual inflation between 1 and 3% over the medium term, with a focus on keeping future inflation near the 2% mid-point", and "to support maximum sustainable employment". In particular, the MPC is required to seek to avoid unnecessary instability in output, interest rates, and the exchange rate. It must also have regard to the efficiency and soundness of the financial system.



A second phase of review of the RBNZ Act is currently underway. It considers the RBNZ’s responsibilities in promoting the maintenance of a sound and efficient financial system. This includes the implementation of prudential policies, such as capital and liquidity standards, macro-prudential policy and undertaking supervision of banks. It is envisaged that the legislative change process can be advanced within the current Parliamentary term.

Chart 4: NZ Official Cash Rate



Source: RBNZ

Fiscal Policy Framework

The Public Finance Act 1989 requires the New Zealand Government to be transparent in both its short- and long-term fiscal objectives and to maintain prudent debt levels. The current and recent Governments show a strong commitment to prudent fiscal management.

The Public Finance Act stipulates the Treasury must publish economic and fiscal forecasts twice a year. These occur at the time of the mid-year Budget (*Budget Economic and Fiscal Update* – BEFU) and at the end of the calendar year (*Half Year Economic and Fiscal Update* – HYEFU). The Treasury must also provide a *Pre-election Economic and Fiscal Update* (PREFU) prior to general elections, which occur at least every three years³. The forecasts extend for four years beyond the current fiscal year ie, “the forecast period”.

Without parliamentary authority, the Government has no authorisation to incur expenses and capital expenditure and spend public money. An Appropriation Act is the means by which Parliament approves expenses and capital expenditure for the Government for the coming year.

This is supplemented by spending that is authorised under Permanent Legislative Authority which continues in effect until revoked by Parliament. The payment of interest on debt is an example of spending authorised under Permanent Legislative Authority.

³ Publication of the HYEFU is not required in the year if the PREFU is published between 1 October and 31 December.

Fiscal Strategy

The Government formally communicates its fiscal strategy twice a year, typically alongside the BEFU and HYEFU. The Government sets out its short-term intentions and long-term objectives with respect to core parameters such as debt, operating expenses, operating revenue, the operating balance and net worth. The Fiscal Strategy Report is released alongside the BEFU. The Budget Policy Statement is generally released alongside HYEFU.

The Government’s most recent Budget Policy Statement was published in December 2019. Its short-term fiscal intentions are to:

- Deliver a sustainable operating surplus across an economic cycle.
- Maintain net debt within a range between 15 and 25 per cent of GDP.
- Prioritise investments to address the long-term financial and sustainability challenges facing New Zealand.
- Take a prudent approach to ensure expenditure is phased, controlled and directed to maximise its benefits. The Government will maintain its expenditure to within the recent historical range of spending to GDP.
- Ensure a progressive taxation system that is fair, balanced and promotes the long-term sustainability and productivity of the economy.

The Government has demonstrated its continued commitment to prudent fiscal strategy throughout its term to date.

The Government also recognises the importance of maintaining a sustainable New Zealand Government Bond (NZGB) market. The *Fiscal Strategy Report 2019* reaffirmed the Government’s commitment to maintain levels of NZGBs on issue at not less than 20% of GDP over time, even if net core Crown debt were to fall below 20% of GDP.

Fiscal Performance

In recent years the Government has been running an operating surplus. In 2018/19 the operating balance before gains and losses was a surplus of NZD 7.3 billion (2.4% of GDP). An operating deficit of 0.3% of GDP is forecast 2019/20, with gradually increasing surpluses over the remainder of forecast period.

Core Crown expenditure, as a proportion of GDP, is forecast to peak in 2020/21, at 29.4%, before declining to 28.1% in 2023/24.

Core Crown residual cash was in deficit in 2018/19. In the current and subsequent four fiscal years, forecast capital spending is expected to drive core Crown residual cash deficits. In 2023/24 a cash surplus is forecast to be restored.



