BUSINESS NZ

PLANNING FORECAST

SEPTEMBER 2018

BusinessNZ

Good growth but risks

Executive Summary

Though a snapshot of the key economic indicators in NZ still provides a pretty positive picture, the more important focus should be on the medium to long-term prognosis. A number of forward-looking indicators show some easing of late.

Changes and potential changes both to international and domestic policy settings have the capacity to heighten the downside risks to growth over the medium term.

On the international front, the World Bank's latest Global Economic Prospects contains a summary likening the world economy to a sailor, and is worth repeating: *"The current state of the global economy resembles that of a sailor whose boat was caught on a sandbar but is now freed by the rising tide. The sailor is naturally relieved to be able to set sail. But this relief must be tempered by the urgency to pilot towards deeper seas before the receding waters beach the ship again."*

International growth rates have improved in key economies such as China and the United States with better investment and employment prospects, but the medium term leaves a lot to be desired, particularly the uncertainty associated with the trend to trade protectionism and continuing high levels of debt.

The risk of a financial market correction, geopolitical hazards and the impact of moves internationally to raise interest rates in light of rising inflationary pressures have the potential to weigh significantly on future international growth prospects.

As an intentional trader still very dependent on commodity exports, NZ will not be immune from any fall-out from lower international growth prospects and the flow-on effects of increasingly nationalistic and protectionist trade policies.

However, despite the above risks, the international ship is still sailing in reasonably deep waters.

What about the domestic scene? The NZ economy is forecast to grow moderately at around 3 percent over the forecast period out to September 2020.

NZ's terms of trade (a measure of the purchasing power of its exports and a key indicator of the economy overall) are robust, driven largely by continuing solid prices for meat and dairy products.

Employment continues to grow and the unemployment rate has stabilised at around 4.5 percent. Inflationary pressures are benign – to date. There is little pressure on the Reserve Bank to raise interest rates and consequently, the NZ exchange rate is still relatively favourable to exporters.

The credit agency Moody's has recently maintained the Government's credit rating at triple A, with the outlook described as stable.

A lot has been said recently about low levels of business confidence, including businesses' own activity. For business to have the confidence to invest, there needs to be a degree of comfort that the key pillars of monetary, fiscal and regulatory policy are fit for purpose or, perhaps more importantly, that they reflect international best practice. With the international market for capital and labour relatively mobile, any undermining can affect whether businesses choose to put their capital at risk.

HIGHLIGHTS

The NZ economy is still forecast to grow at around 3 percent out to September 2020 but potential headwinds may result in slightly lower growth.

The BusinessNZ Economic Conditions Index (a measure of NZ's major economic indicators) sits at 5 for the September 2018 quarter, up 1 on the previous quarter and up 3 on a year ago.

The BNZ - BusinessNZ Performance of Manufacturing Index (PMI) and its sister survey, the Performance of Services Index (PSI), are still in positive territory, although there has been some easing of late.

Despite reasonably robust economic data across a range of sectors, business confidence remains downbeat. Policy uncertainty and some ad hoc changes are likely to be driving this continuing nervousness while businesses await the outcomes of a myriad of government reviews and taskforces.

In making policy changes the Government must be cognisant of the importance of maintaining world best practice in fiscal, monetary and regulatory policy settings. Any undermining of these pillars will scare off both the international and domestic investors on whom NZ is heavily reliant to provide investment and employment for future generations.

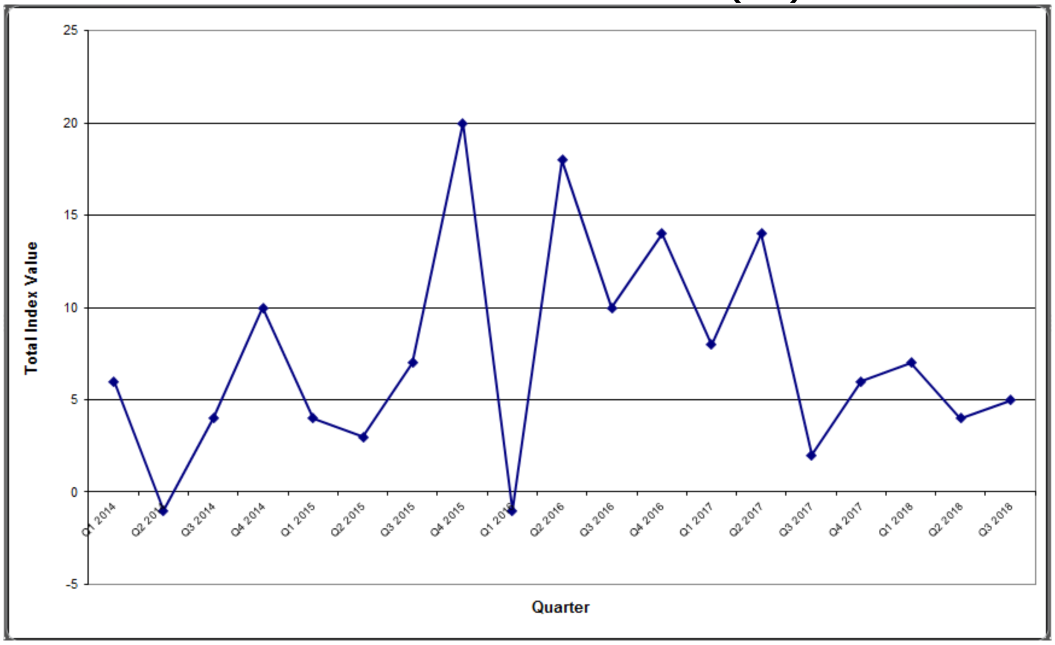
At the international level, growth rates remain solid, although there are risks over the medium term. These include greater moves towards trade protectionism and tit for tat tariff policy retaliation from affected countries.

