NEW ZEALAND COUNCIL OF TRADE UNIONS
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Comment
Predictions on the economic outlook for 2008 are tinged with more than the usual degree of hesitancy. This is a time when many economists are saying, in effect, "there is a lot of uncertainty, markets are volatile". In other words – they don't know! There is obviously more certainty about what has already happened and why. And there can also be some predictions about knock-on effects. But there is uncertainty about quite how bad the US recession will be, how much contagion is still to come from the sub-prime mortgage crisis, what the impact will be on other countries, and how effective the US stimulus package will be and over what time frame.

The IMF has said that "a global economic slowdown is under way: problems in US housing continue, the US and European financial systems remain under stress and growth in the rest of the world is beginning to be dragged down". Their latest forecasts are for a marked US slowdown and a more moderate but still significant slowdown in other industrial countries. The IMF says precise timing of a slowdown in emerging markets is not completely clear, but they think it may come sooner rather than later given their strong linkages with industrialised countries.

The extent of the financial crisis is considerable. There have been large losses of $11.4 billion at Europe's largest bank UBS AG, $11.5 billion at Morgan Stanley, $25.5 billion at City Group and $28 billion at Merrill Lynch. These losses are due to writedowns on securities affected by US subprime mortgages. And the UK Government has had to come to the rescue of Northern Rock. The $63 billion loan from the Bank of England will be converted into bonds guaranteed by the government, to then be sold on to private buyers over the next 5 years.

As the prominent U.S. economist, Paul Samuelson has said, "today's global bankruptcies and macroeconomic quagmires trace directly to the financial engineering shenanigans that the Bush era officialdom both countenanced and encouraged." Unions have warned for years about the damaging impact of hedge funds with their huge appetite for risky debt. Subprime lending in the USA, the riskiest category of aggressive loans, soared from $US150 billion in 2000 to $US650 billion in 2005 as hedge funds and other investors harvested the higher interest rates of sub-prime borrowers -- often 3, 4, or 5 percentage points more than in the prime market. But, more established banks also wanted a slice of the action. Banks such as UBS, once renowned as risk-averse, then opened themselves up to a much more risky portfolio and have since announced writedowns of $billions on fixed-income securities and leveraged loans.

You would think alarm bells would have rung with so many finance firms chasing huge profits off the backs of those least able to afford to pay their mortgage. Memories of the Savings and loans crisis in the 1980s, Enron and Arthur Anderson in 2001, while they had some different features, would surely mean that there were strong arguments for more effective regulation of the finance sector, rather than the opposite. Policy issues arising from the sub-prime crisis include greater scrutiny of rating agencies (which had many of these institutions at impressive ratings prior to massive losses emerging) and more effective regulation of non-banking institutions. But for now the attention is on how to stimulate the US economy. This should not just be about tax rates. As Paul Samuelson says "When fear of risk stifles both investment and consumption spending, sensible and measured fiscal budgetary spending is the prescription to augment central banks' lowering of interest rates." Joseph Stiglitz (who will be in NZ in March) is another Nobel prizewinning economist opposing tax cuts for the rich as a rescue package. He argues for higher benefits for the unemployed and federal assistance for state spending on infrastructure and education.

In New Zealand, the Government is in a strong fiscal position with a healthy operating surplus and gross debt below 20 percent of GDP. Interest rates are high with plenty of room to move down. The judgement call however with an outlook of inflation above 3 percent and growth below 2 percent is around the timing, nature and extent of any NZ-based stimulus if any. In the USA, the focus is on economic growth, not inflation. After all their inflation is at 4.1 percent (due to food and energy price rises) compared with 2.5 percent a year earlier yet the federal funds rate has been cut from 4.25 percent to 3 percent.

For NZ workers, the outlook is not positive. In 2007, food prices rose by 5.4 percent, with a 7.8 percent increase in grocery food prices, and meat and fish prices up by 6 percent. Petrol was up by 16.9 percent over the year. This reflects an international trend with food prices up about 50 percent and oil prices 80 percent on a year ago.

Interest rates here have been rising although the 5 year rates have been dropped to reflect assumptions of lower economic growth. But floating rates are already above 10 percent in many cases with the fixed two year rate at around 9.5 percent. There will be many fixed term mortgages rolling over this year with those householders facing a big lift in interest payments. House prices are cooling which is good in the long run, but also means that people are less likely to withdraw some housing equity to fund major purchases or housing renovations.

There are some encouraging signs in the export sector, but US interest rates are now down to 3 percent compared with 8.25 percent in NZ. While many anticipate downward pressure at the present time on the NZ dollar because of less appetite for risk globally in coming months and a dip in economic growth in NZ, the interest rate differential of 5.25 percent is a real incentive for those in the carry trade and could have a flow on effect forcing up the NZ dollar and damaging export returns. A slower economy and challenges to the export sector suggests a rise in unemployment but this could well be modest.

