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Commentary

Thanks to all those who completed the survey about the Bulletin. We'll report on its findings and our response in the next issue of the Bulletin.

The international economy: risks and opportunities

Summary

International agencies and many commentators including the Minister of Finance in his "state of the economy" speech last week, have been writing about the growing dangers in the international economy. This commentary looks at those dangers, the potential effect on New Zealand, and what policies are needed to put us in a good condition to weather the turmoil should it occur.

A number of factors make the international economic situation particularly worrying. Firstly most of the world's major economies are in trouble: particularly the European Union (EU), China, and the US. Secondly there are major tensions such as the refugee crisis in Europe, in turn driven by the increasingly complex situation in the Middle East, and toxic political deadlock in the US. Finally, the major financial centres of the world – mainly in the U.K., Europe and the US – have not fixed the problems that led to the 2008 crash and the Global Financial Crisis (GFC), in the face of resistance from the powerful financial sector. That, along with political barriers in the US and the EU makes their debt situations difficult to resolve.

A more immediate worry is that many of the cushions that reduced the effects of the GFC have gone. We cannot count on China or the US keeping the international economy working. Many developed economies (though not New Zealand) have high public debt which reduces government capacity – at least in the eyes of the financial markets – to respond by stimulating and stabilising the economy. Interest rates are already very low so cannot be reduced. So we must rely more on government spending, and 'unorthodox' measures such as central bank credit – but in more effective ways than the 'quantitative easing' bailouts of the finance sector.

Another crisis is far from a certainty – don't panic – but it is difficult to judge just how likely a downturn or crisis may be. The possibilities are enough of a worry that we should be thinking about whether we are properly prepared, and I make some suggestions how. It is important to learn from the disastrous mistakes that are still being made around the developed world, and from new thinking that has not yet permeated through to government circles in Wellington. Out of crisis comes opportunity: many of these preparations are policies needed for a better New Zealand.

International agencies and many commentators including the Minister of Finance in his "state of the economy" speech last week, have been writing about the growing dangers in the international economy. In this commentary I will look at those dangers, the potential effect on New Zealand, and what policies are needed to put us in a good condition to weather the turmoil should it occur.

International worries

Concerns about the international economic situation are mounting. A number of factors make it particularly worrying. Firstly most of the world's major economies are in trouble: particularly the European Union (EU), China, and for somewhat different reasons the US. Secondly there are major tensions such as the refugee crisis in Europe, in turn driven by the increasingly complex situation in the Middle East. Finally, the major financial centres of the world – mainly in the U.K., Europe and the US – have not fixed the problems that led to the 2008 crash and the Global Financial Crisis (GFC).

The problems in the major economies of the world are linked but take different forms.

Europe

In the EU, and particularly among its members which have adopted the Euro as their currency (the Euro area), there are still huge economic and financial problems unresolved since the GFC. Economic growth is still weak, with the economies of several countries, including Greece, shrinking. Unemployment remains very high at 10.5 percent in the Euro area and 9.0 percent in the EU: a quarter of the people of Greece wanting work (24.7 percent) can't find jobs, 21.0 percent in Spain, 12.1 percent in Portugal, and 11.4 percent in Italy. These economic conditions have been exacerbated by the austerity policies followed voluntarily in the case of the U.K. and forced upon others such as Greece which is in a deep depression, and Spain.

The tension created by Germany's economic policies is unresolved. It maintains its international competitiveness as one of the world's major exporters in part by holding down wages and selling to countries in the south of the Euro area such as Greece, Italy, Spain and Portugal. They are then unable to build their own export capacity because of (for them) an overvalued Euro and lack of demand in the North. The Euro is a recipe for continued economic crisis unless all countries including Germany surrender more of their economic independence to form a union that is "fiscal" (sharing tax revenues and government expenditure) as well as monetary. That situation too is unresolved.

Like the US, the EU has huge levels of debt, some existing before the GFC, some created by the "quantitative easing" policies in the U.K. to bail out its large, damaged financial sector, more recently replicated by the European Central Bank. In addition public debt has grown in response to the crisis. Paying off the debt will take years – some economists (for example C. M. Reinhart & Rogoff, 2013; C. Reinhart & Sbrancia, 2015) say it cannot be done without inflation (to reduce its value) or 'financial repression' – a refusal by governments to repay on the original terms. Reinhart and Rogoff point out that "debt restructuring or conversions, financial repression, and a tolerance for higher inflation, or a combination of these were an integral part of the resolution of significant past debt overhangs". The alternative is many years of stagnation as Japan has experienced. I return to this below.

The EU's political ability to resolve this already immensely complicated set of issues is further weakened by the current refugee crisis from the war in the Middle East. While the EU's reaction has on the whole been considerably more humane than many other countries, the longer the crisis continues the more pressure it will place on EU internal relationships.

China

China has embarked on a major restructuring of its economy, from one focused on investment and exporting to one that concentrates more on providing goods and services for its own people. The rapidly rising incomes of Chinese working people increase demand for consumer goods and services within China, rather than continuing their very high current level of saving. China is also deliberately reducing its dependence on high-carbon and environmentally damaging raw materials such as coal. The transformation is also driven by the reality that China cannot continue to increase exports at its current rate – indeed its exports have been falling in recent months.

The huge investments that have been made over the last two or more decades formed the necessary base for China's unprecedented speed of growth, but there is suspicion that some of the investments are beyond what the country needs, and the debt incurred in their construction cannot be paid off. We should not underestimate the capability and determination of the Chinese government to resolve these matters, but some realities are not resolvable by government directive. In any case, high levels of debt create a longstanding problem in themselves (see above).

The result of these changes is already a slowing of China's rate of growth and a sharp reduction in China's demand for raw materials such as coal and iron ore (affecting Australia among others – and Australia's problems quickly become our problems). If its domestic debt situation becomes a financial crisis it may not spill into the rest of the world as quickly as did the US financial crash because China sensibly has international currency and capital controls which would slow down the transmission of a crisis, but we would feel the results in a slow-down, even halt, in demand for our goods and services (such as agricultural products and tourism).

It is not only China among the large 'emerging economies' that is facing troubles. Brazil's economy is in recession. So is Russia's, whose position is greatly complicated by the politics of its interventions in Ukraine, Crimea and the Middle East.

The US

Then there is the US. While its economy has, on the face of it, recovered more quickly than Europe, it is still growing only weakly (0.3 percent in the last quarter). Its unemployment rate is lower than ours at 5.0 percent but falling proportions of its working age people are looking for jobs. Its debt situation, like Europe's, is unresolved after several years of quantitative easing that allowed the banks and other financial corporates to continue on largely as if nothing had changed. Like Europe, its debt will be an overhang on the economy for years to come if left to 'the market'.