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 5 for the September 2018 quarter, up 1 on the previous quarter and up 3 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 3 for the September 2018 quarter, down 2 on the previous quarter but up 4 on a year ago. New Zealand's terms of trade remain close to record levels on the back of still solid world commodity prices, including for dairy, beef, lamb and horticultural products.

Monetary policy/pricing indicators sit at 0 for the September 2018 quarter, up 1 on the previous quarter and up 3 on a year ago. Domestic inflation remains under firm control although internationally, inflationary pressures are slowly rising, the consequence of an improved world economy.

Business/consumer confidence indicators sit at 1 for the September 2018 quarter, up 2 on the previous quarter and the same as a year ago. Business confidence remains downbeat while consumer confidence continues to slip and is now around its long-run average.

Labour market indicators sit at 1 for the September 2018 quarter, the same as the previous quarter and down 4 on a year ago. Employment continues to edge up and unemployment has stablished at low levels. Declines in net migration from historical peaks and slowing job ads will dampen future labour force 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. The results for the September quarter 2018 are estimates based on available information to date.

PART 2: THE NZ ECONOMY – WHERE ARE WE HEADING

1.1 Economic growth (GDP) – softening ahead?

Many key economic indicators remain on the positive side of the ledger, although a number of risks (both domestically and internationally) could take the shine off what is still a reasonably positive outlook for economic growth. The NZ economy is forecast to grow moderately, averaging around 3 percent out to September 2020 (see below).

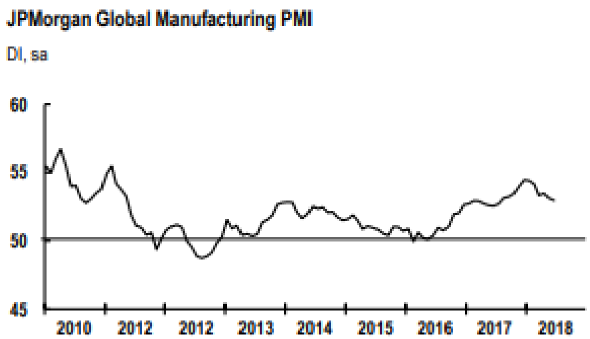
NZ's terms of trade (a measure of the purchasing power of its exports and a key indicator of the state of the economy overall) are still close to an all-time high, driven largely by higher meat and dairy prices.

Employment continues to grow and the unemployment rate has stabilised at around 4.5 percent. Inflationary pressures remain benign. There is little pressure on the Reserve Bank to raise interest rates and consequently, the NZ exchange rate remains relatively favourable to exporters.

Notwithstanding a reasonably positive outlook, there are a number of risks that need to be factored in, both from a domestic and international perspective.

According to the International Monetary Fund (IMF) World Economic Outlook Update (July 2018), global growth is projected to reach 3.9 percent in 2018 and 2019, in line with earlier forecasts. But growth expansion is becoming less even, and risks to the IMF outlook are mounting.

The J.P Morgan Global Manufacturing PMI, measuring the performance of global manufacturing, remains in positive territory, although there has been a slight lowering in growth as outlined in the graph below.



Though the Index posted a 21-month low of 52.5 in August 2018, down from 52.8 in July, the headline PMI has stayed above the neutral 50.0 mark for 30 consecutive months and is currently still above its long-term average of 51.5.

International risks:

- International growth rates have improved in key economies such as China and the United States, with better investment and employment prospects, but medium-term prospects leave a lot to be desired, particularly given the uncertainty associated with moves by trading nations towards trade protectionism and retaliatory action.

- The risk of a financial market correction, geopolitical hazards and the effect of moves internationally to raise interest rates in light of rising inflationary pressures have the potential to weigh significantly on future international growth prospects.

