BUSINESS NZ

PLANNING FORECAST

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BusinessNZ

NZ economy – keep calm, carry on

Executive Summary

The New Zealand economy is currently a very positive story with relatively strong growth over a range of sectors - construction, manufacturing, services and agriculture -backed up by continued strong migration and a tourism sector which keeps going from strength to strength.

All the key economic indicators are pointing in the right direction with 3 percent plus growth expected over the forecast period.

While the Government's pre-election opening of the books showed slightly less in the cupboard for political parties to distribute in pre-election spending promises, overall the Government's fiscal position is solid on current projections. The importance of the Pre-election Economic and Fiscal Update (PEFU) as a mechanism for instilling a degree of discipline on the political parties' proposed spending programmes should not be underestimated.

While the final outcome of the election and future policy directions are uncertain, business and consumer confidence remain high.

Strong business and consumer sentiment is reflected in relatively strong company performance with the New Zealand sharemarket again growing strongly after taking a slight breather in the second half of last year.

Underpinning the New Zealand economy is a stronger international growth outlook, boding well for future growth. The J. P. Morgan Global Manufacturing Performance of Manufacturing (PMI) rose to a 75-month high of 53.1 in August, up from 52.7 in July.

Despite a relatively rosy picture for the New Zealand economy over the forecast period, significant risks remain and must be understood if the economy is to continue to deliver economic growth providing New Zealanders with the sort of opportunities and lifestyles many aspire to.

At the international level, significant issues still confront the global economy despite a recent uplift in general economic data from key players. Not least is an increasingly nationalist approach to trade and the moves towards greater protectionism. Offsetting these difficulties is the good news of New Zealand's mandate to negotiate for a new Trans Pacific Partnership (TPP11). It is positive that all 11 members of the TPP group have agreed to stick closely to the terms of the original agreement and are moving at pace towards a conclusion. TTP will cut tariffs imposed on New Zealand exporters, allow greater access to new markets, and substantially increase returns to this country.

But hovering under all of the above is an increased threat of terrorism along with the continuing stand-off (threats and counter threats) between the US and North Korea.

HIGHLIGHTS

Underpinning the New Zealand economy is a stronger international growth outlook. The J. P. Morgan Global Manufacturing Performance of Manufacturing shows further acceleration in expansion of global manufacturing with the Global PMI rising to a 75-month high of 53.1, up from 52.7 in July.

The BusinessNZ Economic Conditions Index sits at 15 for the September 2017 quarter, up 4 on the previous quarter and up 5 on a year ago.

After a minor blip in expansion this year, not only is the BNZ- BusinessNZ Performance of Manufacturing Index showing continued solid expansion into the second half of 2017, so too is sister survey the Performance of Services Index (PSI).

Performance in several sectors is positive, including manufacturing, services, construction and tourism. The agricultural sector is increasingly back on track with Federated Farmers' July Farm Confidence Survey showing a return to a positive outlook.

Inflation remains well under control assisted by a relatively strong New Zealand dollar offsetting international commodity price rises, while advances in technology are restraining prices increases normally associated with increased demand.

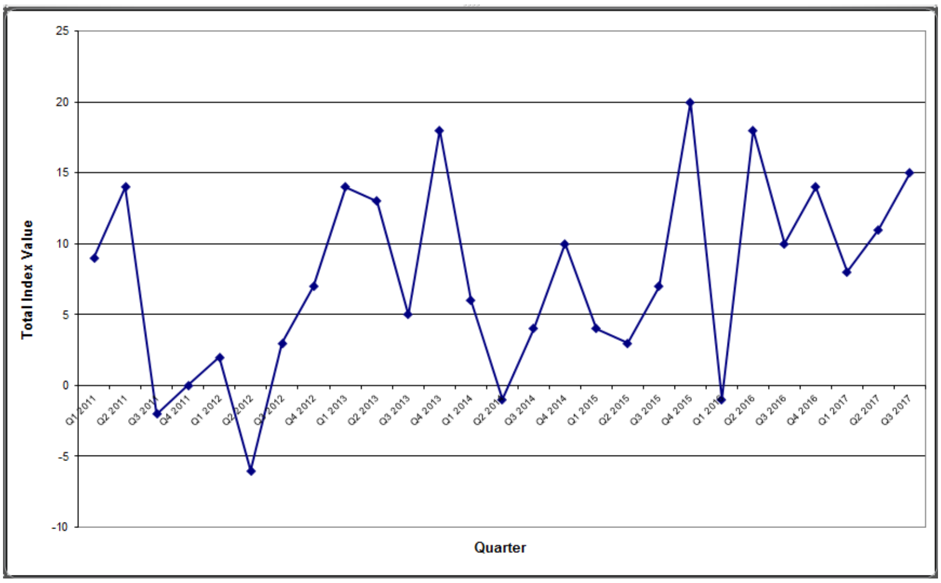
Interest rates are likely to remain on hold for longer than expected: good news for borrowers and high-debt households, but not quite so rosy for those dependent on term deposits as sources of additional income in retirement.