As in Europe, the politics are a major concern. We have yet to see what the election at end of the year will bring, but years of toxic political deadlock have prevented the Obama administration from taking the actions (assuming it wanted to) that were needed to both address the grave faults in the financial system and revive the economy in a sustainable way, beyond bailouts – let alone address the numerous social and environmental problems the country has.

Running short of solutions

Given that the grave faults in the international financial system remain largely unaddressed because of resistance by the powerful financial sector itself (with reinforcement by the TPPA and similar agreements), the debt situations in Europe and the US will be difficult to resolve. We should not underestimate the resistance that the financial sector will continue to place in the way of solutions that suit the working people of these countries (and literally the world) rather than their own interests.

But there is a worrying immediate problem too. The effects of the GFC were to an extent cushioned by some factors, and many of those cushions have gone.

One of the most important was China: its huge, growing economy (with help from some stimulatory policies by its government) maintained demand for goods and services when the other two largest economies in the world were in dire straits. New Zealand experienced this in a sudden spurt in demand for dairy products, Australia experienced it in an equally rapid growth in demand for its minerals. China may not be in a position to do the same should the world go back into financial crisis or economic recession. In previous regional recessions, the huge US economy has played the same role. It may not able to this time around for either economic or political reasons. Certainly Europe can't.

Secondly, while many developed countries had relatively high levels of public debt before the GFC, they would go into a new crisis with depleted government capacity – at least in the eyes of the financial markets – to stimulate and stabilise the economy. New Zealand is far from this situation. Further, most monetary authorities now have their policy interest rates set at very low values – Sweden and Switzerland have negative interest rates and others have used them too – so there is very little room for monetary authorities to lower rates to stimulate depressed economies. New Zealand's official cash rate is high by current international standards, at 2.5 percent, so the Reserve Bank has more room to move – but not nearly as much as its reduction from 8.25 percent to 2.5 percent in less than a year from June 2008 to April 2009 at the onset of the GFC. In any case, in countries deeply ensnared in 'debt traps', where firms and households are focussed on paying off debt rather than spending or investing, lowering interest rates may have little effect in stimulating the economy. If firms don't believe people who are busy paying off debt will buy their products, even the lowest interest rates won't tempt them into risking their money in building new productive capacity to create jobs and incomes. Instead the cheap money is more likely to go into unproductive speculation: bidding up the prices of financial assets or real estate chasing rapid capital gains. As it is now, internationally.

Reactions must therefore be much more reliant on fiscal measures (additional government spending or tax reductions – difficult when they are already heavily indebted) or 'unorthodox' measures such as using the power of the central bank to create credit. To work in stimulating the economy, credit creation measures must be used more effectively than quantitative easing which bailed out the banks in the frequently misplaced hope that they would lend to others.

How likely is all this?

It is far from a certainty – don't panic – but it is also hard to know just how likely a downturn or crisis may be.

The International Monetary Fund (IMF) has repeatedly downgraded its international growth forecasts. This partly reflects its faulty economic forecasting (in which it is not alone), partly its misplaced trust in austerity measures to stimulate growth, but is also partly because of the worsening situation. The graph on the next page comes from the 2016 Economic Report of the US President to Congress[1]. It shows how, with each forecast, the IMF has reduced its forecast for world economic growth, and has yet to be correct in predicting a sustained upturn.

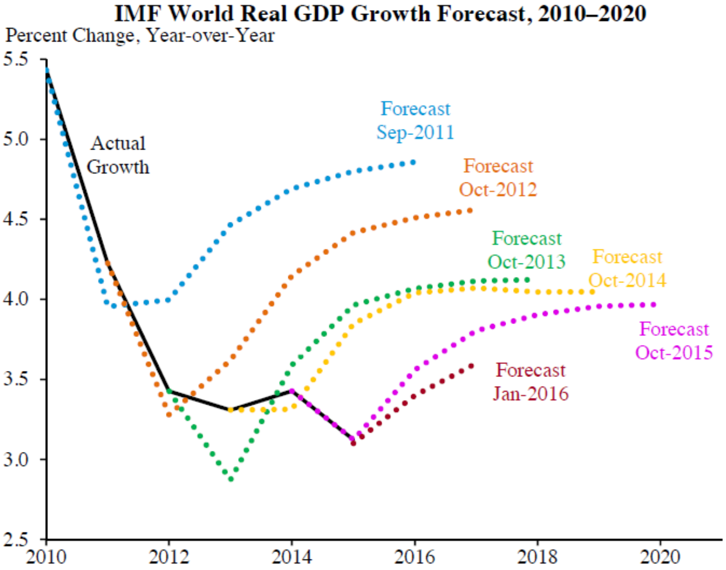
[1] https://www.whitehouse.gov/administration/eop/cea/economic-report-of-the-President/2016, at p.121.

Authorities around the world will be trying to avoid a crash. But they are running out of conventional policies that don't bring them face to face with the financial sector, and many of them are short on the political backing needed to take the measures required. The uncertainty is reflected in falling share markets and signs of greater risk in the financial markets, raising the cost of funding for banks.

The possibilities are enough of a worry that we should be thinking about whether we are properly prepared.

Figure 3-1

IMF World Real GDP Growth Forecast, 2010–2020



Source: International Monetary Fund (IMF).

How should New Zealand be preparing?

The present Government had at least two pieces of luck on its side when confronting the GFC. Firstly, good luck: the huge increase in demand and prices for dairy products from China[1] offset the sharp fall in demand for manufactured exports around the world. Secondly bad luck: the Canterbury earthquakes, despite the human suffering and destruction of assets, acted as an increasingly large boost to the economy. It is questionable whether the Government's tax cuts helped much – they were not aimed at the people who most needed the money and most likely to spend it, though earlier tax cuts from 1 April 2009, legislated by the previous Government may have helped a little – but the fact that it did not cut back hard on social security payments did help. We can't count on China next time round; it may even be part of the problem. We hope natural disaster does not strike again, and the activity of the Canterbury rebuild will start to reduce at some point, subtracting from the economy rather than boosting it. So we must rely on deliberate government actions.