- The potential for a national and international share-market correction, along with rising interest rates, to increase cost structures and uncertainty, adversely affecting company earnings.

International trade is a moveable feast at present with President Trump's desire to reposition the USA to get better trade deals, using the imposition of tariffs left, right and centre to achieve that end. That is resulting in tit for tat tariffs with all countries involved, but mainly China and the EU, ratcheting up the retribution.

Though New Zealand is not directly in the firing line (other than for steel and aluminum), President Trump's moves to subsidise US agriculture to shield its farmers from trade war tariffs could have a negative longer-term impact. Subsidies not only tend to lead to oversupply and stockpiling, thereby depressing international commodity prices, but are also hard for future politicians to remove. Ironically, US agriculture groups are not asking for this sort of support; they would prefer a level playing field for their exports.

On the positive side, the Trump style of negotiation seems to have lit a fire under the rest of the world that still favours open markets and low tariffs, leading to a redoubling of the effort to achieve high-quality rules-based FTAs. New Zealand is benefiting from this move with potential trade deals with the EU, Pacific Alliance and the UK getting better and quicker traction than they would have otherwise.

Notably, South Korea is lining up to be a new addition to the CPTPP – which New Zealand is currently processing through the parliamentary system.

Domestic risks:

- As an international trader still very dependent on commodity exports, NZ will not be immune from the potential fall-out associated with lower international growth prospects and the flow-on effects of increasingly nationalistic and protectionist trade policies.

- For the agricultural community, the (downside) risks are more likely to be related to domestic, rather than international, policy settings. For example, the sector will keenly assess any proposals coming out of the Tax Working Group for their environmental impact, such as wealth and/or environmental taxes. The final report is due around February 2019, with the interim report relatively benign. Increased restrictions on land use (particularly in the rural sector) may also undermine confidence to invest in that sector.

- Fonterra's recent downgrade in the forecast payout for the 2018/19 season by 25 cents to $6.75kgMS will likely have a limited effect on confidence, although the cancellation of the dividend payout for the remainder of the year has seen the Fonterra Shareholder Fund take a bit of a hit on the NZX. Increased Mycoplasma bovis reporting will also be unsettling, the chances of eradication being increasingly remote.

- Outcomes from the numerous Taskforces and Working Groups set up to examine a wide range of issues from tax, monetary policy, local government funding, health and social policy to "fair pay" agreements. The jury is out on whether these will produce consistent policy, promoting increased business competitiveness.

- Net migration numbers, while still high, are continuing to decline from the record levels achieved a year ago. A further significant decline could reduce the demand of goods and services and, also importantly, the supply of labour on which many businesses depend.

- A great deal has been said recently about low levels of business confidence, including businesses' own activity. Uncertainty is part and parcel of doing business. The key is to ensure government policies do not unduly add to the normal market risks that businesses face every day when producing goods and services for both domestic and international markets.

- There is also the potential risk of individuals, households, and businesses seeking government (taxpayer) funding for pet projects, thereby transferring risk from businesses to taxpayers if ventures fail.

For businesses to have the confidence to invest, they need a degree of comfort that the key pillars of monetary, fiscal and regulatory policies are fit for purpose or, perhaps more importantly, that they reflect international best practice. With the international market for capital and labour relatively mobile, any undermining can affect whether businesses choose to put their capital at risk.

Forecasts: Real GDP percent Growth

	Years Ending		
	Sep 18	Sep 19	Sep 20
Highest	2.8	3.1	3.0
Average	2.8	3.1	2.9
Lowest	2.8	3.0	2.7

Source: ASB, BNZ and Westpac

1.2 Monetary conditions – Reserve Bank changes on the way

On the domestic front, proposed changes to the Reserve Bank Act 1989 are making their way through Parliament via the Reserve Bank of New Zealand (Monetary Policy) Amendment Bill currently before the Finance and Expenditure Select Committee.

The Bill has two main objectives, namely to:

1. Amend current monetary policy objectives to require consideration of maximum sustainable employment alongside price stability in monetary policy decision-making; and
2. Institute a monetary policy committee (MPC) to make decisions on monetary policy.

BusinessNZ has been a strong advocate over many years of the 1989 Reserve Bank Act's overriding objective of price stability and independent decision making, with responsibility for monetary policy decisions resting with the Reserve Bank Governor.

A number of reviews of the Reserve Bank Act, including the latest Independent Expert Advisory Panel to the Minister of Finance (March 2018), have found the Reserve Bank has served NZ well over the years. Indeed, a number of papers have upheld the Bank's independence and its clear focus on price stability as being in line with world best practice.

BusinessNZ is concerned that the addition of a "maximum sustainable employment" objective alongside the price stability objective has the potential to muddy the waters when it comes to what monetary policy can actually achieve. Employment outcomes are the result of many factors; beyond the very short term, monetary policy settings are unlikely to have any material impact.