PART 1: THE NZ ECONOMY – WHERE ARE WE NOW?

BusinessNZ Economic Conditions Index (ECI)

The overall BusinessNZ Economic Conditions Index (a measure of NZ's major economic indicators) sits at 15 for the September 2017 quarter, up 4 on the previous quarter and up 5 on a year ago.[1]

Overall Economic Conditions Index (ECI)



Source: BusinessNZ

Data in the ECI is broken into four key sub-groups:

- Economic growth/performance indicators
- Monetary policy/pricing indicators
- Business/consumer confidence indicators
- Labour market indicators

Of the ECI sub-groups:

Economic growth/performance indicators sit at 5 for the September 2017 quarter, the same as the previous quarter, and up 7 on a year ago. With increases in world commodity prices, particularly dairy, New Zealand's terms of trade are now close to record levels.

Monetary policy/pricing indicators sit at 1 for the September 2017 quarter, the same as the previous quarter and down 3 on a year ago. Inflationary pressures are still benign but interest rates are incrementally increasing.

Business/consumer confidence indicators sit at 4 for the September 2017 quarter, up 2 on the previous quarter and up 1 on a year ago. Confidence indicators for both businesses and households continue to consolidate at relatively healthy levels.

Labour market indicators sit at 5 for the September 2017 quarter, up 2 on the previous quarter and the same as a year ago. Overall, employment growth remains strong, while unemployment is still in decline despite still strong migration growth.

[1] The ECI tracks over 30 indicators on a quarterly basis. The overall index value for any particular quarter represents the net balance of the indicators (generally the number increasing minus the number decreasing) thus providing an overall measure of performance. In general, increases in an indicator are seen as positive (e.g. growth in GDP or employment) and declines as negative. However, this is not always the case; for example, declines in unemployment are seen as positive and increases as negative. Some of the results for the June 2017 and September 20017 quarters are estimates based on available information to date.

PART 2: THE NZ ECONOMY – WHERE ARE WE HEADING

1.1 Economic growth (GDP) – solid

The NZ economy is currently a very positive story with relatively strong growth over a range of sectors - construction, manufacturing, services and agriculture. This is backed up by continued strong migration and a tourism sector still going from strength to strength.

Despite the political side-shows preceding the upcoming general election, the economy is still producing the goods.

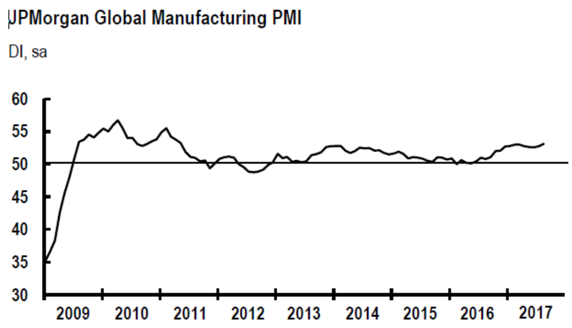
A solid average growth rate of 3 percent plus per annum is forecast out to September 2019 (see below).

Underpinning the New Zealand economy is a stronger international growth outlook, boding well for future growth in the commodity exports on which, relatively speaking, New Zealand is still heavily dependent for our export dollars. The J. P. Morgan Global Manufacturing Performance of Manufacturing (PMI) shows a further acceleration in the rate of expansion of the global manufacturing index.

The PMI rose to a 75-month high of 53.1, up from 52.7 in July and has now remained above the neutral 50.0 mark over the last 18 months as can be seen in the graph below.

Commenting on the survey, David Hensley, Director of Global Economic Coordination at J.P. Morgan, said:

"The upturn in the global manufacturing sector is gathering pace in the third quarter, with August seeing the Manufacturing PMI rise to its highest level in over six years. Rates of expansion in output and new orders also accelerated, underpinning a further solid bounce in job creation. Although price pressures and supply-side constraints are rising, the sector should have sufficient momentum to sustain its current robust expansion."



Global Manufacturing PMI™ Summary

50 = no change on prior month.