The first line of defence is always the social security system. Not only does it give direct help to people through hard times but it also acts as a 'natural stabiliser', ensuring people still have at least some money to spend so that the economy doesn't face the double whammy of an external shock and falling domestic demand. Unfortunately the Government has been running it down. The Government's policies are designed to drive people back into work as quickly as possible. Payments are at poverty level. It has been neglecting people who become unemployed through its focus on pushing single parents into work, and it doesn't know if people are getting into good jobs or bad ones. The social security system needs to change its focus and recreate its capacity to help people into good jobs, with much stronger retraining provisions, relocation assistance and personalised help in finding the right job. Benefits must be raised to ACC-like levels of 80 percent of previous income. We can also learn from Australia's successful policies during the GFC which helped make it one of the few OECD countries not to

[1] Regarding its connection to the China-New Zealand FTA, see http://union.org.nz/sites/union.org.nz/files/CTU-Economic-Bulletin-151-October-2013.pdf

go into recession. These included direct income supplements paid to low income households, and bringing forward small construction and maintence projects around the country. Their experience says we should prepare for this in advance.

At the start of the last crisis, there were some tripartite arrangements between government, unions and employers for shorter work weeks. Lost hours were compensated at least partly by government. These can work well, but only when organised on a tripartite basis. The trust and capacity for that has to be rebuilt. Germany, with several decades of experience in tripartite arrangements, showed this could work very successfully in the GFC.

There must also be plans for projects which can be funded by the government to create jobs and encourage investment. The present Government instituted some of these such as roading projects, but they need more imagination, need to be closer to funding-ready, and could have more future-focussed purposes such as expanding rail or public transport, building low-energy state or local government housing (especially in Auckland), rebuilding increasingly decrepit hospitals, and renewable electricity generation. Expanding public services in job-rich areas such as health is another option. Some funding could also go to encourage industry development in promising high-value sectors, and the research and development to support it. While this kind of project is longer term, it prepares the ground so that we come out of a recession in a stronger, more diversified, shape – something this Government failed to do.

How would this be funded? Despite much rhetoric, New Zealand's public finances can easily manage higher debt for times of crisis. Senior IMF researchers Ostry, Ghosh and Espinoza (2015) listed New Zealand as having the third greatest "fiscal space" – the "distance to the debt limit" (though it is still strongly debated whether there is in fact a debt limit, or if there is one, just how high it might be). But funding does not all need to be from debt raised on financial markets. In times like these of low inflation and possibly even deflation, and especially if the economy has spare capacity as the result of an international crisis or recession, the funding could come from the Reserve Bank. Funding could also come from new progressive taxes including on assets or capital gains.

Work is also needed on New Zealand's financial system. For some time, including its most recent report on New Zealand, the IMF has been warning that the banking sector's "reliance on offshore funding and a large share of mortgage lending remain sources of vulnerability" (International Monetary Fund, 2016, p. 2). In times of financial crisis, overseas borrowing that the banks use to fund mortgages and other domestic lending can dry up. There needs to be further work to require banks to reduce this vulnerability. New Zealand also has a vulnerability in the short-term funds that can destablise the financial system and economy by spilling in or out of the country in a crisis. We need measures in place to control these movements of capital, both in times of crisis and to help manage the exchange rate.

A crisis could also trigger falls in property prices. Household debt levels fell briefly after the GFC, but are now resuming their upward march as a proportion of the size of the economy (GDP). Highly indebted New Zealanders are vulnerable to falls in values of homes and farms. Some dairy farmers may unfortunately face loss of their farms from the fall in dairy price, but viable farms and home mortgages could be helped with concessionary lending.

This is not intended to be about doom and gloom. It is important to learn from the disastrous mistakes that are still being made around the developed world, and from new thinking that has not yet permeated through to government circles in Wellington. A crisis may not happen; if one does then out of crisis can come opportunity, and these kinds of policies help us to take that opportunity. Many of these preparations are policies needed anyway for a better New Zealand.

Bill Rosenberg

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Information

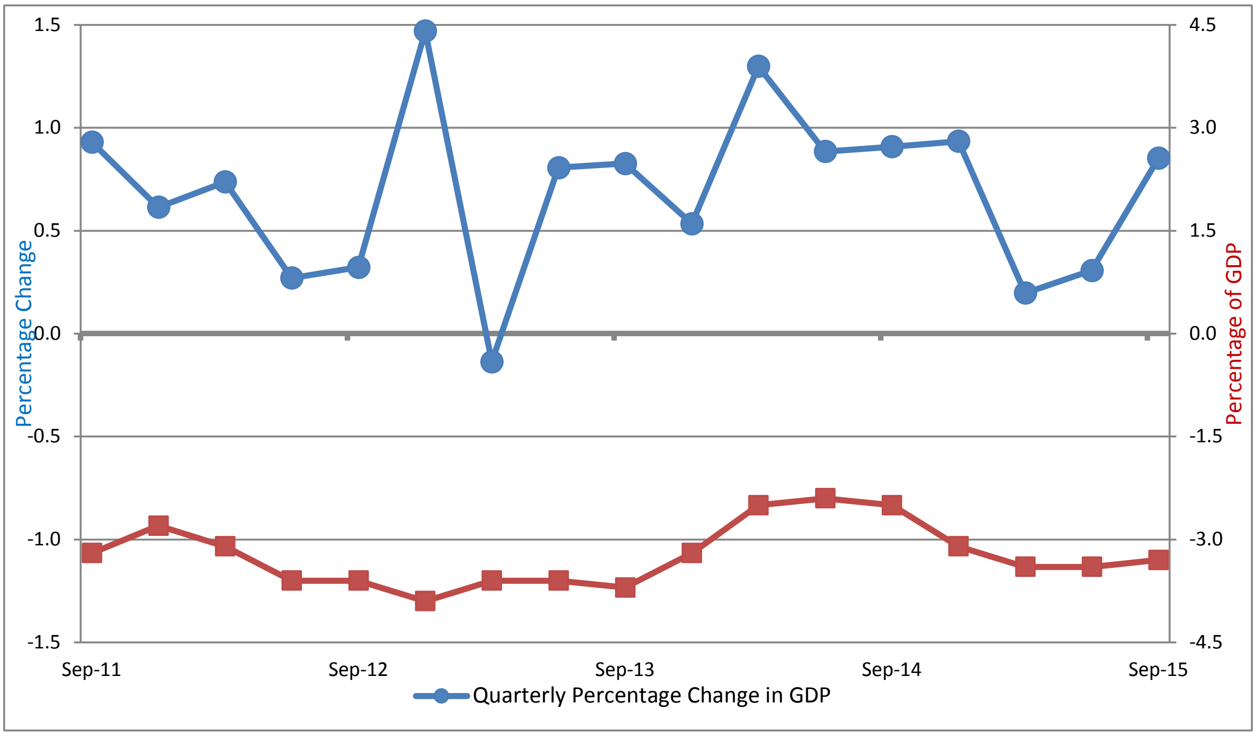
A ★ indicates information that has been updated since the last bulletin.

Forecast

- This NZIER forecast was released on 11 December 2015.