The Expert Advisory Panel Report to the Minister of Finance (May 2018) appears at least to acknowledge this fact by stating that:

> *"Monetary policy is not, however, a primary determinant of the level of full employment, which is largely determined by structural factors such as the level of skills in an economy, the tax system, and labour and product market regulations" (para 8, p.10).*

Consultation on Phase 2 of the Reserve Bank Act Review will run from November 2018 until late January 2019. A consultation paper will be released covering the following topics:

- Overarching objectives of the Reserve Bank set out in legislation
- Institutional governance and decision making
- The case for and against separation of prudential supervision from the Reserve Bank
- The case for and against depositor protection (including the option of deposit insurance)
- Reconsidering the regulatory perimeter of bank regulation.

Interest rates – locked down

The 90-day bill rate is forecast to edge up slightly by September 2020 (see forecasts below).

At its last review, the Reserve Bank, as widely predicted given some current uncertainty both nationally and internationally, kept the OCR at 1.75 percent. There is little pressure at this stage to lift the rate, certainly the majority – but not unanimous – view of the Institute of Economic Research's (NZIER's) Shadow Policy Board at its most recent review.

At the international level, an improvement in the global economy has seen a number of countries raise interest rates, albeit from a very low base. Rising interest rates resulted in a sell-off in equities markets earlier this year, particularly in the US, although key US equity indexes have since recovered the ground lost in February. However, the potential for trade wars in light of President Trump's trade policy measures is creating some volatility in international, and particularly US, equity markets.

For other countries, including the EU, moving towards more normalised interest rates and monetary policy settings is still some way off, with very low or even negative interest rates continuing to be the order of the day.

Forecasts: Interest Rates (90-day bills)

	Years ending		
	Sep 18	Sep 19	Sep 20
Highest	2.0	2.3	3.0
Average	1.9	2.1	2.6
Lowest	1.9	2.0	2.4

Source: ASB, BNZ and Westpac

The NZ dollar – stable

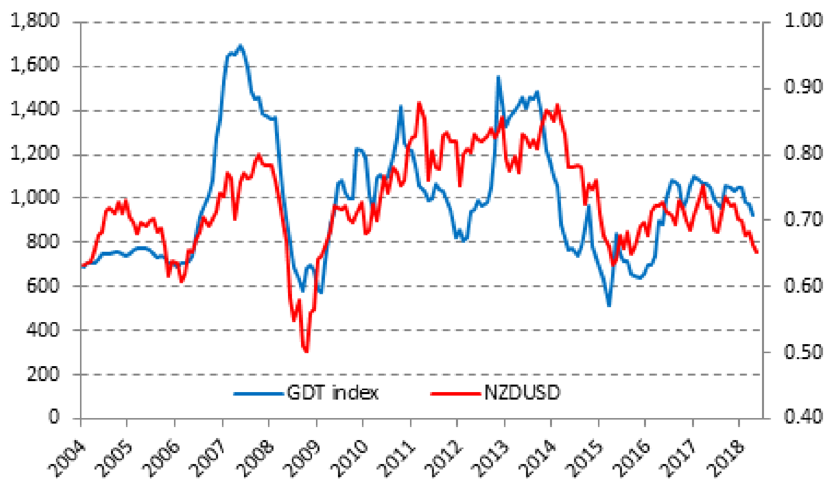
The $NZ, on average, is expected to remain relatively stable over the period to September 2020 (see below).

Uncertainty over trade deals and uncertainty in general will impact on the currencies of countries such as NZ that depend largely on commodity-based exports.

The pattern in global currency markets over recent months has been for a strengthening in the US dollar against almost all currencies when the threat of trade wars raises its head – quite often over recent months.

The fortunes of the NZ dollar have generally been closely correlated within movements in world commodity prices, as can be seen from the relationship between the global dairy trade (GDT) and the NZDUSD (see below).

Global Dairy Trade (GDT) v NZDUSD



Other factors that may keep the NZ dollar stable include the Reserve Bank's clear signal of lower interest rates for longer, while continuing low levels of business confidence have also tended to weigh the NZ dollar down.

Notwithstanding the above, trying to predict the future value of the NZ dollar or any other currency is fraught. Some volatility is the name of the game at present.

Forecasts: Exchange Rates

AUD (cents)			
	Sep 18	Sep 19	Sep 20
Highest	0.92	0.92	0.92
Average	0.91	0.91	0.91
Lowest	0.90	0.91	0.91

USD (cents)			
	Sep 18	Sep 19	Sep 20
Highest	0.67	0.69	0.69
Average	0.67	0.67	0.68
Lowest	0.66	0.64	0.67

TWI			
	Sep 18	Sep 19	Sep 20
Highest	72.4	72.1	72.0
Average	72.1	71.3	70.8
Lowest	71.8	70.0	69.6

Source: ASB, BNZ and Westpac

Inflation – stability rules to date

Forecasts below show inflation likely to remain well within the Reserve Bank's target band of 1-3 percent to September 2020, although gradual rises cannot be ruled out. There are potential pressures from both tradable and non-tradable inflation.