So clearly there is an ability in New Zealand to use a mix of spending, tax cuts, and interest rate cuts to stimulate the economy. Working for Families will act as an income cushion for some families. There are now economic as well as political reasons to go early on tax cuts. But the current focus seems to be to put inflation concerns above those of an economic slowdown – and wait and see what emerges in the global economy – sit tight.

For unions, the arguments for decent wage increases are as strong as ever. This should sit alongside our willingness to engage on longer term productivity issues and also promote KiwiSaver. The only sustainable solution for workers facing a cost squeeze this year is to have rising real wages, improved savings, and confidence in ongoing government provision of vital social services. This is much better than a sense of financial wellbeing based on reliance on large annual increases in house prices for those with a house, more and more credit card debt, and anticipation of big tax cuts. After all it is the appetite for risk, hugely leveraged debt and a diminished role for government regulation that is the heart of the current global financial crisis. That is not a good strategy for workers and households.

The stage is set in election year for the economy to be a major talking point. Unions have a good story to tell. It is one that says investment in economic development works, that a rising minimum wage has coincided with more jobs, that improvements in annual leave and other benefits are affordable, that investment in skills does pay dividends, that unions not only argue for decent pay but do something about it… and so much more. And unions also will be putting out policy suggestions – for instance on how to more effectively lift wages on an industry or multi-employer basis. So fasten your seat belts – it will be an interesting year!

Consensus forecasts[1] published by NZIER

The consensus forecasts were updated in December 2007.

March Years, percent	**2008**	**2009**	**2010**
GDP	2.9	2.1	2.7
CPI	3.1	2.8	2.8
Wages (QES)	4.1	4.1	3.7
Employment	1.1	0.8	1.1
Unemployment	3.8	4.2	4.3

[1] The consensus is made up of the average of forecasts from NZIER, Berl, ANZ- National Bank, ASB Bank, BNZ Bank, First New Zealand Capital, Deutsche Bank, UBS, Westpac, Reserve Bank of New Zealand and Treasury. They are done every 3 months which means that we sometimes have actual figures for some of the forecasts.

Economic Snapshot

Consumer prices rose 1.2 percent in the December 2007 quarter, and were up by 3.2 percent annually. The next CPI update is on 15th April 2008. Food prices rose 0.9 percent from November 2007 to December 2007, and 5.4 percent over the past 12 months. Unemployment is at 3.5 percent. Māori unemployment is 8.0 percent and Pacific peoples' unemployment is at 5.5 percent, compared with 2.4 percent for European/Pākehā. The minimum wage is $11.25 an hour for a person who is aged 18 or over and $9.00 an hour for those aged 16 or 17 years old or a trainee. Ordinary time wages, as measured by the Quarterly Employment Survey (QES) for September 2007, were up annually by 4.0 percent (3.7 percent in the private sector and 4.9 percent in the public sector). The QES showed that the average ordinary time hourly wage is now $23.06 ($21.53 in the private sector and $28.92 in the public sector). The female rate of pay is $21.32, compared to the male rate of $24.49. The Labour Cost Index (LCI) shows that ordinary time wages went up by 3.1 percent in the September 2007 year (3.3 percent in the private sector and 2.9 percent in the public sector). The next update of wages data is on 5th February. Economic activity increased 0.5 percent in the September 2007 quarter, compared with 0.8 percent in the June 2007 quarter. In the year ended September 2007, the economy grew 2.7 percent, up from the 1.6 percent growth recorded in the September 2006 year. The next GDP update is on 28th March. The Official Cash Rate (OCR) remains at 8.25 percent.

Consumer Price Index

The CPI rose by 1.2 percent in the December 2007 quarter and by 3.2 percent in the year to December. The Food Price Index showed a lift of 5.4 percent in 2007 with a 7.8 percent increase in grocery food prices, and meat and fish prices up by 6 percent. Petrol prices rose by 16.9 percent over the year, new housing prices were up by 6.1 percent, rates by 6.7 percent, and electricity 6.5 percent. Education costs were down by 2.5 percent with early childhood education down a huge 34.8 percent due to government subsidies. Tradable inflation was 2.8 percent with non-tradable inflation at 3.5 percent compared with 3.8 percent and 4.3 percent in previous years.

Economic Growth

GDP increased 0.5 percent in the September 2007 quarter, and by 2.7 percent in the year to September 2007. This compares with growth of 1.4 percent in the September 2006 year. Due to improvements in the terms of trade, real gross national disposable income rose by 3.6 percent for the year.

Minimum Wage

From 1 April 2008 the minimum wage for employees aged 16 years and over will rise to $12.00 an hour before tax. The training wage will rise to $9.60 an hour. From 1 April 2008, there will no longer be a minimum wage for youth. Instead there will be a new entrants' minimum wage. The new entrants' minimum wage will be $9.60 an hour before tax on 1 April, 2008. A new entrant is a worker who is 16 or 17 years old except if they have completed 3 months or 200 hours of employment, whichever is shorter, or they have been supervising or training other workers, or they are subject to the minimum training wage.