Index	Jul.	Aug.	+/–	Summary
Global PMI	52.7	53.1	+	Rising, faster rate
Output	53.1	53.6	+	Rising, faster rate
New Orders	53.7	54.2	+	Rising, faster rate
New Exports	52.5	53.4	+	Rising, faster rate
Employment	51.6	52.0	+	Rising, faster rate
Input Prices	55.0	56.5	+	Rising, faster rate
Output Prices	51.9	53.0	+	Rising, faster rate
Future Output	63.5	63.5	=	Positive, same extent

Forecasts: Real GDP percent Growth

	Years Ending		
	Sep 17	Sep 18	Sep 19
Highest	2.6	3.4	3.9
Average	2.6	3.1	3.2
Lowest	2.5	2.8	2.6

Source: ASB, BNZ and Westpac

The Government's recent pre-election opening of the books (PEFU) shows that while there are not as many lollies in the cupboard as was forecast in the earlier May Budget, the projections still show room for further targeted expenditure, potential tax cuts and further debt reduction, all at the same time. This is a choice that many of the countries we compare ourselves to simply do not have.

Given that most key economic indicators show the New Zealand economy is continuing to perform at satisfactory standards, it is perhaps not surprising that the business community in New Zealand is relatively comfortable with current policy settings, including fiscal policy settings.

The recent 2017 Deloitte BusinessNZ Election Survey shows the business sector to be relatively happy with New Zealand's policy direction but wanting some key changes. The survey, conducted in May 2017, covered 575 businesses of all sizes in all sectors and regions of New Zealand. The complete results can be found on www.businessnz.org.nz

According to the 2017 survey, the business community is relatively satisfied with current policies for economic growth and international trade, with the effectiveness of Government spending, and with the current structure of the tax system.

Key findings in the 2017 Deloitte BusinessNZ Election Survey include:

- Corporate tax – 48% are in favour of reducing business tax to 20%, while 39% are opposed
- Capital gains tax – 28% are in favour of a capital gains tax; 59% are opposed
- Income tax – 76% are against increasing the top rate (but 66% would support an increase if spent on transport infrastructure and 55% would support an increase if spent on social investment)
- Foreign investment – 53% are satisfied with policies for attracting foreign investment; 23% would like to see more foreign investment
- Immigration – there is a split in opinion on whether ImmigrationNZ has got the balance right in letting skilled people into New Zealand (28% say too many are being let in, 19% say not enough are being let in, and 33% say the balance is about right)
- Resource Management Act – 35% say the RMA is broken and should be replaced; 30% say it could work if it constrained what councils can regulate; 28% say it could work if planning processes were shorter
- Infrastructure – 60% say more should be spent in infrastructure; 64% want infrastructure provided by public-private partnerships
- More than half (56.9%) thought water, wastewater and roading services should be subject to greater commercial discipline and user charges
- Local government – 65% want councils to focus on core services (local infrastructure and goods and services that can't be provided more efficiently by business)
- Skills – 61% are unhappy with the skills of young people coming out of the education system.

Some of the above issues raise important considerations when assessing the polices of various political parties promoting their wares for the upcoming general election.

Some politically fraught issues such as reform of freshwater management require calm analysis rather than any ad hoc approach that could affect incentives on business to invest.

While clearly a water user does not have the right to ownership of the actual water resource, resource consents do give the user the right to take, dam or divert water. To that extent, a resource consent is a property right. Moreover, water permits are recognised and valued as rights, particularly where there is an increasing demand for water. Therefore semantics aside, water consents are water rights, as reflected in the large infrastructure investment undertaken in New Zealand - electricity generation, large scale irrigation schemes, manufacturing, processing and mining etc. In many cases the value of consents for agricultural irrigation has been capitalised into land values.

A sound water policy regime should ultimately ensure that current and future generations gain the greatest economic, social, environmental and cultural benefit associated with water use within a sustainable management framework. From a business perspective this means allocating scarce resources to their most efficient uses. This involves a number of considerations, including security of property rights from confiscation (without compensation), reasonable internalisation of costs associated with water use (user pays), and the ability to transfer rights efficiently where appropriate. Such considerations are often given little or no account under current water management regimes but must be part of any water reform agenda post-election.

Irrespective of the make-up of the government voters will deliver in a couple of weeks' time there are still a number of tensions and issues that need to be addressed, and, in some cases, managed.

These include, in no particular order of importance:

- *NZ dependency on export markets for our trade in goods and services.* Protectionist moves internationally (particularly by President Trump in the US) are likely to leave the country vulnerable if the protectionist stance gains further traction. Offsetting this is the good news of New Zealand's mandate to negotiate for a new Trans Pacific Partnership (TPP11). The move is positive in that all 11 members of the TPP group have agreed to stick closely to the terms of the original agreement and are moving at pace towards concluding the agreement. TTP will cut tariffs imposed on New Zealand exporters, allow greater access to new markets, and substantially increase the returns to this country.