On the tradable side, a continued improvement in the world economy is putting some, at this stage minor, upward pressure on commodity prices, while monetary policies across a range of countries are finally moving back toward more long-term normalised positions. In short, inflationary pressures, while still low internationally, have the potential to escalate over time, particularly as oil prices continue to ramp up in light of global demand.

The latest J.P Morgan Global Manufacturing PMI for August 2018 showed that in terms of global manufacturing costs, input cost inflation remained elevated in August, despite easing to a three-month low. Part of the rise in purchase prices was passed on to clients, leading to a further solid increase in average output prices.

A weaker NZ dollar is having some upward impact on the petrol prices facing motorists, while the specific Regional Fuel Tax introduced in Auckland on 1 July 2018 will add further to price increases.

Increases to the minimum wage for lower income earners may put some upward pressure on prices although in most industries, both domestic and international, the pressure will either see costs largely absorbed through greater productivity gains or households sourcing materials off-shore.

Downside pressures on inflation also exist.

Over recent years, global competition and innovation have allowed 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 are dropping, both in real and nominal terms, a significant shift away from the traditional assumption that generalised inflation is here to stay. Moreover, consumers have much more choice in where they can source their products, including the fact that on-line shopping is now a very fast and efficient method of obtaining goods and services.

House prices have largely stabilised, although there are pockets across the country where price rises are still significant.

Overall, the housing market is cooling faster than many have predicted as migration continues to ease, while the Government is considering a number of policy changes that have, or will potentially have, a sobering effect on house price inflation. These include loss ring fencing, extension of the bright line test, and any changes to the tax treatment of housing that might come out of the Tax Review, such as some form of capital gains tax.

Net long-term migration numbers have trended down after the record number of people coming into the country over the last few years and this will continue to take some of the pressure off both the housing market and general demand. But the Government's decision to stop foreigners buying property in NZ is likely to have little effect on house prices.

Given all the above, the factors potentially driving inflationary pressures up closely align with the factors driving inflationary pressures down. Therefore, it is unlikely the Reserve Bank will be moving on interest rates, either up or down, for some time.

Forecasts: Percent Change in Inflation (CPI)

	Years Ending		
	Sep 18	Sep 19	Sep 20
Highest	1.8	2.2	2.1
Average	1.7	1.9	1.8
Lowest	1.7	1.6	1.6

Source: ASB, BNZ and Westpac

1.3 Business activity and consumer confidence

Business activity and business confidence – mixed messages

Though a number of business activity indicators are still relatively solid, business confidence remains in the doldrums with little uplift since the post-election drop-off last year.

Key quantitative indicators, such as the latest BNZ-BusinessNZ Performance of Manufacturing Index (PMI) and its sister survey, the Performance of Services Index (PSI), remain in expansion mode but the level of expansion has continued to ease over recent months. On the other hand, business confidence remains at historically low levels not seen since the global financial crisis (GFC) a decade ago.

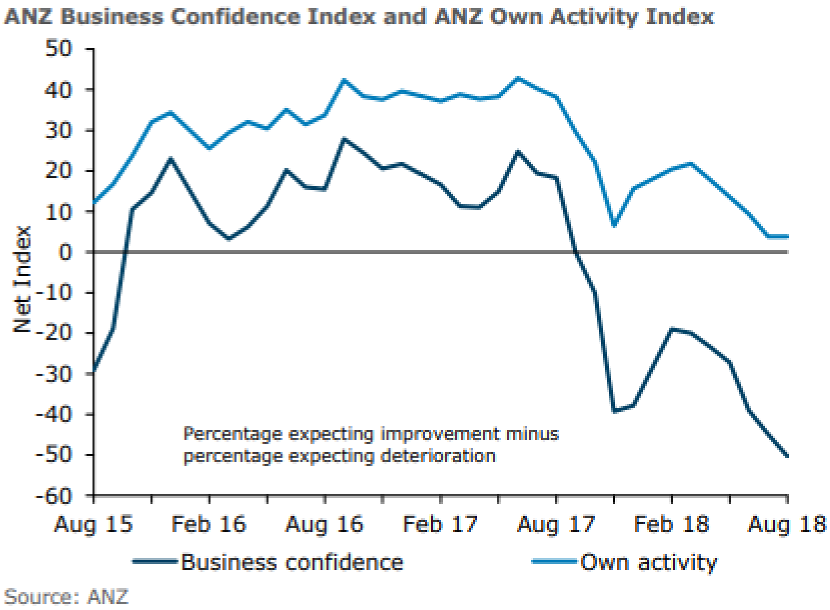
Perhaps more importantly, businesses' view of their own activity levels, while stable, is still low by historical standards. Some commentators have rightly said that confidence has often fallen post-election in the past, but that businesses continue to be concerned about their own business prospects is worrying given the relatively close connection between firms' own prospects and economic growth over time. The other worrying factor is that this concern is evident over a wide range of surveys on business sector confidence, tending to negate any bias factors associated with any particular survey.