Net core Crown debt was 19.0% of GDP in 2018/19. This ratio is forecast to increase slightly, peaking at 21.5% in 2021/22, before gradually declining to reach 19.6% in 2023/24.

Environmental, Social and Governance (ESG) Considerations

The New Zealand Government has clearly stated Environmental, Social and Governance objectives. Many of these are outlined in the Government’s Wellbeing Budget 2019 which focuses on the wellbeing of people, the health of the environment and the strength of the community⁴.

The Government is committed to progressing a climate change programme that allows for a just transition to a low-emissions economy. Cabinet has agreed a framework which will drive climate change policy towards low greenhouse gas emissions and climate resilience in New Zealand⁵.

The framework supports New Zealand’s commitments under the Paris Agreement, including the target to reduce emissions by 11% below 1990 levels by 2030. In November 2019, the Government passed an Amendment to the Climate Change Response Bill that set new reduction targets by 2050 for greenhouse gases (to net zero) and biogenic methane (below 2017 levels by between 24%

and 47%). These targets are in addition to establishing an independent Climate Change Commission to provide advice to Government on climate change mitigation and adaptation, and to monitor progress towards the new 2050 target and emissions budgets.

Securities Law

The Financial Markets Authority Act 2011 establishes the Financial Markets Authority (FMA) as New Zealand’s market conduct regulator. The FMA is an independent Crown Entity whose main objective is to promote and facilitate the development of fair, efficient and transparent financial markets. The FMA enforces financial markets legislation, including the Financial Markets Conduct (FMC) Act.

The FMC Act 2013 regulates the offering and trading of investments and the provision of certain financial services. It regulates the operation of securities and derivatives exchanges and trading behaviour on those exchanges. It also provides general prohibitions on misleading and deceptive conduct in financial markets. New Zealand Government Securities are “securities” for the purposes of the FMC Act.

Table 1: Summary of the Treasury’s Economic and Fiscal Forecasts

Year Ending 30 June	Actual	Forecast				
	2019	2020	2021	2022	2023	2024
Economic						
Real GDP (production basis, annual average % change)	2.4	2.2	2.8	2.7	2.5	2.4
Real GDP per capita (production basis, annual average % change)	0.8	0.7	1.4	1.3	1.1	1.1
Unemployment rate (% of labour force, June quarter)	3.9	4.3	4.2	4.2	4.3	4.3
CPI inflation (annual % change, June quarter)	1.7	1.9	1.9	2.0	2.0	2.0
Current account balance (% of GDP)	-3.4	-3.2	-3.4	-3.6	-3.7	-3.8
Fiscal (% of GDP)						
Core Crown tax revenue	28.4	27.7	28.0	28.0	28.2	28.4
Core Crown expenses	28.6	29.3	29.4	28.8	28.6	28.1
Total Crown Operating balance before gains and losses	2.4	-0.3	0.0	0.5	1.1	1.5
Core Crown residual cash	-0.2	-1.6	-2.4	-1.6	-0.6	0.2
Net core Crown debt	19.0	19.6	21.0	21.5	20.9	19.6
Net worth attributable to the Crown	45.9	43.7	42.6	42.2	42.5	43.5

Source: The Treasury, in conjunction with HYEUFU, 11 December 2019

⁴ <https://treasury.govt.nz/publications/wellbeing-budget/wellbeing-budget-2019>

⁵ <https://www.mfe.govt.nz/climate-change/climate-change-and-government/climate-change-programme>



New Zealand Government Securities Market

New Zealand Debt Management is a function of the New Zealand Treasury. Its primary responsibility is the efficient management of the Crown's debt and associated financial assets within an appropriate risk management framework. The maintenance of a well-functioning New Zealand Government Securities market is central to this remit.

The New Zealand Crown has always paid, when due, the full amount of principal, interest and amortisation requirements upon its external and internal debt, including guaranteed debt.