- *The risk of ongoing terrorist attacks, always in the background*. Some security experts suggest New Zealand is not necessarily immune from such threats. And eco-terrorism, which could potentially damage our clean/green reputation overnight – not to mention public health - should not be easily discounted.

- *Any escalation of the stand-off between the US and North Korea.* This remains a critical issue to world peace and stability with the preferred position of trying to get North Korea back into sensible talks. Missile launches across the bows of Japan and threats (and counter threats) to destroy are not the kind of diplomacy required to gain a lasting solution. North Korea's latest nuclear testing has been condemned by world leaders, including New Zealand although there is no silver bullet solution in sight.

- *House price escalation, particularly in the main centres*. This is a problem that affects the ability to attract skilled labour and imposes significant stress on family budgets. The potential for social unrest is very real unless action is taken to ensure home ownership is within New Zealanders' reasonable reach. Short-term fixes such as Loan-to-Value Ratios (LVR) introduced by the Reserve Bank are unlikely to deal with the key long-term factors impacting on house costs. These are not limited to but are nonetheless highly dependent on restrictions on available land supply.

- *The level of household debt.* The average household debt level is now close to 170% of household income and again climbing consistently after taking a breather following the 2008 global financial crisis. High debt levels will have a damaging effect on households should interest rates rise significantly. However, it has to be understood that debt in itself is not necessarily bad but needs to be put in context. Debt for investment purposes may often be highly desirable as opposed to debt simply to fund short-term consumption.

- *The question whether New Zealand shares are becoming too expensive compared to underlying returns and whether it is time to ease back.* The New Zealand share market continues to consolidate after falls in the latter half of last year. Given very low interest rates in New Zealand (and indeed around the world) and the amount siphoned off into KiwiSaver schemes, the share market has until now had a ready source of capital looking for a home, with respectable returns. But increasingly, investment fundamentals suggest a correction is inevitable sooner or later. This is not only an issue for New Zealand; it is also an international problem with continuing low interest rates proving many investors with very limited choices.

- *Strong tourism numbers adding pressures on some regions' ability to cope with associated infrastructure at peak times, including water and sewerage.* Infrastructure funding has been a source of tension where locals want to see tourism growth but don't want to be the principal funders of tourism growth's requirements. Alternatives to general rates, such as bed taxes proposed in Auckland, have not had a favourable reception. One wonders why, with the advent of time use monitoring etc., more user-pays principles cannot be bought to bear on some of these so-called controversial issues. It is noted that the Labour Party has advocated for a relatively low level tourist tax on people entering the country to pay for some of the pressures on infrastructure, mainly in areas tourists frequent. While it could be argued that a broad-based level tax is better than a very narrowly based targeted tax such as a bed tax, the question remains: what is the problem a tax is supposed to solve and is it the most appropriate mechanism to address the issue at hand?

A week - or even a day – has been a long time in politics over the last few weeks, and the final outcome of the general election come September 23 is still far from certain. However, it is important for all political parties to reflect on the key strengths or the economy and not quickly dismantle any of sound fiscal, monetary and regulatory settings that have generally served New Zealand well over the last 3 decades or so. One of New Zealand's key strengths has been the quality of its institutions and the transparency with which decisions are generally made - often the envy of many of the countries we traditionally compare ourselves to.

Property rights and enforcement of same are fundamental pillars of a market economy. Without reasonable security from confiscation by the state or others, the incentive on individuals and businesses to invest and build up productive assets is severely weakened.

1.2 Monetary conditions – short-term no change

Monetary policy has often been the subject of political point scoring in the build-up to a general election and this election has been no different, with the usual murmurings from some quarters for the Reserve Bank to have multiple objectives rather than a single focus on inflation. Also questioned is whether the OCR should be the sole responsibility of the Governor or whether the Reserve Bank Board, or some other expert committee should set the rate. Current monetary policy as espoused in the Reserve Bank Act, with the overriding focus on inflation containment, has been broadly supported by successive Governments for at least three decades.

Over the last decade there have been a number of reviews and discussion papers on monetary policy with two key reports endorsing New Zealand's approach as generally consistent with international best practice.

In May 2000, the Minister of Finance invited Lars Svensson, an international expert on monetary policy from the Institute for International Economic Studies, Stockholm University, to review the operation of monetary policy in New Zealand. Terms of Reference were provided.