There will likely be a range of reasons for such business community pessimism, not least the uncertainty over policy direction and the ad hoc changes mentioned earlier in this report.

Much has been said recently about low levels of business confidence, including businesses' own activity. Uncertainty is part and parcel of doing business. The key is to ensure government policies do not unduly add to the normal market risks that businesses face every day when producing goods and services for both the domestic and international markets.

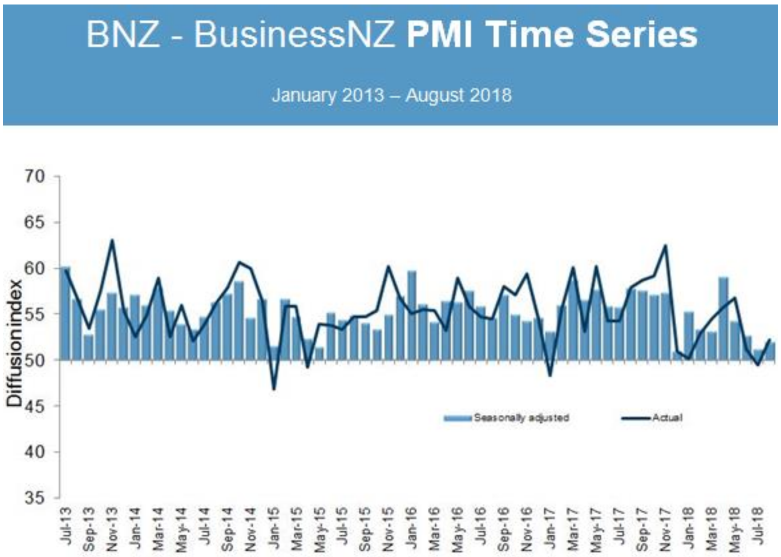
For businesses to have the confidence to invest, they need a degree of comfort that the key pillars of monetary, fiscal and regulatory policy are fit for purpose or, perhaps more importantly, that they reflect international best practice. Any undermining of these pillars can affect whether businesses will elect to put their capital at risk. At the end of the day, the international market for both capital and labour is highly mobile.

The New Zealand Institute of Economic Research's (NZIER) latest Quarterly Survey of Business Opinion (QSBO) shows headline business confidence and measures of businesses' own activity falling in the June 2018 quarter, while the ANZ's monthly Business Outlook (August 2018) shows the deteriorating trend continuing into July, although business' own activity levels stabilised at historically low levels.

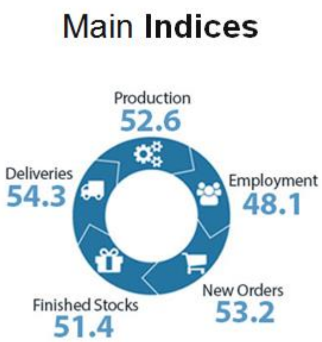


A net 50 percent of businesses are pessimistic about the year ahead, down a further 5 points from July. Firms' views of their own activity have stablished at a net 4 percent expecting an improvement, well below the long-term average of +27 percent.

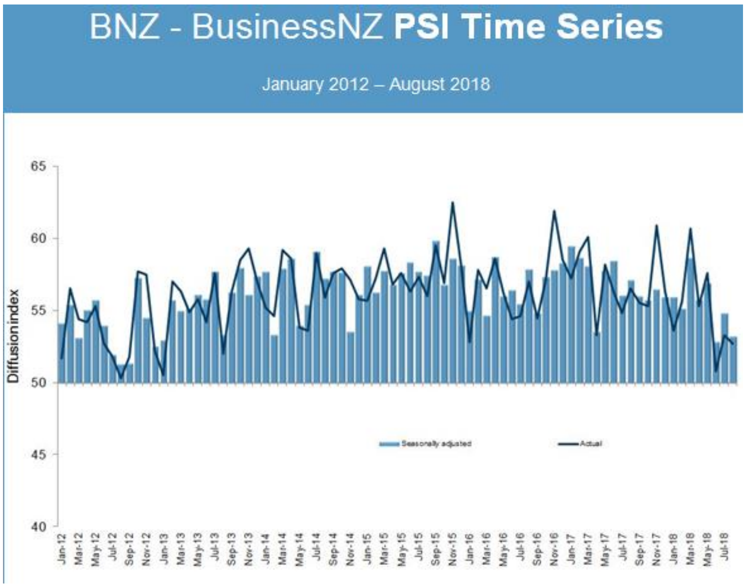
The seasonally adjusted BNZ-BusinessNZ Performance of Manufacturing Index (PMI) August 2018 was 52.0 (a PMI reading above 50.0 indicates that manufacturing is generally expanding, below 50.0 that it is declining). Though this was 0.8 points higher than July, it remains below the long run average expansion level of 53.4.