New Zealand Government Securities

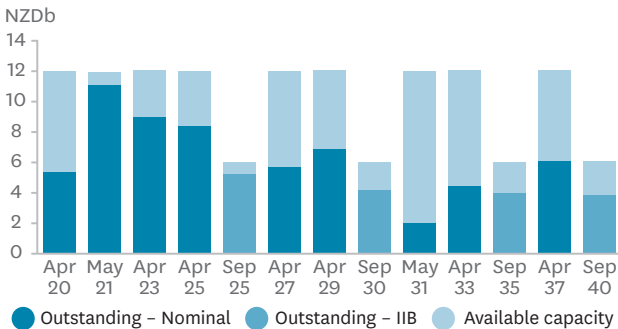
The New Zealand Debt Management function manages the issuance of nominal bonds, inflation-indexed bonds (IIBs) and Treasury Bills (T-Bills) in the wholesale market.

At 30 November 2019 there were NZD 79.1 billion of bonds on issue. Of these, NZD 75.8 billion were market bonds that may be freely traded in the secondary market. In addition, there were NZD 2.4 billion of T-Bills on issue.

Over the forecast period, total outstanding market bonds are projected to remain between NZD 70 and 90 billion. The Government's stated commitment to maintain NZGBs on issue at not less than 20% of GDP over time ensures long-term durability of the NZGB market, even if net core Crown debt were to fall below 20% of GDP.

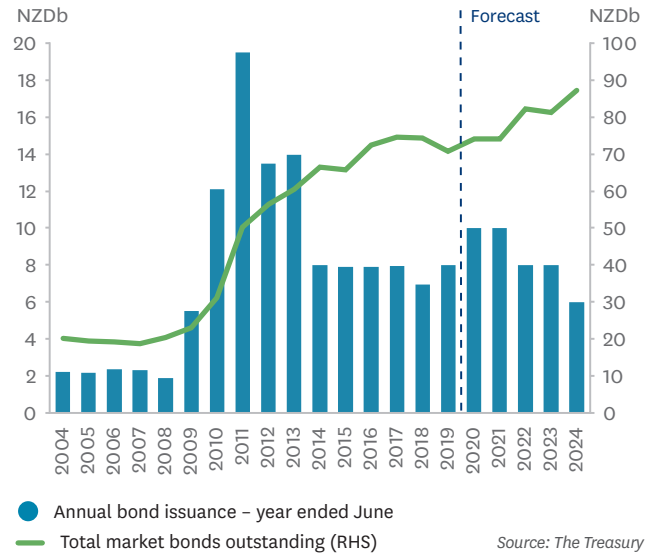
At 30 November 2019 there were nine nominal bond and four IIB maturities as shown in Chart 5. Individual nominal bond maturities are capped at NZD 12 billion face value outstanding, while IIB maturities are capped at NZD 6 billion. Coupons on nominal bonds are paid on a semi-annual basis, in arrears. For IIBs, coupons are paid quarterly.