The *Independent Review of the Operation of Monetary Policy in NZ: Report to the Minister of Finance* (The Svensson Report - February 2001) found with regard to the operational framework and management of monetary policy in pursuit of New Zealand's inflation target that *"….monetary policy in New Zealand is currently entirely consistent with the best international practice of flexible inflation targeting, with a medium-term inflation target that avoids unnecessary variability in output, interest rates and the exchange rate."*

In 2007, the Finance and Expenditure Committee conducted an inquiry into New Zealand's future monetary policy framework - *Inquiry into the future monetary policy framework* (Report of the Finance and Expenditure Committee, September 2008).

The Committee's terms of reference covered a range of areas including, among others, the causes of inflationary pressures, the effectiveness of current monetary policy in controlling inflation, the interaction of monetary policy and fiscal policy, and productivity issues.

The report was presented to the House of Representatives in September 2008.

Some key findings were:

- The importance of maintaining price stability as a vital component of a healthy and well performing economy
- Acknowledgement that New Zealand's monetary policy approach, emphasising central bank independence and inflation targeting, is standard among small, open, developed economies
- Acknowledgement that at times of strong inflation pressures, the cost of maintaining price stability is often borne disproportionately by the export sector
- Acknowledgement that factors other than monetary policy – such as sustained improvement in trend productivity – play a key role in lessening the adjustments required to maintain low inflation over the medium term
- Evidence at that time was not sufficiently compelling to support the pursuit of supplementary stabilisation instruments such as a mortgage interest rate levy, an interest-linked savings scheme, and other taxes that might complement interest rates in managing inflation.

While it has been argued at times that these reports endorsing New Zealand's current monetary policy framework were produced a decade or so ago, it is important to reflect on the need for the Reserve Bank to have a sound and independent role in ensuring that the economy can prosper and that businesses and households can be confident about the parameters within which the Bank operates.

The present Governor of the Reserve Bank, Graeme Wheeler has stood down with the Deputy Governor, Grant Spencer to take on a caretaker role for the next six months. This will allow an incoming government time to consider what the ideal requirements for a new Governor should be. Some post-election horse trading could occur in relation to longer-term momentary policy settings.

Interest rates – remain low for longer

The 90-day bill rate is forecast to lift slightly to reach 2.6 percent by September 2019 (see forecasts below).

The Reserve Bank, as widely predicted, kept the OCR at 1.75 percent at the last review. Given low inflation is almost cemented in place at the moment, there is little pressure on the Reserve Bank to lift the OCR, and a number of respectable economic commentators expect the OCR to remain on hold until late next year.

Forecasts: Interest Rates (90 day bills)

	Years ending		
	Sep 17	Sep 18	Sep 19
Highest	2.0	2.3	3.2
Average	2.0	2.1	2.6
Lowest	2.0	2.0	2.1

Source: ASB, BNZ and Westpac

The NZIER Monetary Policy Shadow Board, in its most recent statement (8 August), also saw little urgency for the OCR to increase. Its recommendation to the Reserve Bank was broadly unchanged from the previous meeting in June: *"Although inflation is back within the Reserve Bank's 1 to 3 percent target band, there is limited risk of acceleration. The recent easing in inflation and softer than expected GDP adds to the case that there is little urgency to lift the OCR"*

The Shadow Board's average recommended interest rate eased from 1.82 (last quarter) to 1.79 percent.

The NZ dollar – a bob each way

While the outgoing Governor of the Reserve Bank, in his farewell speech, tried to argue that the New Zealand dollar is overvalued and needs to be lower, his comments are likely to have little effect on the direction of the dollar over the short term. It is interesting that respondents' comments for the BNZ-BusinessNZ Performance of Manufacturing Index (PMI) and its sister survey the Performance of Services Index (PSI) are not expressing major concerns about the value of the dollar.

The terms of trade data for the June quarter show terms of trade (purchasing power of New Zealand's exports aboard) again approaching record levels, with a strong and ongoing demand for New Zealand's exports. Migration levels continue to remain high and New Zealand's very stable political and governance regime is an added bonus.

Notwithstanding the above, determining the future direction of the exchange rate is fraught with difficulty and short-term fluctuations will continue to be the order of the day – whether driven by internal decision-making or perhaps more importantly, what is happening on international markets and the stability of the international economy more generally.

Averaging forecast results suggests there will be very little movement in exchange rates although the differences between the highest and lowest forecasts are quite significant as can be seen below.