Though production (52.6) returned to expansion and new orders (53.2) also improved from July, employment (48.1) fell back into contraction to its lowest level since August 2016. Looking at the remaining sub-indices, deliveries (54.3) remained largely unchanged, while finished stocks (51.4) decreased 2.1 points.



Like the PMI, the seasonally adjusted BNZ-BusinessNZ Performance of Services Index (PSI) continues to drift downwards, although from a higher base level.



The PSI for August was 53.2, which was 1.6 points lower than July (a PSI reading above 50.0 indicates that the services sector is generally expanding, below 50.0 that it is declining). This was also below the long run average of 54.5 for the survey.

Looking at the sub-indices, the two key sub-indices, involving activity/sales (53.8) and new orders/business (58.8), both decreased in August, with the former at its lowest point since February. For the third month running, employment (49.9) remains stubbornly stuck on a figure representing almost no change, while stocks/inventories (51.8) showed some improvement from July.

On a brighter note, the proportion of positive comments in August (56.0) recovered somewhat from the decrease in July (53.8%).

Consumer confidence – cooling

Consumer confidence, unlike business confidence, is still relatively solid and is now around its historical average, although there has been further slippage of late. A number of factors are likely to be at play, including labour market activity remaining strong, inflation under firm control and interest rates remaining at historically low levels, reducing the cost of borrowing.

The ANZ-Roy Morgan NZ Consumer Confidence Survey showed confidence unchanged in August at 118, around its historical average. Though a little off the high reached in September last year, consumer confidence has been more or less solid for the last couple of years, as can be seen below.

ANZ-Roy Morgan Consumer Confidence

Source: ANZ, Roy Morgan

Consumers still appear to have little enthusiasm for paying down debt and household debt levels continue to edge up despite the threat of higher interest rates down the track. Consumers appear comfortable with the fact that mortgage interest rates have been at historical lows for some time now. However, they seem not to have factored in an understanding that interest rates will rise again, perhaps sooner rather than later, putting many households, and indeed some businesses, under financial strain.

Levels of household debt remain high at around 166 percent of household income as evidenced by data from the Reserve Bank. It should be noted that household debt comprises mortgage loans, consumer loans such as credit cards, and student loans.

1.4 Labour market – working parties aplenty

The Government continues apace with labour relations reform through both legislative changes and the establishment of a myriad of working parties looking at various issues to advance its agenda.

Many reforms have not been welcomed by business as they will reduce flexibility, increase costs, and in general make NZ businesses less competitive internationally. But some working parties are more technical in nature, addressing specific issues that have bothered employers and employees alike such as the much-needed Holidays Act changes, for example. Other working parties will likely result in vigorous debate – such as proposals to set up Fair Pay Agreements.

Below are reports on some of the working groups and their current status.

Fair Pay Agreements

The Working Group has so far had a number of meetings, and discussions are still at the exploratory stage. To date, no conclusions, preliminary or otherwise, have been reached. Many see the Fair Pay Agreements concept as taking New Zealand back to something like the earlier national award system where third party-agreed terms and conditions were set for most occupations, regardless of employer size or profitability. Some comparison can be made to the Australian Workchoices legislation which has been criticised as failing to leave economic forces free to have their effect. Contrary to intention, that has tended to limit rather than encourage wage growth.

Holidays Act

Early work of The Holidays Act Working Group has focused on defining issues prior to taking a broader consultative approach. The Group is to look at all aspects of entitlement and payment but will not be covering historical issues over leave payment. These will be managed separately and their resolution might require recourse to the courts, possibly via a test case. The Minister has said he wants the law to be right (with neither side losing out) and to take time to ensure that it is. The Group is to report back within 12 months.

Film Industry ("Hobbit Law")

This Group, set up to address the Government's election commitment to repeal the "Hobbit law", which protects the status of contractors in the film industry, has now concluded its work. Recommendations to the Minister of Workplace Relations and Safety will be delivered shortly once the full Working Group report is complete. It will focus on ensuring the screen industry (wider than film) remains incentivised to base operations in New Zealand.

