NEW ZEALAND COUNCIL OF TRADE UNIONS
Te Kauae Kaimahi

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Commentary

Oh, Christchurch!

Summary

Just as both life and geology in Christchurch seemed to be stabilising from the September earthquake, the vicious 22 February quake has hit with terrible human pain and physical destruction. It would be hard to show more starkly how inadequate Gross Domestic Product (GDP) is to measure our progress and welfare. It does not measure most of the harm to people and to the quality of their lives nor to the community's assets and environment.

In contrast it seems almost crass to discuss the effects on GDP but the debate on policy options has begun.

The government today announced welcome initial measures to help workers affected and it promises further assistance. How should the government fund its promised contribution? It would be fairest and most effective to either continue spending and allow debt to rise, or bring in a special tax like Australia has for the Queensland floods. It levies people on high incomes at a greater rate but exempts flood victims and people on incomes under A$50,000. It has the merit of spreading the cost fairly. If the government continues to cut public spending it in effect would make users of reduced government services, displaced public sector workers and beneficiaries pay for Canterbury's reconstruction.

The September quake was not the main cause of the recent fall in GDP. The Reserve Bank and Treasury both estimated that the effect would be small. The 22 February quake will cause much greater loss in GDP before reconstruction begins, but is clear there are other strong effects that are causing the economy to falter in the absence of an adequate government stimulus. But even if the earthquakes are hitting GDP less than you might expect, GDP hides most of the pain. Christchurch, we are thinking of you.

Just as both life and geology in Christchurch seemed to be stabilising from the September earthquake and 5,000 aftershocks, the vicious 22 February quake has hit with terrible human pain and physical destruction. It would be hard to show more starkly how inadequate standard economic measures such as Gross Domestic Product (GDP) are to measure our progress and welfare. It does not measure the loss of life or searing physical and emotional pain, nor the huge loss in quality of life and leisure as people struggle to obtain life necessities such as shelter, food, water, and power. Neither does it measure the enormous destruction of homes, commercial buildings, water pipes, roads, power lines, environment, historic buildings and much more. We are long overdue for adopting better measures of welfare and meaningful progress – and for economic policies (and theories) that take them into account.

In contrast it seems almost crass to discuss the small part of reality that GDP represents. But bank economists are already making their estimates of the effect on GDP and its future growth. Rating agencies are commenting on the effect on the government's credit rating (not much). The government is connecting the September quake to the fall in GDP in the September quarter. There are suggestions for a special tax to pay for the costs to government of the disaster. The Prime Minister is saying "we've got the financial capacity to deal with the earthquake" in contrast to the strong government messages this year that it was urgent to pay off debt. These issues will play an important part in forming government policy.

How do the earthquakes affect GDP? By even this inadequate measure there will be a far greater immediate hit to GDP from the 22 February quake than the September one. There will be much greater disruptions to businesses, more people will be off work for longer, their financial and emotional reserves are lower, and more people will lose their jobs and livelihoods. When the reconstruction gets underway, it is likely to show up as a much greater boost to GDP than was anticipated from the September shock. GDP considers the reconstruction as progress – even though it just replaces what was there before the quake.

The government today announced an initial support package to give help to workers whose employers are either considering the future of their business (a wage subsidy to employers of $500 per week gross for each full-time employee or $300 for part-timers), or consider that their business is no longer viable or cannot be contacted ($400 net per week for full time employees and $240 for part-timers). The payments are backdated. The priority to get immediate financial assistance to affected workers is the right one.

They are also promising to provide funding for the recovery. It is not clear yet what the total cost will be, but while estimates of the September quake costs to central government were in the hundreds of millions, this one could conceivably reach a billion dollars or more. It is going to be an even longer lasting need, and the complexity of the disruption to almost every aspect of Christchurch's life will be immense. Christchurch and New Zealand will also want to see a quality rebuilding of the city as quickly as possible.