Forecasts: Exchange Rates

AUD (cents)			
	Sep 17	Sep 18	Sep 19
Highest	0.92	0.95	0.95
Average	0.92	0.93	0.93
Lowest	0.92	0.90	0.91

USD (cents)			
	Sep 17	Sep 18	Sep 19
Highest	0.73	0.76	0.80
Average	0.72	0.71	0.72
Lowest	0.72	0.67	0.65

TWI			
	Sep 17	Sep 18	Sep 19
Highest	76.7	77.6	78.3
Average	76.6	75.8	76.0
Lowest	76.4	73.4	72.1

Source: ASB, BNZ and Westpac

Inflation – settled

Forecasts below show inflation will likely remain well within the Reserve Bank's target band of 1-3 percent to September 2019, although gradual rises cannot be ruled out.

An interesting fact of inflation is that over recent years both global competition and innovation have cranked up the development of better products and services at lower cost. Consequently, the old argument that as demand ratchets up prices will rise does not necessarily hold now as it did in the past. Prices over a wide range of products and services, in real terms and nominal terms, are dropping. This is a significant shift away from the traditional assumption that generalised inflation is here to stay.

Some of the factors driving non-tradables' inflation to date have eased slightly over recent months, particularly house price inflation. This change has no doubt been influenced to some extent by loan-to-value ratio restrictions and generally tighter (voluntary) bank restrictions on lending. More recently, the uncertainty surrounding the outcome of the general election could have some people holding off making key investment decisions to better gauge the lie of the land post-election.

On the international scene, relatively low global inflation combined with a relatively stable New Zealand dollar is ensuring that tradables inflation remains firmly under control.

One factor which might impact on inflation is the continued spending promises, increasing almost daily, as the parties try to woo swinging voters. Depending where the election results end up, there could be substantial expenditure increases ultimately putting more pressure on capacity.

Forecasts: percent Change in Inflation (CPI)

	Years Ending		
	Sep 17	Sep 18	Sep 19
Highest	1.9	1.9	1.8
Average	1.7	1.6	1.8
Lowest	1.6	1.3	1.7

Source: ASB, BNZ and Westpac

1.3 Business activity and consumer confidence remain solid

Business activity solid

Business and consumer confidence has generally remained firmly in positive territory for some time. More importantly, businesses are generally upbeat about their own business prospects, a good indicator of future growth prospects.

A number of regular surveys show business and consumer confidence firmly on solid ground.

The New Zealand Institutes of Economic Research's Quarterly Survey of Business Opinion (QSBO) shows confidence on the whole remaining solid across sectors with businesses remaining optimistic about increasing employment and investing in plant and machinery.

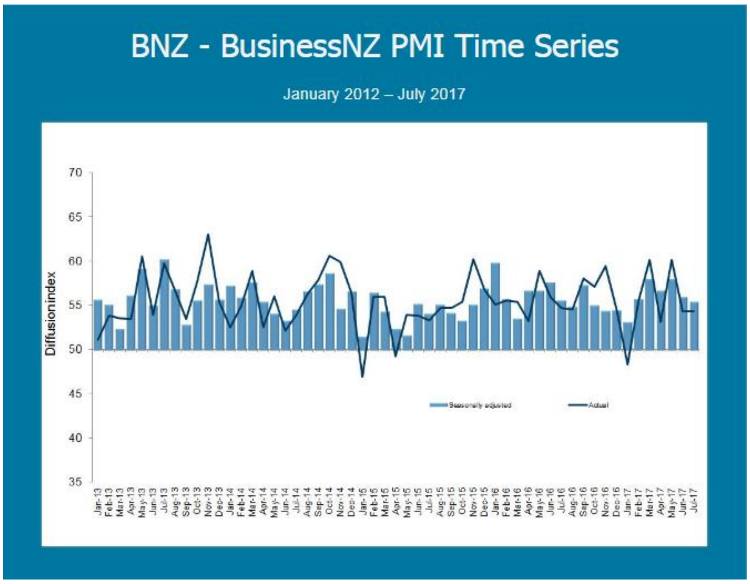
Federated Farmers' July Farm Confidence Survey shows the highest level of confidence in general economic conditions since 2014. Perhaps not surprisingly, dairy and arable farmers are the most optimistic and all regions are demonstrating more optimism than in the last survey in January 2017.

The Federated Farmers' survey showed regulation and compliance costs are farmers' biggest concerns, leapfrogging over farm-gate and commodity prices, now in second place. 'Public perceptions of farming' is third on the list of concerns and the environment is fourth.

Business confidence is also seen in the recent 2017 Deloitte BusinessNZ Election Survey, the monthly BNZ – BusinessNZ Performance of Manufacturing Index (PMI) and its sister survey, the Performance of Services Index (PSI).