Chart 5: Outstanding NZGBs and Capacity for Issuance – At 30 November 2019



Source: The Treasury

Chart 6: Total NZGBs and Projections



Source: The Treasury

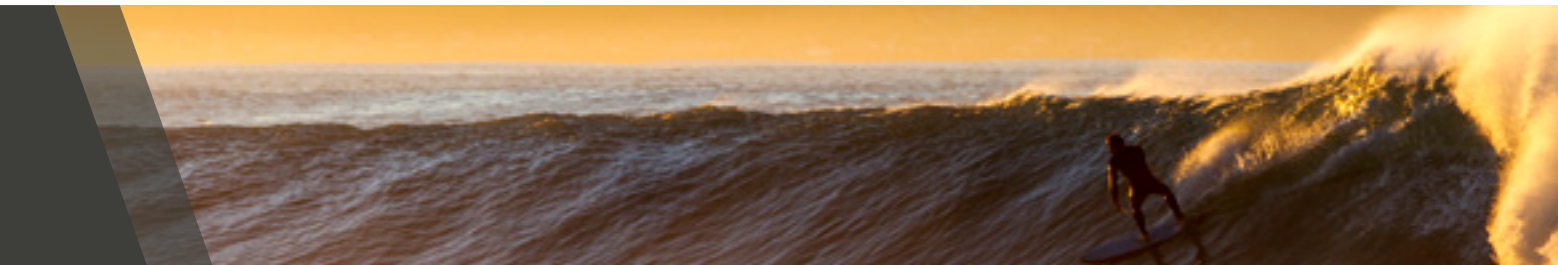
Credit Ratings

New Zealand's credit rating is within the top twenty sovereign ratings globally. Rating agencies S&P Global Ratings and Fitch Ratings currently maintain an AA long-term foreign currency rating for NZGBs. In January 2019, S&P Global Ratings revised the outlook on New Zealand's long-term rating from stable to positive based on their view that the general government budget could achieve a surplus in the early 2020s. Moody's Investor Service has maintained an Aaa long-term foreign currency rating on the bonds since October 2002.

Table 2: NZGB Long-term Credit Ratings

Rating Agency	Local Currency	Foreign Currency	Latest Update
Moody's Investor Service	Aaa (stable outlook)	Aaa (stable outlook)	Sep-18
S&P Global Ratings	AA+ (positive outlook)	AA (positive outlook)	Jan-19
Fitch Ratings	AA+ (stable outlook)	AA (stable outlook)	Jan-19

Source: Moody's Investor Service, S&P Global Ratings, Fitch Ratings



Primary Issuance

Primary issuance of New Zealand Government Securities is undertaken through competitive tenders and/or syndications.

The BEFU and HYEUFU announcements contain a breakdown of the core Crown's funding needs and annual bond issuance forecasts. They also include forecasts of the level of T-Bills on issue. The most recent update, published alongside HYEUFU on 11 December 2019, is shown in Table 3.

Ahead of each quarter, a regular bond issuance schedule is announced, including the full details of tender dates, maturities, and volumes. This will generally occur at the time of the confirmation announcement for the last tender of the preceding quarter.

In September 2019, the New Zealand Debt Management team introduced changes to the Primary Market Access Framework, which has created a more formalised relationship with the intermediaries involved in the NZGB market. The ultimate objective of the changes was to assist Registered Tender Counterparties (RTC) perform their role of intermediating primary market issuance to end investors and to support secondary market liquidity. RTCs are listed on the New Zealand Debt Management website⁶, to create visibility for investors regarding those entities that have primary market access and are regular participants in the NZGB market.

NZGB tenders are typically held on Thursdays. Only RTCs may take part in tenders. Interested parties may offer their bids through a RTC. Bids must be submitted by 2pm on the day of tender. The minimum denomination is NZD 1 million (principal) and in multiples of NZD 1 million thereafter.

T-Bills are also issued via tender. These occur fortnightly, on Tuesdays, when bids need to be submitted by 2pm. Typically 3 month, 6 month and 12 month maturities are offered. The volume and maturities on offer may vary and are announced the day prior to tender.

Syndication has historically been confined to launching a new bond. This method enables the placement of a large volume into the market, promoting liquidity in the new bond from initiation. Recent syndication volumes have been between NZD 1.5 and 2.0 billion.

Secondary Market

The secondary market is supported by major local banks and global intermediaries. There is a repurchase market for NZGBs. RBNZ also offers a bond lending facility as a lender of last resort.

NZGB yields generally trade above global developed market peers. Chart 7 shows generic 10-year NZGBs yields relative to sovereign peers with similar credit ratings, as captured in Chart 3. Over the past two decades, generic 10-year NZGBs have traded between -70bps and 320bps over their US equivalents. Over the same period, they have traded between -40bps and 110bps over Australian equivalents.

