

Tracking the Economy

Too much risk

The economy is fragile and there are many risks. The RBNZ left interest rates unchanged as a result. Contained inflation, weak building consents, softening exports and continued global uncertainty means the economy and interest rates will stay in a holding pattern well into 2012.

Unchanged OCR

The RBNZ left the OCR unchanged at 2.5% on 27 October 2011. This is because the recovery is fragile. Growth is modest and business confidence has dimmed. The European debt crisis continues and the global recovery is stalling. This will slow tourism and exports, although the Canterbury rebuild will provide some much needed activity.

Inflation in the September 2011 quarter was outside the Reserve Bank's 1%-3% target range at 4.6%. But this included the GST increase, and underlying measures of inflation are running closer to 2%. There is little reason for the RBNZ to raise interest rates now.

Pre-election update makes grim reading

The Government's finances are in a bad position. Revenues have fallen and expenses are increasing. This is partly due to the Canterbury earthquakes, but mostly because of a long recession. The fiscal deficit in the year to June 2011 was 9.2% of GDP, one of the worst on record. The Treasury's forecasts were optimistic compared to the subtext of the document. A quick return to surplus is unlikely. There is little headroom for this election to be a lolly-scramble. Instead the focus needs to be on two key issues facing New Zealand: productivity and the ageing population.

Export growth slowing

Export growth has slowed, particularly to China, which had been a buffer against the GFC. Merchandise exports to China have fallen 6% in the last six months. Exports had been resilient until now. With cracks appearing in the China growth story and a broader slowdown in global growth, exports may slow further in coming months.

Resilient labour market, Canterbury flagging

The labour market is resilient. Employment rose 0.7% over the year to September 2011, despite a 3.4% decrease in Canterbury. A similar picture was evident in paid hours, which mirrors economic activity. The earthquakes have clearly impacted on the Canterbury region, but the rest of New Zealand remains encouragingly resilient.

While resilient, employment growth has been slow. This means wage growth is subdued and still lagging behind living costs. Subdued wage growth means household spending will be slow to recover.

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