Unless other action is taken, this will add to the debt the government is running to keep the economy going through the recession and which the government has shown greater urgency in cutting. If the government reacts to this by even greater spending constraints, in effect it would make users of reduced government services, beneficiaries and displaced public sector workers pay for Canterbury's reconstruction. Yet the need for government services is rarely clearer than in times of disaster with local government, emergency services, social welfare, government emergency response lines, hospitals, scientists, engineers, ACC, EQC, and even Treasury and the Reserve Bank all playing important or crucial roles.

An alternative is a special tax. Australia has one for the Queensland floods – 0.5 percent on income between A$50,000 and A$100,000 and 1 percent on income above A$100,000. People receiving disaster relief or earning under A$50,000 pay nothing. A tax exempting those affected and levying others according to their ability to pay spreads the cost fairly over the whole country. Any dampening effects on the economy are likely to be small and could be partially offset by the Reserve Bank easing monetary conditions. Of course cuts in government spending also have dampening effects: the choice is one of fairness.

We believe the government can afford higher debt and continue to spend for this period, as we have been advocating to counter the faltering economy, but a well designed tax is the most equitable alternative.

In December, official estimates for the total cost of the September earthquake reconstruction were about $5 billion (about 2.6 percent of annual GDP), spread over about two years. Estimates now go as high as $8 billion. The February earthquake will cost several times that. Early estimates range up to $16 billion or roughly 8 percent of GDP. Much of that will come from insurance from reserves or from overseas, but some will still be a direct cost to individuals, businesses or the government. Where the cost will fall is not yet clear.

Is the September quake the main cause of the faltering economy shown in the fall in GDP in the September quarter (and in a December quarter fall which Bill English seems to be anticipating)? In the September quarter (the latest we have), GDP fell by 0.2 percent but the Reserve Bank had estimated the negative effect of the quake in that quarter would be just 0.1 percent and forecast a 0.3 percent rise in GDP. Treasury had estimated a negative effect of 0.2 percent and forecast GDP would rise 0.4 percent. Both thought the quake effect was small, and both forecast an increase in GDP despite it. In fact it fell and was 0.4 to 0.6 percent lower than either expected.

Treasury itself commented in its January Monthly Economic Indicators, the fall was "only partly due to events such as the earthquakes in the Canterbury region… The recovery in the economy has been weak even accounting for these events". It forecast a 0.9 percent increase in GDP for the December quarter after taking the earthquake into account and the Reserve Bank a more modest 0.4 percent. If the December GDP movement does turn out to be very small or negative, it confirms that the economy is being held back by much more than the September earthquake. We can blame the earthquakes for many things, but not for everything.

The 22 February quake will cause much greater loss in GDP before reconstruction begins, but is clear there are other strong effects that are causing the economy to falter in the absence of an adequate, well directed government stimulus and which should not be pushed under the carpet.

Even if the earthquakes are hitting GDP less than you might expect, GDP hides most of the pain. Christchurch, we are thinking of you.

Bill Rosenberg

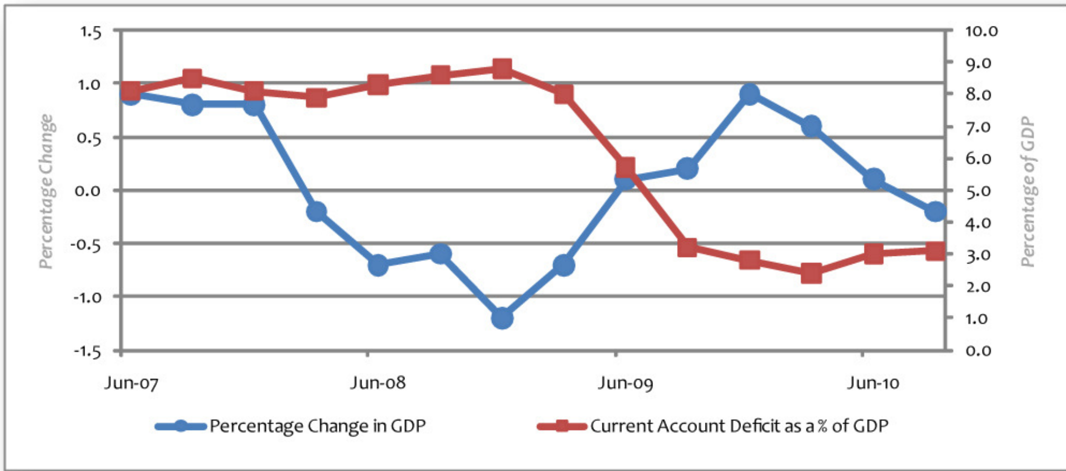
Forecast

This NZIER consensus forecast was published on 14 December 2010.

