

Tracking the Economy

A darkening outlook

The global economic outlook is deteriorating rapidly. This will depress New Zealand's fledgling recovery. The mounting risks to growth and slowing inflationary pressures mean the RBNZ will not raise interest rates until 2013. The risks to the economic outlook are firmly to the downside, hinging critically on the path of the European debt crisis and its contagion to the rest of the world.

In a holding pattern

NZIER expects economic growth of just 1.5% in 2012, similar to this year. Other New Zealand economists expect growth of 2.5% to 3.7%. The key growth depressant is a soft global growth outlook, including in Australia and China. Also, the Canterbury situation is worsening with deep and broad job losses.

European crisis close to home

The European sovereign debt crisis is the key risk for New Zealand. The linkages with our economy are clear. The price and volume of our exports will fall. The cost and ease of access to global credit will worsen. This means investment by households and businesses will remain depressed. We face the risk of another recession.

Slow domestic economy

Even before the onset of the latest global fears, businesses were struggling with flat sales and thinning margins. Firms are unable to pass on cost increases because of weak demand. Inflationary pressures are muted and will remain so for some time. So the RBNZ will maintain low interest rates for a protracted period. If global growth slows further, the RBNZ may have to cut the OCR to protect the economy.

Crisis scenario

We hope the European Monetary Union (EMU) will not break apart, with a political solution found over coming months. But if it does break, the ramifications will be severe: perhaps similar or worse than the Global Financial Crisis (GFC). Financial market dysfunction would precede a global recession. There is limited ability to offset this with monetary and fiscal stimulus; these have been largely exhausted in the aftermath of the GFC.

Fiscal consolidation more difficult

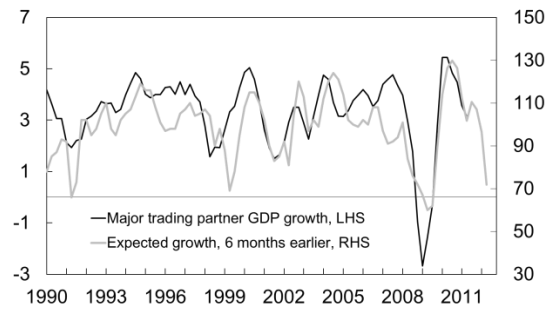
A downbeat economic outlook means tax revenue will be low and it will be difficult to return the operating balance to a surplus over the next five years. Spending cuts flagged to date may not be enough, meaning the next Budget in May 2012 will have to consider a broader package of cuts or raise revenue.

397 words

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Global growth & confidence

Annual % change, left scale; net % of respondents, right scale

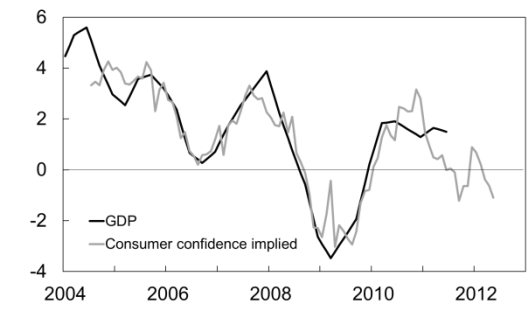


Source: CESIFO, DataStream, NZIER



GDP growth – actual and confidence implied

Annual % change

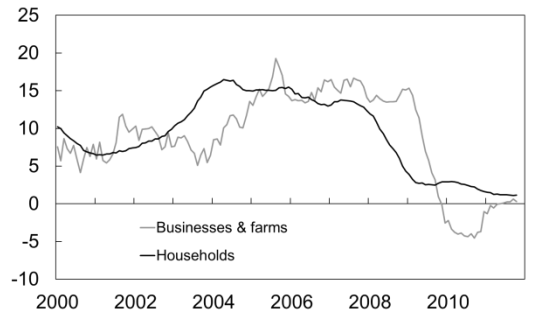


Source: Statistics NZ, ANZ-Roy Morgan, NZIER



Borrowing growth

Annual % change

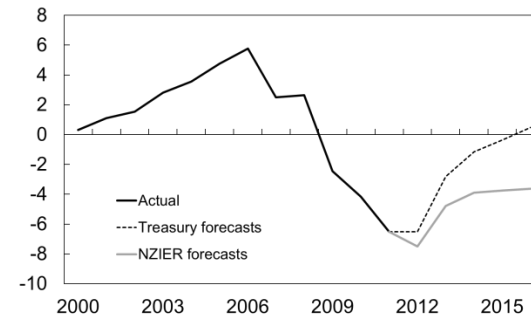


Source: RBNZ



Core fiscal balance

Revenue less expenditure, % of GDP



Source: Treasury, Statistics NZ, NZIER