The seasonally-adjusted PMI for July was 55.4 (a PMI reading above 50.0 indicates that manufacturing is generally expanding; below 50.0 that it is declining). This was slightly lower than June, and similar to expansion levels seen in February. At 55.4 in July, the PMI remains firmly above its long-term average of 53.3. Overall, the sector has remained in expansion in all months since October 2012.

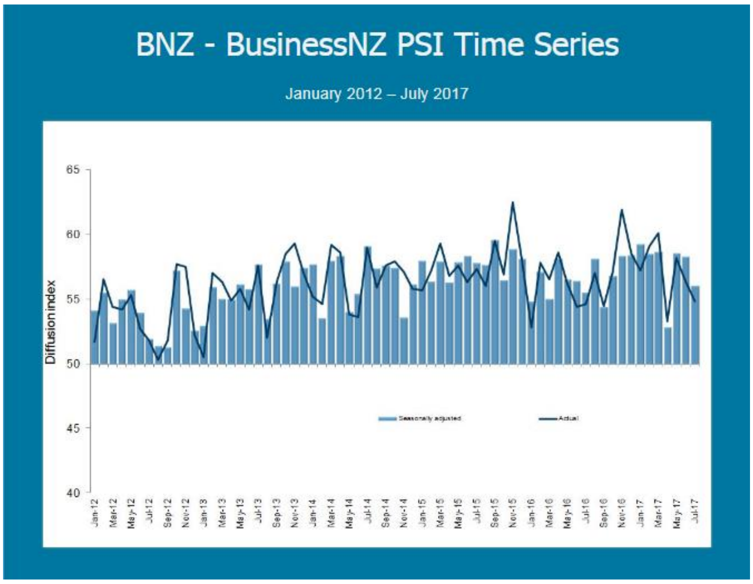
Expansion across the fives indices (Production, Employment, New Orders, Finished Stocks and Deliveries) was very even for July, with the total difference between the lowest and highest results at only 1.2 points. Of particular note was the highest level of expansion for employment (56.4) since September 2014, along with finished stocks (also at 56.4). However, both production (56.0) and new orders (55.4) continued to slip in terms of expansion.



With expansion again easing during July, the proportion of positive comments dropped to 56.1 percent, compared with 68.2 percent in June and 69.4 percent in May.

The services sector also remains in positive territory, despite winter having a negative effect on some businesses.

The PSI for July was 56.0. This was 2.3 points lower than June, and the lowest value since April (A PSI reading above 50.0 indicates that the services sector is generally expanding; below 50.0 that it is declining).



Despite the dip in expansion, July's result was still clearly above the long-term average for the survey, and showing solid expansion.

Of respondents' responses, a number of negative comments centered on wet and wintery conditions hampering business activity, although almost 60 percent were still positive.

1.4 Labour market – marching on

Employment – solid growth

The labour market continues to perform reasonably well with a number of forward-looking indicators showing unemployment is likely to remain relatively static at around 4.6 percent over the forecast period, as can be seen below.

Forecasts: Unemployment percentage (HLFS)

	Quarter		
	Sep 17	Sep 18	Sep 19
Highest	4.7	4.7	4.7
Average	4.6	4.6	4.6
Lowest	4.5	4.5	4.4

Source: ASB, BNZ and Westpac

A number of official statistics and business surveys indicate the labour market is relatively strong. StatisticsNZ's Household Labour Force Survey (HLFS), the PMI and its sister survey, the PSI, show continued strength largely across the board. The PMI shows the level of expansion for employment in July 2017 (56.4) was the highest since September 2014. The PSI also shows employment trucking along at a satisfactory level of expansion (55.2) for July.

The Ministry of Business, Innovation and Employment (MBIE) *Jobs Online* Monthly Report – July 2017 measures changes in online job advertisements from four internet job boards – SEEK, Trade Me Jobs, the Education Gazette and Kiwi Health jobs.

The MBIE report shows that over the year to July, online vacancies have increased by 9.2 percent with Construction and Engineering leading the charge (up 20.4 percent from July 16 to July 17) as the table below indicates.

***All Vacancies Index* by industry group, trend series**

Industry	Monthly change (Jun 17 - Jul 17)		Annual change (Jul 16 - Jul 17)	
Accounting, human resources, legal and administration	▲	0.2%	▼	0.6%
Construction and engineering	▲	1.5%	▲	20.4%
Education and training	▲	1.2%	▲	13.7%
Healthcare and medical	▬	n/c	▲	5.4%
Hospitality and tourism	▼	0.3%	▲	8.2%
Information technology	▬	n/c	▼	11.8%
Sales, retail, marketing and advertising	▼	0.2%	▲	5.3%
Other	▲	1.1%	▲	20.4%
Total job vacancies*	▬	n/c	▲	9.2%

* The totals may not line up as each industry is individually seasonally adjusted, while the total job vacancies series is seasonally adjusted separately.