Annual Percentage Change (March Year)	**2010-11**	**2011-12**	**2012-13**
GDP	2.1	3.5	2.6
CPI	4.6	2.6	2.5
Private Sector Wages	1.8	2.9	3.3
Employment	1.3	2.4	1.8
Unemployment	6.2	5.5	5.1

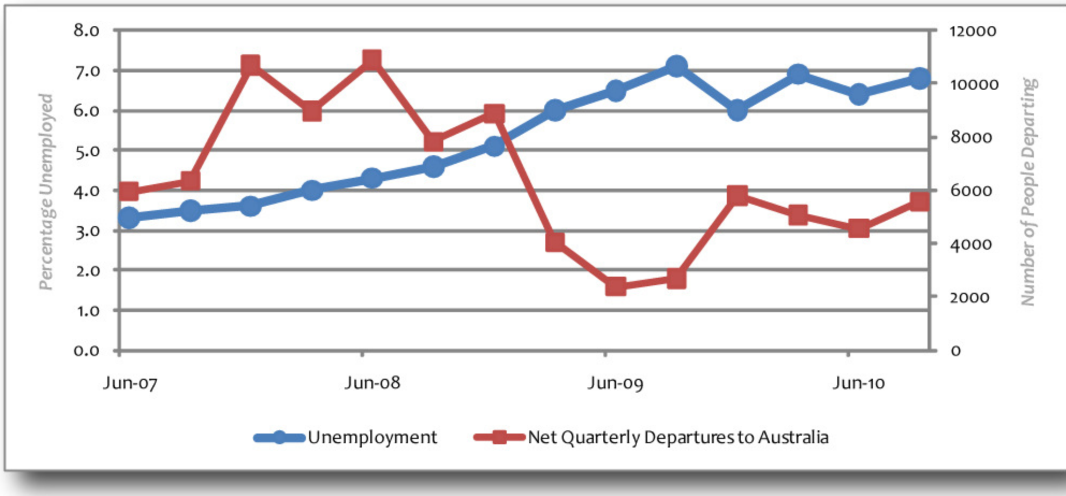
A ★ indicates information that has been updated since the last bulletin.