Annual Percentage Change (March Year)	**2015-16**	**2016-17**	**2017-18**	**2018-19**
GDP	2.2	2.5	2.7	2.3
CPI	1.3	1.9	2.0	1.9
Private Sector average wage	2.9	2.7	2.8	2.8
Employment	1.5	1.8	1.8	1.6
Unemployment rate	6.1	6.0	5.8	5.6

Economy



- Growth in New Zealand's economy was strong in the September 2015 quarter, with Gross Domestic Product rising by 0.9 percent, compared to weak quarterly increases of 0.3 percent in June and 0.2 percent in March. It was mainly due to strong growth in Manufacturing activity (up 2.8 percent, all sectors rising except Textile, leather, clothing and footwear manufacturing, Wood and paper products manufacturing, and Non-metallic mineral product manufacturing), and Professional, scientific, technical, administration, and support (up 2.0 percent). There was also strong growth in Wholesale trade (up 2.2 percent), Retail trade and accommodation (up 1.6 percent), and Transport, postal, and warehousing (up 2.6 percent). Output fell in Agriculture (down 1.5 percent), Forestry and logging (down 1.9 percent), Electricity, gas, water, and waste services (down 0.7 percent), Construction (down 2.9 percent), Information media and telecommunications (down 1.4 percent), and Arts, recreation and other services (down 0.7 percent). Growth for the year ended September 2015 was 2.9 percent. However GDP is barely keeping up with the rapidly growing population: GDP per person grew only 0.4 percent in the September quarter, having shrunk by 0.1 percent in the June quarter and 0.3 percent in the March quarter. Worse, real gross national disposable income per capita, which takes into account the income that goes overseas in interest and dividends to overseas investors and the falling prices for some of our main exports, fell 0.2 percent in the September quarter having risen 0.4 percent and 0.5 percent in the two previous quarters. Growth in GDP per capita is flat lining at a level around the lowest it was during the 2000s before the Global Financial Crisis hit, separating from GDP growth due to the strong population growth driven by high net immigration. Output per hour worked in the economy grew only 0.8 percent in the year to September, indicating weak productivity growth.
- New Zealand recorded a Current Account deficit of $1.8 billion for the September 2015 quarter in seasonally adjusted terms ($4.7 billion actual), compared to a $2.1 billion deficit in the June quarter. There was another deficit in the goods trade ($562 million, seasonally adjusted, following a $639 million deficit in the June quarter) and a surplus of $451 million ($282 million in June) in goods and services, while the deficit on primary income (mainly payments to overseas investors) stayed steady at $2.2 billion compared to $2.2 billion in June. For the year to September 2015, the current account deficit was $8.1 billion or 3.3 percent of GDP compared to a $8.3 billion deficit in the year to June (3.4 percent of GDP). The deficit on investment income was $9.1 billion.
- The country's Net International Liabilities were $151.0 billion at the end of September 2015 (61.9 percent of GDP) up from $148.0 billion (61.3 percent of GDP) at the end of June, but similar to the $151.4 billion (63.8 percent of GDP) in September 2014. The rise in net liabilities in the quarter was largely due to rises in the net market valuation of assets and liabilities and net financial derivative valuation changes, partly offset by a net financial in flow (outflows of liabilities exceeded outflows of assets) and other valuation changes. There was $2.3 billion net inflow of investment. Without the market value changes, the net liabilities would have been $145.7 billion. Assets rose in value from $233.1 billion to $234.2 billion mainly because of exchange rate and financial derivative valuation changes ($7.8 billion) against financial outflows of $4.2 billion and market price changes of $4.0 billion. Liabilities rose from $381.1 billion to $385.2 billion with financial outflows accounting for $6.6 billion negates by net valuation changes of $10.6 billion. New Zealand's international debt was $289.3 billion (118.7 percent of GDP), of which 29.4 percent is due within 12 months, compared to $146.8 billion in financial assets (other than shares; 60.2 percent of GDP), leaving a net debt of $142.5 billion (58.4 percent of GDP). Of the net debt, $9.6 billion was owed by the government including the Reserve Bank (equivalent to 3.9 percent of GDP and up from $6.6 billion in June) and $103.5 billion by the banks (42.4 percent of GDP), which owed $60.6 billion to

related parties. Total insurance claims owed by overseas reinsurers from the Canterbury earthquakes are estimated at $20.2 billion, and at 30 September 2015, $17.1 billion of these claims had been settled, leaving $3.0 billion outstanding.

★ Overseas Merchandise Trade for the month of January saw exports of goods rise 5.9 percent from the same month last year while imports rose faster at 7.2 percent. This created a small trade surplus for the month of $8 million or 0.2 percent of exports. In seasonally adjusted terms, exports rose 9.5 percent or $382 million over the month (compared to a 2.5 percent fall the previous month) led by rises in Dairy (up 2.7 percent or $26 million) and Fruit (up 49.3 percent or $76 million) but offset by falls in Meat (down 2.0 percent or $11 million), Logs, wood and wood articles (down 2.8 percent or $9 million), Crude oil (down 65.3 percent or $55 million, not seasonally adjusted), Seafood (down 12.8 percent or $19 million), Aluminium and aluminium articles (down 25.3 percent or $25 million, not seasonally adjusted), and Wine (down 6.2 percent or $9 million). Seasonally adjusted imports rose 6.0 percent or $256 million over the previous month, creating a trade deficit of $106 million compared to a $232 million deficit in the previous month. Imports rose in Textiles and textile articles (up 23.6 percent or $46 million), but fell in Petroleum and products (down 20.6 percent or $85 million), Mechanical machinery and equipment (down 14.4 percent or $87 million), Electrical machinery and equipment (down 3.8 percent or $14 million), Plastic and plastic articles (down 7.4 percent or $14 million) and Optical, medical and measuring equipment (down 1.1 percent or $2 million). Our top six export destinations accounted for 59.1 percent of our exports in the year (of which China accounts for 17.8 percent and Australia 17.1 percent), compared to 58.9 percent in the previous year (China 18.8 percent, Australia 17.6 percent). China is easily top source of imports accounting for $10,420 million of imports in the year compared to Australia at number two with $6,294 million and the trade balance with China has moved from a $609 million surplus in the 2015 year to a deficit of $1,661 million in the 2016 year, a turnaround of $2.3 billion. Imports from China rose 19.3 percent in the year, and 1.3 percent from Australia. In the month, imports from China rose 21.3 percent while imports from Australia rose 18.8 percent compared to the same month in the previous year.