Source: MBIE

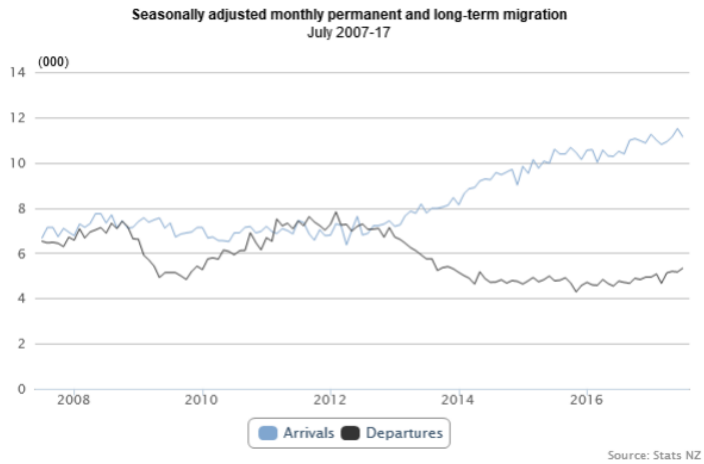
The latest ANZ Jobs Ads data for August 2017 shows that job ads (seasonally adjusted) reached a new record high – just.

Notwithstanding the overall positive picture for aggregate employment growth and associated declines in unemployment, plus continued strong growth in job vacancies, significant regional differences and perhaps more importantly differences in various regional areas' unemployment rates remain. Considering that there are still relatively high levels of youth unemployment and young people not in education, employment or training (NEETS) a great deal of effort will be required to ensure the most vulnerable in society are able to actively participate in the labour market rather than simply fall into a life of benefit dependency.

The Government has rightly focused on a social investment approach to improving outcomes for at-risk youth but the need remains to strengthen mechanisms to encourage and retain a connection with the labour market. This may involve greater individual case management to understand the barriers to greater workforce participation, whether these involve child-care, transport or other issues. In this respect many of the political parties contesting this election are putting a particular focus on ensuring the connectedness of youth to employment, training, or generally getting people up to speed.

While the focus on improving outcomes is very positive, it is important that the effect of any labour market policy or legislative change is well-thought through and the potential for unintended consequences understood. For example, while the objective of increasing salaries/wages for the most low-skilled employees (or potential employees) is a worthy objective, the mechanisms to achieve this could have negative effects on precisely the people any such policy is intended to help. For example, significant increases in the minimum wage without commensurate increases in labour productivity are likely to result in increased unemployment, effectively locking the most vulnerable out of the labour market. This underlines the importance of ensuring policy is well coordinated and acts to support growth in opportunities, not introducing polices that potentially work against each other.

Net migration continues to reach record highs with annual net migration over 72,000 in the year to July 2017. Given the importance of migration to the NZ economy in supplying the skills in order for the economy to grow it is disconcerting that one of the focuses of pre-election campaigning has been on proposals to substantially cut migration numbers without seriously looking through the implications of drastic cuts.



Simplicity is needed for an effective immigration policy. Concerns about immigration levels over recent years have resulted in a system laden with rules that are complex and hard to navigate. This in itself is a constraint on business.

It is to be hoped that post-election, there can be a rational discussion of immigration settings able to stand the test of time, rather than knee-jerk reactions to politically-charged hot-spots.

Labour costs – increasing slowly

Forecasts below indicate labour costs in general increasing relatively slowly and remaining at around 2 percent growth per annum over the forecast period to September 2019.

Forecasts: Labour cost index percentage change (wages & salaries)

	Years ending		
	Sep 17	Sep 18	Sep 19
Highest	2.2	2.2	2.4
Average	2.0	2.1	2.1
Lowest	1.9	2.0	2.0

Source: ASB, BNZ and Westpac

Expectations are that a tighter labour market will not flow through to significantly increased wage pressures, as can be seen below.

In many respects it is slightly puzzling that with greatly improved employment growth and firms' reported difficulties in finding skilled staff, wage costs have not risen significantly – yet.

Given several political parties are advocating quite significant changes to employment relations legislation, including restrictions on immigration and significant changes to minimum wage legislation and new wage bargaining mechanisms, it could well be a case of watch this space. However, with New Zealand largely open to international capital and labour flows, wage rises in the absence of significant productivity gains are likely to be short-lived and unsustainable.