
Volume 72 No. 1, March 2009

Contents

| | |
|---|----|
| Editor's note | 3 |
| Articles | |
| Financial vulnerability of mortgage-indebted households in New Zealand – evidence from the Household Economic Survey <i>Mizuho Kida</i> | 5 |
| Thinking about more than one thing at a time: Eric Leeper on monetary and fiscal policy interactions <i>Interview by Tim Ng</i> | 13 |
| Recent trends and developments in currency <i>Alan Boaden and Kristin Langwasser</i> | 23 |
| Overview of a recent Reserve Bank workshop: nowcasting with model combination <i>Kirdan Lees</i> | 31 |
| Coping with global financial and economic stresses <i>Alan Bollard and Tim Ng</i> | 34 |
| For the record | |
| Discussion papers | 46 |
| News releases | 47 |
| Publications | 53 |
| Articles in recent issues of the Reserve Bank of New Zealand <i>Bulletin</i> | 55 |

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ISSN 1174-7943 (print)
ISSN 1177-8644 (online)



Editor's note

In this edition of the Reserve Bank *Bulletin* we present five articles covering a range of topics.

Our first article, by Mizuho Kida, discusses financial vulnerability in the household sector. Between 2001 and 2008, aggregate household debt more than doubled, alongside similarly rapid increases in house prices. Now, with house prices falling and the economy weakening, questions arise about the risk of households being unable to meet their debt obligations. The article presents evidence and modelling results suggesting that household financial vulnerability did not greatly increase during the debt build-up, though a small proportion of households remains vulnerable under certain scenarios.

Our second article is an interview with Eric Leeper, Professor of Economics at Indiana University. Professor Leeper visited New Zealand in 2008 as the Reserve Bank and Victoria University of Wellington Professorial Fellow. Eric and I chat about his work on advancing the modelling of fiscal policy and its interaction with monetary policy, how fiscal policy could be enhanced by making it more transparent, and the progress of fiscal and monetary policymakers so far in handling the current financial and economic crisis.

In our third article, Alan Boaden and Kristin Langwasser present our annual review of trends in the use of banknotes and coins. Last year, there was an unusual increase in issuance of \$50 and \$100 notes late in 2008, associated with public nervousness about the state of the financial sector. The article also discusses the physical quality of our banknotes, and the rate of counterfeiting in New Zealand.

Kirdan Lees presents in our fourth article an overview of a recent workshop held at the Reserve Bank on technical advances in the forecasting of current or near-term economic conditions. He notes some themes that emerged from the workshop, including how the combination of forecasts from different models can improve forecasts. Full papers from the workshop are available on the Reserve Bank's website.

Our fifth article is a reprint of the paper for a speech delivered by Governor Alan Bollard to the Canterbury Employers' Chamber of Commerce in January. The paper discusses how the current economic and financial crisis reflects a correction of the large economic imbalances built up over this decade,

with associated vulnerabilities in the world financial system. It puts into international context New Zealand's position and policy responses so far in this crisis, and looks at how New Zealand households, firms and banks might be expected to cope with the stresses.

I hope you enjoy the range of articles in this edition.

Tim Ng

Editor



**RESERVE
BANK**
MUSEUM

The Reserve Bank Museum celebrates and records New Zealand's economic and banking heritage.

Displays range from timelines and interactive exhibits to comprehensive display panels outlining both the Reserve Bank's history and role, and how the New Zealand economic system has developed.

Artefacts include the only working example in New Zealand of the MONIAC hydro-mechanical econometric computer developed by New Zealand economist and inventor Bill Phillips in the late 1940s.

In early 2008, the museum received its 10,000th visitor.

The museum is open 9.30a.m.–4.00p.m. weekdays. It is closed weekends, public holidays, and for special events. Please call to confirm opening hours.

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Photography by Stephen A'Court.