★ The Performance of Manufacturing Index[1] for January 2016 was 57.9, a rise from 57.0 in the previous month. The employment sub-index was at 54.9, a rise from 53.5 in the previous month. While the index shows uninterrupted expansion since Sept 2012 (as Bill English boasted in a recent speech), the official GDP figures show manufacturing contracted in the March 2013, March 2015 and June 2015 quarters.

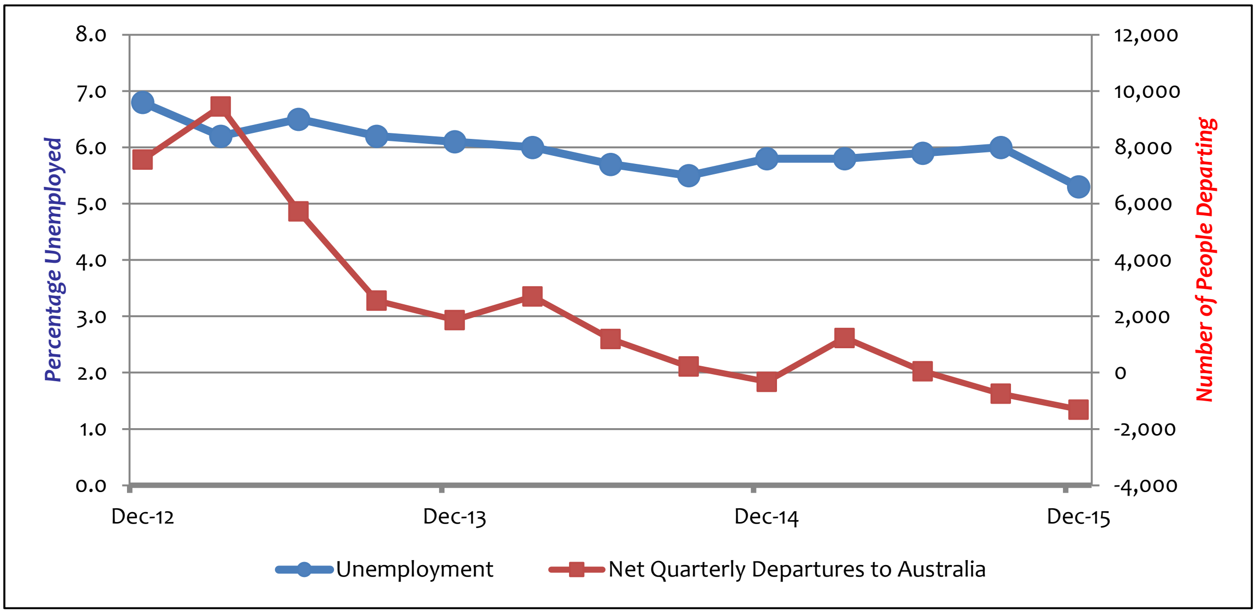
★ The Performance of Services Index[1] for January 2016 was 55.4, a fall from 58.5 in the previous month. The employment sub-index fell to 50.9 from 53.4 in the previous month. Bill English described Services as "having been growing at the fastest level in seven years". They actually grew faster in 2010 and most of the 2000s according to the official GDP figures, and growth has slowed over the last nine months.

★ The Retail Trade Survey for the three months to December 2015 showed retail sales rose 5.3 percent by volume and 4.4 percent by value compared with the December 2014 quarter. They rose 1.2 percent by both volume and value in the quarter, seasonally adjusted. By value, the largest positive contributors to the increase in the quarter were Specialised food (up 2.9 percent), Non-store and commission retailing (which includes internet purchases) which was up 3.7 percent, Hardware, building and garden supplies (up 5.5 percent), Accommodation (up 6.0 percent), and Fuel (up 2.5 percent). The largest fall was in Recreational goods (down 2.6 percent). Supermarket and grocery stores, the largest single sector, was static at 0.0 percent change by value and 0.1 percent rise by volume.

- On 28 January 2016 the Reserve Bank left the Official Cash Rate (OCR) unchanged at 2.5 percent, having reduced it from 2.75 percent to 2.5 percent on 10 December, but signalled that there could be further reductions. The Governor's statement noted increased uncertainty about the strength of the global economy, particularly China and other emerging markets. Commodity prices, including for oil are weak, international inflation remains low and financial market volatility has increased. Though the domestic economy was weaker during the first half of 2015, it was expected to strengthen in 2016 due to strong net immigration, tourism and construction. A further lowering of the exchange rate was appropriate due to low export prices. House price inflation remained a financial stability risk and it was too soon to tell if it was moderating in Auckland but was growing in other regions. There are therefore many risks in the economic outlook. Though "headline" CPI inflation remained low, "core" inflation which excludes temporary price movements was, he said, around 1.6 percent and so in the target range. This suggests the Reserve Bank would hold interest rates if it could. However given "headline" inflation is still well below the target range, further reductions in the OCR may be required over the coming year. The next OCR review will be announced on 10 March 2016 and will include a Monetary Policy Statement.

- ★ According to REINZ, the national median house price rose $22,000 or 5.2 percent to $448,000 in January 2016 compared to a year before and down$17,000 or 3.7 percent on the previous month. The Auckland median price rose 9.1 percent over the year, but fell 6.5 percent on the previous month. Excluding Auckland the national median price rose $20,250 to $361,250, up 5.9 percent compared to a year before. There were 3 or 0.1 percent fewer sales under $400,000 compared to the same month a year ago taking the number to 2,187, a rise of 63 (17.5 percent) to 423 in the $1 million plus range, and 149 more (15.2 percent) to 1,128 in the $600,000 to $999,999 range. Sales under $400,000 accounted for 43.3 percent of sales in the month but 45.2 percent in the same month a year before.

Employment



- According to the Household Labour Force Survey the unemployment rate in the December 2015 quarter unexpectedly fell to 5.3 percent or 133,000 people, compared to 6.0 percent in September (150,000 people), seasonally adjusted. Treasury and other forecasters had predicted a substantial rise. It would not be a surprise if it rose again in the March quarter. This is the first fall since September 2014 and has not been this low since March 2009, though is still more than half as much again than the 3.4 percent it was in December 2007. It is also 5.3 percent actual (not seasonally adjusted) or 132,500 people, down a relatively modest 9,400 from 141,900 or 5.5 percent a year before. By contrast, there were 259,400 people jobless (including the officially unemployed), up 2,200 from 257,600 a year before, and there were 92,800 part-timers who wanted more work, down 20,200 from a year before. Part of the reason for the fall in official unemployment appears to be a fall in the participation rate, including people discouraged from looking for work. The participation rate (the proportion of the working age population either in jobs or officially unemployed) fell from 68.7 percent to 68.4 percent over the three months, and from 69.4 percent a year before, all in seasonally adjusted terms. There are 37,100 unemployed people who have been out of work for more than 6 months (down from 40,800 a year before), and they are 28.0 percent of the unemployed compared to 28.8 percent a year before. Those out of work for more than a year is at 10.9 percent of the unemployed compared to 11.1 percent a year before. Compared to OECD unemployment rates, New Zealand has 10th equal lowest (out of 34 countries), an improvement on the 15th equal in September.