In terms of absolute levels, NZGB yields have been on a declining trend in recent decades, in line with the global disinflationary trend. Specifically in New Zealand, the RBNZ Act of 1989 entrenched an inflation-targeting mandate. This has contributed to structurally lower yields as inflation expectations have declined.

Table 3: Forecast – New Zealand Government Bonds and Treasury Bills

Year Ending 30 June (face value)	2020	2021	2022	2023	2024	Total
Gross NZGB issuance (NZD billion)	10.0	10.0	8.0	8.0	6.0	42.0
NZGB maturities and repurchases (NZD billion)	6.6	9.8	0.0	8.9	0.0	25.4
Net NZGB issuance (NZD billion)	3.4	0.2	8.0	-0.9	6.0	16.6
NZGBs on issue (NZD billion)	74.0	74.1	82.1	81.2	87.2	n/a
NZGBs on issue (% of GDP)	23.5%	22.4%	23.5%	22.2%	22.7%	n/a
Forecast T-Bills on issue*	3.0	4.0	4.0	4.0	2.0	n/a

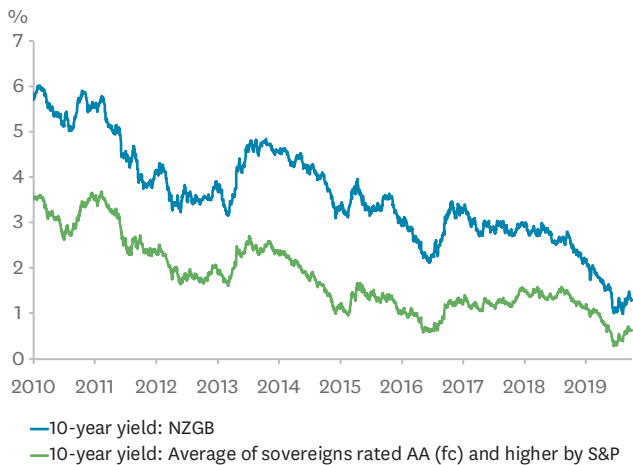
* The forecasts show current expectations of how short-term cash liquidity needs will be met at fiscal year-end. However, the actual issuance of T-Bills, may vary from forecast, based on actual short-term cash needs and an assessment of relative costs.

Source: The Treasury, in conjunction with HYEUFU, 11 December 2019

6 The list is available at <https://debtmanagement.treasury.govt.nz/government-securities/primary-market-access-information>



Chart 7: NZGB Yields Relative to Peers with Similar Rating⁷



Source: Bloomberg

Considerations for Non-Residents

For non-resident investors, NZGBs are effectively free from withholding tax. While NZGBs are subject to an Approved Issuer Levy like other New Zealand bond issues, the Crown will pay this tax on behalf of non-resident investors.

At 30 October 2019, 52.8% of NZGBs were held by non-resident investors. Over the past fifteen years this percentage has ranged between 50% and 80%. Participants in the market are diverse by type and by regional location. Nominal NZGBs and IIBs are currently constituents of a number of global benchmark bond indices.

New Zealand Government Securities are currently issued only in New Zealand dollars. However, documentation is maintained to enable issuance in alternative currencies.

Investor Communications

The New Zealand Debt Management team at the Treasury maintains regular contact with investors via a variety of channels and welcomes enquiries.

To receive communications via email please contact: debtmanagement@treasury.govt.nz

For further information on New Zealand Government Securities see: debtmanagement.treasury.govt.nz

For detailed current economic information see: treasury.govt.nz

For further information on the RBNZ see: rbnz.govt.nz

For further information on the New Zealand Government's Wellbeing Budget policies see: budget.govt.nz

⁷ Of the 12 sovereign peers captured in Chart 3, Kuwait, Liechtenstein, and Luxembourg are excluded.

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