Recession in New Zealand deepens

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Despite widespread media praise lavished on a late December retail "boom", New Zealand's recession is worsening. Latest figures confirm that the economy shrank for the third consecutive quarter in the three months to September.

According to Statistics New Zealand's December 23 report, economic activity decreased by 0.4 percent in the September quarter, following declines in both the June and March quarters. The fall was cushioned by a 6 percent increase in the agricultural sector, while manufacturing (-2.5 percent) and construction (-1.2 percent) both contracted sharply.

The current account deficit—the gap between external income and spending—also grew, highlighting the country's vulnerability to the global credit crisis. The $NZ6 billion deficit for the quarter pushed the annual deficit to $15.5 billion, a rise from 3.1 percent of GDP at the beginning of 2002 to 8.6 percent for the year ended September 2008.

New Zealand's current account deficit is the fifth-worst of the 30 OECD countries, after Iceland, which is forecast to have a deficit equal to 24 percent of GDP for 2008, Greece 14.5 percent, Portugal 10.9 percent and Spain 9.7 percent. By comparison, the United States' current account deficit is predicted to be 4.9 percent of GDP for 2008.

According to financial analyst Brian Gaynor, New Zealand has become a "huge debtor nation," with international liabilities of $297.1 billion and assets of only $131.2 billion. The $165.9 billion difference between assets and liabilities compares with a $97 billion gap at the beginning of 2002.

The housing market was the main driver in the mounting debt gap, as local banks borrowed abroad and on-lent this money to property buyers. At the beginning of 2002, the banks had overseas assets of $29 billion and liabilities of $69.3 billion, giving a net overseas deficit of $40.3 billion. At the end of the latest quarter, the banks had foreign assets of $28.7 billion and liabilities of $147.9 billion, resulting in a deficit of $119.2 billion.

The deficit has been exacerbated over the past two quarters by the sharp fall in export commodity prices. Dairy, which makes up more than 20 percent of the value of exports, has suffered heavily. According to the ANZ Bank, dairy prices fell by 9.9 percent in October and 12.2 percent in November, down 42.7 percent from a peak in November 2007. Fonterra, the country's dominant export company, reduced its forecast payouts to suppliers for milk solids by 9 percent in November and has foreshadowed a New Year's resolution to make further cuts.

The $165.9 billion gap between foreign claims on the economy and investment abroad is equivalent to 92 percent of GDP, very high by international standards. The bulk of that—$154 billion—is debt and much of it is short-term, increasing the country's exposure to the turbulent global credit markets. The inflow of capital to fund the deficit came largely ($5.5 billion) from a divestment of foreign exchange reserves held by the Reserve Bank and the Treasury.

Commentators, such as ANZ Bank economist Philip Borkin, immediately signalled deepening attacks on living standards. Borkin argued that the ballooning current account deficit "means we are spending much more than we save as a nation". Bringing the deficit down would require "a period of weak economic activity and a lower currency".

In fact, the economic crisis is already severely impacting on the lives of ordinary people. Treasury's latest economic update, released December 18, warns that official unemployment, currently at 4.2 percent, will reach as much as 7.2 percent by 2010. Treasury's "downside" scenario predicts the economy to shrink for the next two years.

Economists widely agree that these forecasts are too optimistic, as they are based on data that are already out of date. Radio New Zealand's economics correspondent Nigel Stirling noted: "The forecasts for the world economy [on which Treasury based its domestic predictions] were completed on November 20. Since then, three of the world's four largest economies—the United States, Japan and China—have taken a significant turn for the worse."

In a sign of sharply reduced spending by households, consumption dropped by 0.2 percent in the September quarter. Despite this, and reports, such as that in the December 21 *Sunday Star-Times*, that retail sales had been "flat or falling for most of 2008", there were high hopes for a holiday boom in the sector. On December 20, the *New Zealand Herald*'s editors attempted to persuade readers that spending was their "social duty", absurdly declaring: "As consumers we hold the recession's cure in our hands".

Paymark, which monitors about 75 percent of all electronic payments across the country, reported that the amount of money spent at retail stores during December had fallen by some 0.5 percent up to December 22, compared to the corresponding period of 2007. Retail performance then appeared to turn around on Christmas Eve, and by December 28, the value of transactions was up by 2.6 percent on the previous year. The reversal produced ecstatic headlines: the *New Zealand Herald* declared "Retailers in the money," while the *Sunday Star-Times* ran, "Kiwis go wild in the aisles".

However, the supposed boom was illusory. Until 2008, Paymark's usual year-on-year rise had been 8 percent, due to higher debit card use, inflation and increasing consumption. Furthermore, the Christmas sales were fuelled by substantial discounting, with some stores advertising reductions as great as 70 percent. Paymark data on turnover volume—up 6 percent in the same period that saw a less than 3 percent increase in turnover value—indicates low profit margins for retailers.

Just before the sales period, an ANZ Bank survey indicated that 49 percent of retailers expected their businesses to perform badly in the year ahead. The figure was not only a record low but also 19 percent below the previous low, recorded in March 1991. Whatever confidence has been instilled by the late December "success" will find little support in 2009, as disposable income shrinks and credit becomes less available.

The housing market continues to deteriorate. A recent Lincoln University study revealed that 100,000 to 130,000, or up to one in five households, are now in negative equity (meaning that the value of their house is less than the amount owed on its mortgage). Lincoln University property studies professor Chris Eves told the *Sunday Star-Times* that with unemployment set to rise steeply, many of those in negative equity could be forced to sell their homes at a substantial loss. Real estate agent Peter Thompson told the *Dominion Post* last month that mortgagee sales are already up 25 to 35 percent compared with 2007.

In his *Herald* column on December 21, economist Bernard Hickey wrote: "The pain for home owners and property investors has only just begun and next year is set to be the worst year for house prices in New Zealand's history." He noted: "New Zealand house prices have tracked US house prices and the share prices of US home builders closely since 2001 with a lag of 16 and 28 months respectively." Hickey and a number of other commentators have tipped house prices to fall by a further 30 percent.

Already, more workers are being made redundant. On December 15, 228 workers lost their jobs as biscuit manufacturer Griffin's closed its 70-year-old Lower Hutt factory, consolidating its business in Auckland. In the finance sector, GE Money announced on December 17 that it would shut down its mortgage business, Wizard Home Loans, closing 25 branches and axing 80 jobs. GE Money Australia and New Zealand chief executive Mike Cutter blamed the move on "extreme volatility" in the mortgage market. In October, GE Money closed its New Zealand vehicle finance business, with the loss of another 80 jobs.

The number of poor and hungry people is increasing dramatically. On the weekend of December 20 and 21, for the first time since the Great Depression of the 1930s, people formed queues outside the Auckland City Mission. In the four weeks leading up to Christmas, the Mission gave out food to about 6,000 people—double the normal number for that time of year. Mission spokesperson Diane Robertson told Radio New Zealand that many of those asking for food had never done so before. The Salvation Army said it expected to help 20 percent more people over Christmas than it normally would.

Prime Minister John Key's newly-elected National Party government is moving to impose the full burden of the economic breakdown on the backs of working people. It has passed legislation to allow small businesses to sack employees at any time during a 90-day "probation period" without having to provide a pretext for doing so. The government has also cut the amount of money available for retrenched workers. During its election campaign the National Party said it would set aside a meagre $42 million a year for accommodation and welfare supplements, up to a total of $160 a week per worker, for those made redundant as a result of the recession. In a warning of what is in store in the period immediately ahead, the government has now reduced this fund to $52 million over a two-year period.