- In the North Island, only Waikato (5.1 percent) and Taranaki (4.1 percent) has unemployment below the 5.3 percent average for the country (not seasonally adjusted), though it fell over the year in all but Bay of Plenty where it worsened from 5.7 percent in December 2014 to 6.2 percent in December 2015. Gisborne/Hawkes Bay with 6.7 percent (8.0 percent a year before), and Manawatu-Whanganui with 6.8 percent (9.2 percent a year before) are particularly hard hit. Auckland’s unemployment rate was 5.4 percent (compared to 5.8 percent a year before). The South Island looks considerably better, with Tasman/Nelson/Marlborough/West Coast at 4.2 percent, Canterbury at 3.9 percent, Otago at 4.5 percent and Southland at 4.1 percent. All except Tasman/Nelson/Marlborough/West Coast are higher than a year ago.

- By industry, over the year 85 percent of the increase in employment came from Construction (27,500 workers out of a 32,200 increase), followed by Professional, scientific, technical, administrative, and support service (7,200 people) and Education and training (7,900 people). However this was offset by falls led by Arts, recreation, and other services (down 4,100 people), Transport, postal, and warehousing (down 5,100 people) and Wholesale trade (down 3,100 people). During the December quarter however, employment increased in all industries except Mining, and Wholesale trade, creating an increase in employment following six months of falls. Over the year, employment in the Services sector was static, it fell by 1,000 in the Primary sector, but rose by 29,300 in the Goods sector (mainly due to Construction).

- The seasonally adjusted female unemployment rate at 5.7 percent was considerably higher than for men (5.0 percent), though both fell from the previous quarter (6.5 percent and 5.5 percent respectively). Māori unemployment fell from 12.2 percent in December 2014 to 10.6 percent, and Pacific people's unemployment fell from 11.4 percent to 9.7 percent over the year.

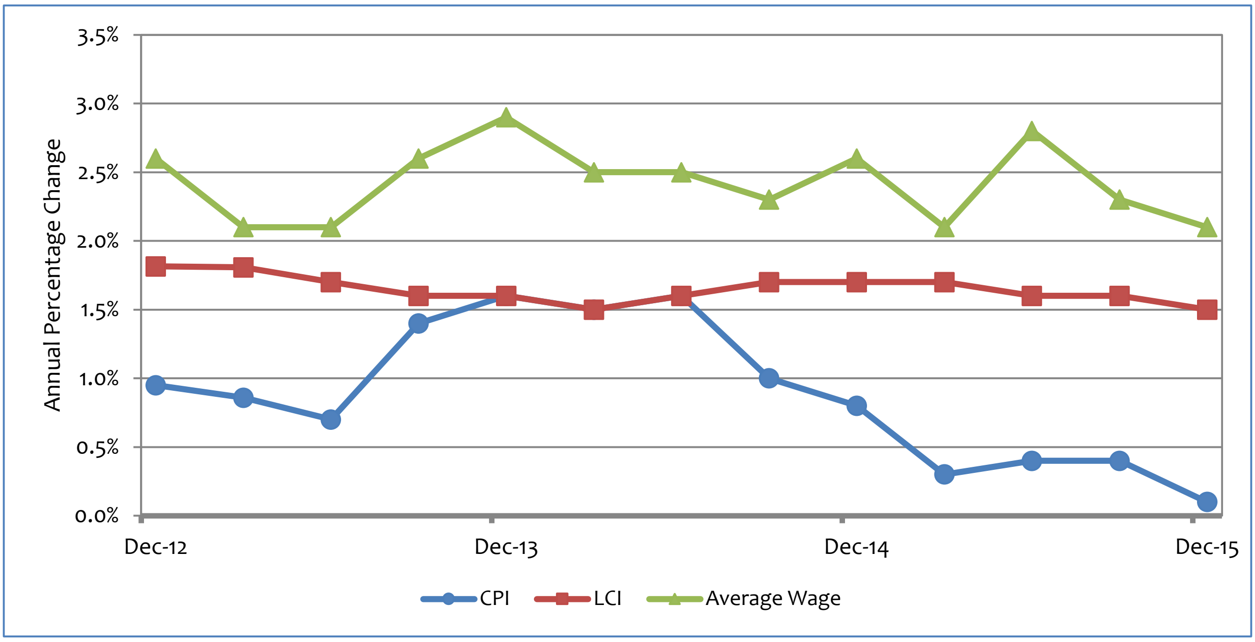
- Youth unemployment for 15-19 years was 23.0 percent, up from 21.4 percent in September and 21.2 percent a year before; for 20-24 year olds it was 9.0 percent, down from 11.6 percent in September and 11.5 percent a year before, all in seasonally adjusted terms. The Not in employment, education, or training (NEET) rate for 15-19 year olds was 6.5 percent, down from 6.7 percent in September and 7.8 percent a year before while for 20-24 year olds it was 15.0 percent, barely changed from 14.9 percent in September and 14.8 percent a year before. For the whole 15-24 year old group, unemployment was higher for those in education (17.6 percent) than those not in education (11.1 percent). There were 71,000 people aged 15-24 years who were not in employment, education, or training (NEET).

- The Ministry of Social Development reports that at the end of December 2015 there were 122,927 working age people on the Jobseeker benefit, a fall of 1,704 from a year before but a rise of 2,026 from 120,901 in September 2015 (the third quarterly rise). At December 2015, 67,670 were classified as 'Work Ready', and 55,257 were classified as 'Health Condition or Disability'. A total of 301,349 were on 'main' benefits, 7,796 fewer than a year before and 14,182 more than September 2015. It was 31,617 more than in December 2007. Of 41,059 benefits cancelled during the three months to December, 19,190 or 46.7 percent obtained work, 14.7 percent transferred to another benefit and 1.7 percent became full time students.