The "Hobbit" discussion is a small subset of the wider conversation the Government has committed to have over the relationship between employed and contracted labour. Overall, this contracting versus employment discussion will be one of the most crucial issues employers will have to contend with in the coming months.

Future of Work

The Group has met, and reports indicate it will focus primarily on four key themes:

- Just transition
- Learning for life
- Technology
- Workplace productivity

LEGISLATION

Employment Relations Amendment Bill

The Government's Employment Relations Amendment Bill was reported back from the Education and Workforce Select Committee on 10 September, an extension from its previous report back date of 1 August 2018.

Aspects of the bill have been subject to considerable employer opposition, in particular:

- 90-day trial periods
- Union access to workplaces
- The duty to conclude a collective agreement, and
- The repeal of the ability to opt out of collective bargaining

Though the Bill as reported back contained some technical changes and a tightening up of language in some cases, there is little change that addresses the fundamental concerns that businesses had with the original bill.

Employment Relations (Triangular Employment) Amendment Bill

The triangular employment relationships issue should be part of the dependent contractor/general contracting discussion but is being addressed separately through the parliamentary process. The bill is currently before the Education and Workforce Select Committee with public hearings yet to begin. The bill's report back date is 29 November 2018 (extended out from its previous 21 September date).

Employment – modest growth and unemployment stabilising

According to StatisticsNZ's Household Labour Force Survey (HLFS) for the June 2018 quarter, the number of employed increased by 0.5 percent from the previous quarter to reach 2.631 million.

The unemployment rate and the underutilisation rate increased marginally from the previous quarter.

The unemployment rate was up 0.1 percentage point to 4.5 percent while the underutilisation rate was also up 0.1 percentage points to 12.0 percent.

The unemployment rate for males rose to 4.3 percent (up 0.3 percentage points) while for females it fell to 4.7 percent (down 0.2 percentage points).

The underutilisation rate is arguably just as important as the unemployment rate, in that it provides a broader gauge of untapped capacity in the NZ labour market than the unemployment rate alone.

In the June 2018 quarter, Southland had the lowest unadjusted regional unemployment rate at 3.0 percent, while Manawatu-Wanganui had the highest at 6.6 percent.

The unemployment rate is forecast to remain broadly stable at 4.4 percent out to September 2020 (see below).

Notwithstanding a still reasonable picture overall for aggregate employment growth, associated declines in unemployment and a continued, but moderating, growth in job vacancies, significant regional differences remain - perhaps more importantly, differences in various regional areas' unemployment rates. With levels of youth unemployment and young people not in education, employment or training (NEETS) still relatively high, a great deal of effort will be required to ensure the most vulnerable in society are able to participate actively in the labour market.

A slump in business confidence is also starting to flow through to future labour demand where both investment and employment intentions have eased.

Job ads growth continues to ease, consistent with a projected slightly lower growth path than many forecasters predicted a year ago.

Forecasts: Unemployment percentage (HLFS)

	Quarter		
	Sep 18	Sep 19	Sep 20
Highest	4.5	4.7	4.5
Average	4.4	4.4	4.4
Lowest	4.4	4.2	4.2

Source: ASB, BNZ and Westpac

Labour costs – edging up

Expectations are that a tighter labour market will slowly filter through into increased wage rates, as can be seen in the forecasts below.

Forecasts indicate labour costs in general are increasing relatively slowly with a growth rate of just over 2 percent per annum over the forecast period to September 2020.

Notwithstanding very modest increases in wage rates to date, significant increases in minimum wages over the next couple of years could have flow-on effects to other areas as employees raise relativity arguments. The Government's proposed regulatory regime for labour markets is also likely to ratchet up labour costs, more so than in the past, given a generalised move towards more centralised bargaining arrangements.

On 1 April 2018, the Government raised the minimum wage by 75 cents to $16.50 an hour. According to Statistics NZ, if wages affected by the minimum wage had remained constant in the June 2018 quarter, the Labour Cost Index (LCI) would have increased by 1.8% for the year to June 2018 rather than the 1.9 percent reflected in the LCI. The minimum wage will continue to rise in increments, reaching $20 per hour by 2021. These further rises will likely have greater impacts on the LCI given that more and more people will be affected by the successive rises.

Significant rises in public sector pay settlements for nurses and potentially more to come for the education sector and police etc could not only put the Government's accounts under added pressure but have the potential to add significantly to wage pressures. It is unclear how much has been set aside within the Government budget to fund specific contingencies such as wage claims, but the Minister of Finance has said there is a strictly limited pool available. The risk of relativity arguments may well force the Government's arm to revisit the coalition's fiscal responsibility rules.

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

	Years ending		
	Sep 18	Sep 19	Sep 20
Highest	2.0	2.4	2.7
Average	1.9	2.4	2.6
Lowest	1.8	2.3	2.3

Source: ASB, BNZ and Westpac