Economy



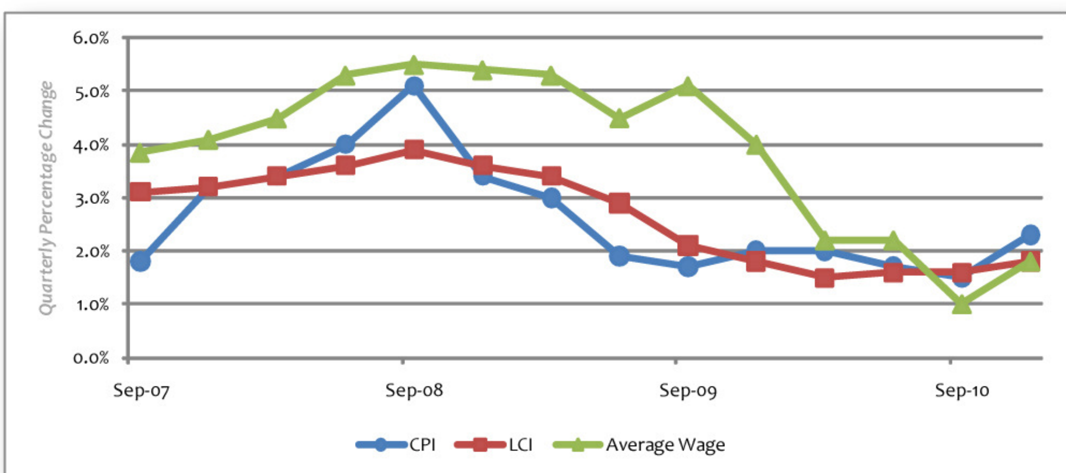
- Gross Domestic Product was down 0.2 per cent in the September 2010 quarter, leaving GDP growth for the year to September 2010 at 1.4 per cent.
- New Zealand recorded a Current Account deficit of $1.7bn for the September 2010 quarter and a deficit for the year to September of $5.9bn – 3.1 per cent of GDP. The deficit is on the rise again having fallen to low levels as a result of low company profits and interest rates during the recession.
- The country's Net International Liabilities were $162.5bn at the end of September 2010 – 85.2 percent of GDP but $600m less than at the end of June.
- ★ For January 2011 Overseas Merchandise Trade recorded a $11m surplus – 0.3 percent of the value of exports for the month, but $260m less than the surplus for the same month in 2010. For the year to January 2011, New Zealand recorded a surplus of $865m (2.0 percent of exports). Exports are still led by dairy products, but a steep increase in imports (up 14 percent from last January) was led by mechanical and electrical machinery and equipment, a positive sign that firms are gearing up for increased production.
- ★ The Performance of Manufacturing Index for January 2011 increased to 53.7[1], up from 53.2 in December showing stronger expansion. The employment sub-index also showed improving expansion at 52.8, up from an adjusted 51.3 in December.
- ★ The Performance of Services Index for January 2011 was 50.8[1], down from the adjusted December figure of 52.1. The employment sub-index contracted further to 47.8, down from 49.3 in December.
- ★ The Retail Trade Survey found retail sales were down 0.1 per cent between the September and December 2010 quarters but up 1.5 percent on the December quarter in 2009. (Note Statistics New Zealand has now stopped publishing monthly retail trade data).
- On 2 January 2011 the Reserve Bank left the Official Cash Rate unchanged at 3.00 percent. The next review will be on 10 March 2011.
- ★ The REINZ Housing Price Index recorded a 2.6 percent decline in house prices for the month of January 2011, with the median house price falling $9,210 to $351,450. House prices are also down 1.6 percent for the year to January.

Employment



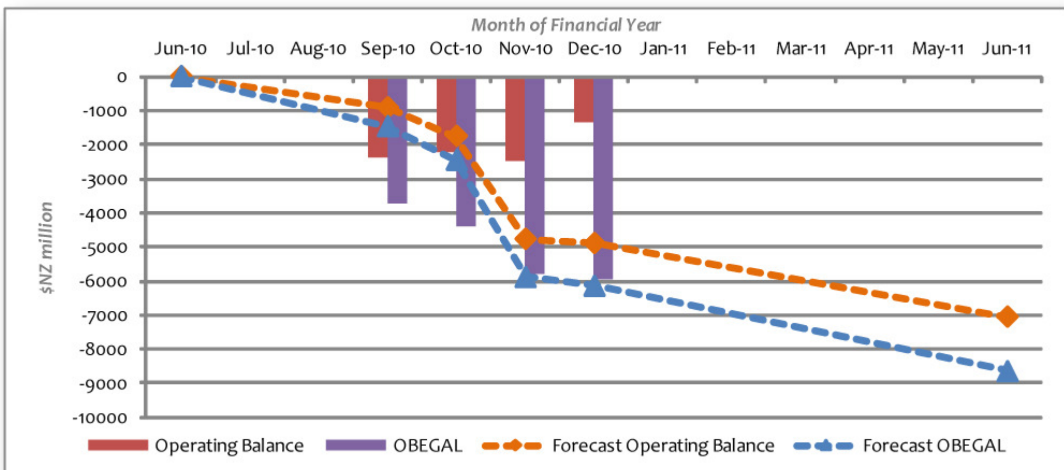
- According to the [Household Labour Force Survey]() the unemployment rate in the December quarter was 6.8 percent, up 0.4 per cent on the September quarter. The participation rate was 67.9 percent – down 0.4 per cent on September. Māori unemployment was 15.5 percent, Pacific unemployment was 13.5 percent, Asian unemployment was 9.3 percent and European/Pakeha unemployment was 4.6 percent. Youth unemployment (15-19 year olds) was 25.5 percent.
- At the end of January 2011 there were 68,151 people on the Unemployment Benefit, an increase of 1002, or 1.5 percent, from December 2010. (Quarterly figures on Unemployment Benefit numbers are available from the MSD website.)
- In the three months to the end of December 2010 Job Vacancies Online increased 6.9 percent and advertised vacancies for skilled jobs increased 7.1 percent.
- International Travel and Migration figures show 7225 permanent and long-term arrivals to New Zealand in December 2010 and 6922 departures. Net migration in the year to December 2010 was 10,451 arrivals. Net migration to Australia in the year to December was 20,988 departures.