- Job Vacancies Online for January 2016 showed the number of job vacancies rose by 1.9 percent in the month and rose 9.0 percent over the same month a year previously in seasonally adjusted terms. Over the year, vacancies in Auckland rose 17.3 percent, Wellington 5.7 percent, rest of the North Island 6.6 percent, South Island other than Canterbury 7.2 percent, while Canterbury fell 5.7 percent. By industry, the greatest annual increase was in Accounting, HR, legal and administration which rose 14.9 percent, Hospitality and Tourism which rose 11.1 percent and "Other" industries which rose 11.8 percent, while at the other end of the scale, Construction and engineering fell 38.8 percent and Information Technology fell 5.0 percent. By occupation, the greatest rise was in Clerical and Administration (up 19.3 percent over the year) followed by, Technicians and Trades workers (up 11.9 percent), Community and Personal Services (up 10.8 percent) and Labourers (up 7.8 percent) while the lowest was for Professionals (up 3.6 percent) and Managers (up 3.9 percent).

★ International Travel and Migration data showed 10,770 permanent and long-term arrivals to New Zealand in January 2016 and 4,640 departures in seasonally adjusted terms, a net gain of 6,130. There was an actual net gain of 65,911 migrants in the year to January. Net migration to Australia in the year to January was 1,255 arrivals, with 24,397 departures and 25,652 arrivals. However there was still a net loss of 4,197 New Zealand citizens. For the month of January, there was a seasonally adjusted net gain from Australia of 320 compared to a loss of 80 a year before. In January, 10.6 percent of the arrivals had residence visas, 25.1 percent student visas, 27.0 percent work visas, and 4.9 percent visitors. A further 32.0 percent were New Zealand or Australian citizens.

Wages and prices



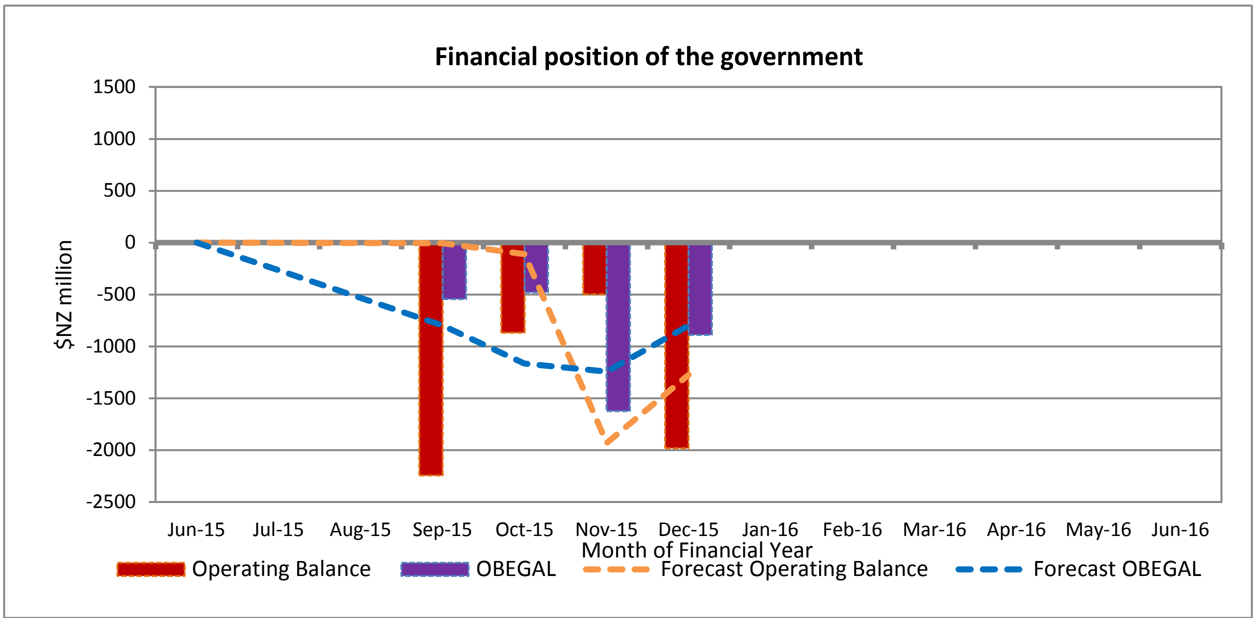
★ The Labour Cost Index (LCI) for salary and ordinary time wage rates rose 0.4 percent in the three months to December 2015. The LCI increased 1.5 percent in the year to December, ahead of the 0.1 percent increase in the CPI. It increased 0.5 percent in the public sector and 0.4 percent in the private sector in the three months to December. Over the year it rose 1.3 percent in the public sector and 1.6 percent in the private sector. During the year, 46 percent of jobs surveyed did not receive a pay rise, and 49 percent did not in the private sector. For the 54 percent of those surveyed who received an increase in their salary or wage rate during the year, the median increase was 2.4 percent and the average increase was 3.0 percent. For those jobs that received increases, the median increase in the public sector was 2.0 percent and in the private sector 2.5 percent; the average increase in the public sector was 2.3 percent and in the private sector 3.2 percent. We estimate that jobs on collective employment agreements were 2.3 times as likely to get a pay rise as those who were not, and are more likely to get a pay rise of any size ranging from less than 2 percent to more than 5 percent. Only 43 percent of jobs that were not on a collective got a pay rise during the year. In the construction industry, salary and ordinary time wage rates in Canterbury are now rising more slowly than in the rest of the country: 0.4 percent in the quarter in Canterbury compared to 0.5 percent in the rest of the country; and over the year to December, 1.3 percent in Canterbury compared to 1.9 percent elsewhere. For those getting a rise, Canterbury wage rates rose 3.6 percent compared to 4.0 percent elsewhere.