Work Stoppages

There were 29 work stoppages in the year to September 2007, compared with 50 in the year to September 2006, and 52 in the year to September 2005. There were 22 complete strikes, 6 partial strikes and one lock out. Manufacturing and the health/community services sector had the highest number of stoppages in the September 2007 year, each with nine stoppages.

Government Accounts

Figures for the five months ending November 2007 show the operating balance was $506 million (28.3 percent) lower than forecast at $1.28 billion. The OBEGAL (this stands for Operating Balance Excluding Gains and Losses and replaces the OBERAC) was $240 million (12.5 percent) higher than forecast at $2,161 million (compared to a forecast of $1,921 million) with core Crown operating expenses under forecast. Gross debt was 19 percent of GDP. The NZ Superannuation Fund operating balance showed a deficit of $143 million compared to a forecast surplus of $395 million. Treasury advise that the decline in return was driven in large part by the recent slowing in United States' economic activity, and future growth uncertainty generated by the recent fall out in the sub-prime lending market.

Housing and Property

REINZ figures show that the property market ended 2007 with a national median sales price of $345,000, slightly down from $352,000 in November but up from $330,000 in December 2006. Quotable Value's December statistics show a 10 percent growth in property values over the past year. The growth rate eased from 11.4 percent reported in November with the average New Zealand sale price also easing to $388,253 (from $393,198). According to the latest monthly Fairfax Media Home Loan Affordability report, higher interest rates kept New Zealand home loan affordability near its worst levels ever in December. Nationally, the proportion of take-home pay required by a median income earner fell slightly from 83.5 percent to 81.9 percent to make a mortgage payment on a median priced house purchased in December. The report follows the Demographia survey showing New Zealand had the least affordable housing in the English-speaking world alongside Australia. Of the urban markets surveyed, New Zealanders and Australians can expect to pay 6.3 times their annual earnings to house themselves. For the British, it is 5.5 times, the Irish 4.7, the Americans 3.6 and the Canadians 3.1 times annual household earnings all higher than an affordability level assessed at a maximum of 3 times annual household earnings. Building consents data shows that the trends for both the number of new housing units and the value of residential buildings are declining, with 1,738 new housing units authorised in December 2007, 145 fewer compared with December 2006.

Trade, Balance of Payments and International Investment Position

December exports were $3.7 billion, with dairy exports up two-thirds on a year ago. Compared with the September 2007 quarter exports increased by 20.8 percent, the largest increase on record. For the December 2007 year, exports were $36.6 billion, up 5.6 percent from the previous year. Dairy exports were up by $1.2 billion and petroleum exports by $892 million. Imports were also up by 11 percent in the December quarter and also annually. Capital goods imports were up by 18 percent in the quarter also which could reflect expanded investment in plant and machinery. The New Zealand dollar (as shown by the Trade Weighted Index) was 5.2 percent higher than in December 2006. The current account deficit for the year ended September 2007 was $14.2 billion, a rise from $13.7 billion, which was the deficit for the year ended June 2007. As a result, the current account deficit rose to 8.3 percent of GDP - up from 8.1 percent in June 2007 but lower than 8.8 percent for the year ended September 2006. Out of the $14.2 billion deficit on the current account, $12.4 billion (87 per cent) is from the investment income deficit. Statistics NZ noted that "the larger investment income deficit was mainly due to an increase in profits earned by foreign-owned New Zealand companies, and higher interest payments made on New Zealand's rising levels of overseas debt. New Zealand's net international liability position at 30 September 2007 was $151.1 billion. The level of foreign investment in New Zealand was $269.5 billion as at the September 2007 quarter, an increase of $33.1 billion from September 2006.

Retail Sales

In November 2007, total retail sales increased 2.0 percent compared with October 2007. This is the largest monthly increase since February 2007, when sales rose 2.3 percent. Some economists were surprised to see that total retail sales lifted by this level compared with expectations of a 0.7% increase. This took annual growth in nominal sales to 6.7%, up from 4.2% in October.

Migration

In the year ended November 2007, there were 82,600 permanent and long term arrivals, down less than 1 percent from the November 2006 year and there were 76,000 departures, up 11 percent. As a result, net migration was 6,600 in the November 2007 year, down from 14,800 in the November 2006 year, but slightly above the 6,200 recorded in the November 2005 year. There was a net inflow of 7,400 from the United Kingdom, down from 11,300 the previous year. There were also net inflows of 3,500 from India, 3,200 from the Philippines, 2,400 from Fiji, 1,800 from South Africa, and 1,700 from China in the November 2007 year. The net outflow to Australia was 27,200 in the November 2007 year, compared with 20,500 in the November 2006 year.

Burgeoning Student Loans

The average student loan now stands at $28,838. This is an increase of more than 50% in the last three years. The average debt has risen 54% since 2004 and is 147% higher than in 1998. Student debt has now reached $9.5 billion.

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