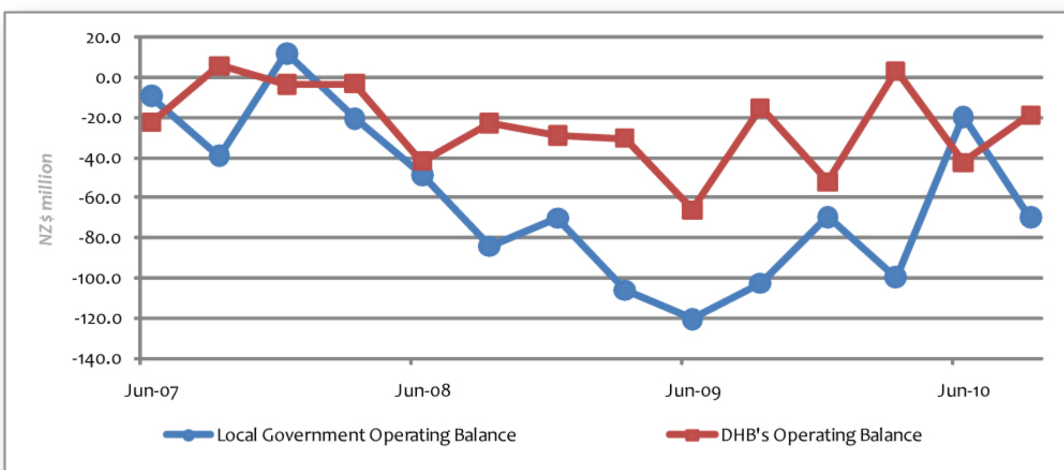
Wages



- ★ The Labour Cost Index (Wage and Salary Rates) (LCI) rose 1.7 percent for the year to December 2010 and 0.5 percent for the December quarter. For those surveyed who received an increase in their salary or wage rate during the year, the median increase was 2.9 percent.
- ★ The December 2010 Quarterly Employment Survey found the average hourly earnings for ordinary-time work was $25.83, up 0.5 percent on the September quarter. The average ordinary-time wage was $23.87 in the private sector (up 0.6 percent) and $32.71 in the public sector (up 0.3 percent). Per hour, female workers earned 87.7 per cent of what male workers earned.
- ⭘ The Consumer Price Index for the December 2010 quarter rose 2.3 percent, and 4.0 percent for the year to December.
- ★ The Food Price Index rose 1.8 percent in the month of January, and food prices were 3.8 percent higher in January 2011 than in January 2010.

Public Sector





- ★ According to Treasury's Month End Financial Statement for the six months to the end of December 2010, Government revenue was down $172m (0.6 percent) on budget figures, and expenditure was up $162m (0.5 per cent). The operating deficit before gains and losses (OBEGAL) was on the forecast track, and the operating deficit of $1.3bn was $3.6 billion less than forecast due to good performance of the public investment funds and changes in ACC's discount rate. The Government's net debt is 20.7 percent of GDP, exactly matching forecasts in the Half Year Economic and Fiscal Update.

- District Health Boards recorded a $42.4m deficit for the September 2010 quarter, up from a deficit of $18.7m in the June Quarter. Employment costs were $1.2bn, up 3.0 per cent for the quarter, compared to total expenses of $3.2bn up 0.2 per cent.
- Local Government recorded a 2.0 percent decrease in income and a 0.8 percent increase in costs for the September 2010 quarter, resulting in a deficit for the quarter of $69.8m.

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.

An online version of this bulletin is available at www.union.org.nz/economicbulletin121
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