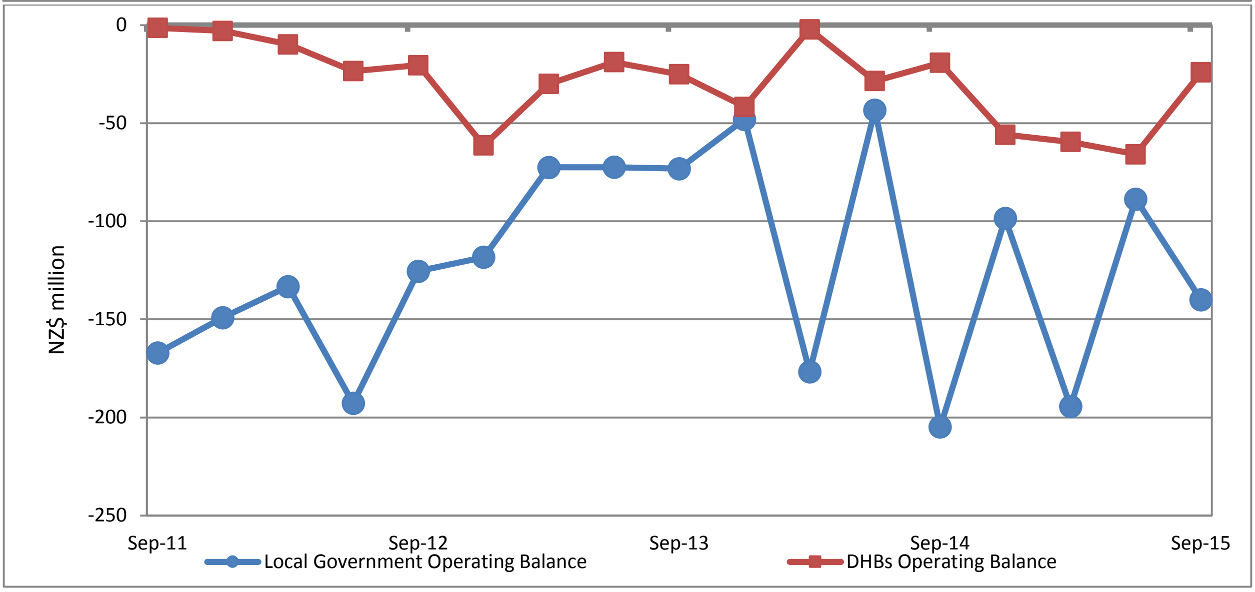
★ The Quarterly Employment Survey for the three months to December 2015 found the average hourly wage for ordinary-time work was $29.38, up 0.3 percent on the previous quarter and up 2.1 percent over the year. The average ordinary-time wage was $27.44 in the private sector (up 0.2 percent in the quarter and up 2.5 percent in the year) and $36.53 in the public sector (up 0.4 percent in the quarter and up 1.5 percent in the year). Female workers (at $27.14) earned 13.3 percent less than male workers (at $31.30) for ordinary time hourly earnings.

○ The Consumer Price Index *fell* 0.5 percent in the December 2015 quarter compared with the September quarter, and increased just 0.1 percent for the year to December. For the quarter, Housing and household utilities (up 0.5 percent), including Home ownership (up 1.2 percent) and rents (up 0.65 percent), Passenger transport (up 6.1 percent) and Real estate services (up 3.5 percent) were the largest upward influences. Those offsetting them were led by Food (down 2.1 percent), Alcoholic beverages and tobacco (down 1.0 percent), Transport (down 1.2 percent, despite the rise in Passenger transport, mainly due to a 7.0 percent fall in the price of petrol and 8.2 percent in other vehicle fuels and lubricants), Communications (down 0.8 percent), and Personal care (down 0.8 percent). Inflation in Canterbury for the year was negative 0.3 percent, the third time it has been below the national average since June 2011. It was *negative* 0.3 percent in Wellington and negative 0.2 percent in the rest of the South Island. In Auckland it was 0.5 percent and 0.1 percent in the North Island other than Auckland and Wellington. Housing costs rose at the average rate of 2.8 percent in Canterbury for the year, second only to Auckland, which rose 3.9 percent, compared to 1.6 to 2.4 percent elsewhere. In seasonally adjusted terms, the CPI fell 0.2 percent from September, Food fell 0.5 percent, Clothing and footwear fell 0.1 percent, Housing and household utilities rose 0.8 percent, Communications fell 0.8 percent, Recreation and culture fell 0.8 percent, and Education rose 0.7 percent.

★ The Food Price Index rose by 2.0 percent in the month of January 2016 (rising 0.4 percent in seasonally adjusted terms). Food prices fell 0.6 percent in the year to January. Compared with December, fruit and vegetable prices rose 4.4 percent (but fell 0.7 percent seasonally adjusted); meat, poultry, and fish prices rose 3.3 percent; grocery food prices rose 1.6 percent (up 0.7 percent seasonally adjusted); non-alcoholic beverages rose 2.2 percent; and restaurant meals and ready-to-eat food prices rose 0.2 percent.

Public Sector





★ According to Treasury's Financial Statements of the Government of New Zealand for the six months ended 31 December 2015, core Crown tax revenue was just $14 million lower than forecast in the 2015 Half Year Economic and Fiscal Update (HYEFU). Corporate tax was $246 million or 5.9 percent below forecast, some of which is likely to be due to timing, and PAYE was 1.1 percent ($150 million) above forecast. However core Crown revenue was $171 million (0.5 percent) below forecast, "largely due to core Crown interest revenue being $204 million lower than forecast. This difference is largely due to some financial derivatives being replaced at maturity, whereas they had been forecast to mature into interest-bearing deposits". Core Crown expenses were $142 million (0.4 percent) below forecast. As a result, the Operating Balance before Gains and Losses (OBEGAL) was $889 million in deficit, $92 million worse than forecast. The Operating Balance was a $2.0 billion deficit, $709 million (55.7 percent) worse than expected, "largely due to higher than expected actuarial losses on the ACC claims liability, mostly reflecting the impact of changes in valuation assumptions used compared to forecast". Net debt at 27.5 percent of GDP ($66.9 billion) was $1.1

billion worse than the $65.8 billion forecast. Gross debt at $85.7 billion was $615 million better than forecast.

★ District Health Boards recorded combined deficits of $61.6 million for the six months to December 2015. This is $12.1 million worse than their plans. The Northern region was $2.7 million behind plan with a surplus of $6.3 million and three of the four DHBs in surplus (Northland being the exception), the Midland region was $1.9 million behind plan with a combined deficit of $16.8 million and all DHBs in deficit though Waikato at $8.9 million accounted for more than half the total, Central region was $9.5 million behind plan and all DHBs in deficit including Capital and Coast at $7.8 million, for a total $24.7 million, and the Southern Region was $2.0 million ahead of plan with a $26.4 million deficit and three of the five DHBs in deficit including Canterbury at $11.5 million and Southern at $15.3 million. The DHB furthest ahead of plan was Southern by $4.4 million, and MidCentral was furthest behind, by $4.4 million. The Funder arms were in surplus by $22.5 million, and Provider arms in deficit by $84.6 million.

- Local Government recorded a 3.7 percent ($83.2 million) fall in operating income and a 1.4 percent rise in operating expenditure ($31.9 million) including no change in employee costs for the September 2015 quarter compared to June 2015. This resulted in an operating deficit of $140.0 million in the September quarter, compared with a deficit of $88.6 million in the June quarter, and deficits in all the quarters back to March 2008 with the exception of June 2010, all in seasonally adjusted terms. Note that the latest quarter results are provisional and seasonally adjusted figures are revised with each release.

Notes

1 For the Performance of Manufacturing Index (PMI) and Performance of Services Index (PSI) a figure under 50 shows the sector is contracting; above 50 shows that it is growing. Previous month’s figures are often revised and may differ from those published in a previous Bulletin.

This bulletin is available online at http://www.union.org.nz/economicbulletin176.

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