

Additional insights on the economic impacts of the COVID-19 pandemic

April 2020



Infometrics

Economics put simply

Authorship

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Overview

This report sets out additional insights on the economic impacts of the COVID-19 pandemic. It details Infometrics' latest economic forecasts and our key views around how the economy is likely to respond.

We also outline the expected effects on some of New Zealand's key industries, providing more detailed insights on key drivers of activity across the economy.

This report is designed to supplement our regional economic impact reports.

Infometrics Economic Outlook: Biggest hit to economy since the Great Depression

The latest Infometrics economic forecasts were published on Friday 17 April, reflecting data and insights up to 9 April 2020. Below is our Forecast Story, published on 17 April alongside the forecasts, which details the drivers of activity and our assessment of the economy.

COVID-19 presents the greatest economic shock in living memory, and although the full extent of the shock is still to play out, it is clear that the economy will be irrevocably changed by this pandemic. These times are highly uncertain, as we communicated in **Well, that escalated quickly!** The speed with which the economic outlook changed during March far exceeded anything we experienced during the Global Financial Crisis (GFC) during 2008/09, which itself felt particularly fast-moving at the time.

We are rewriting our economic manuals due to the overwhelming combination of body blows to the economy. We are currently forecasting a 13% contraction in economic activity between the December 2019 and June 2020 quarters, with most of the decline occurring in the June quarter due to the current lockdown. This contraction is set to be at least four times larger than anything we've seen in living memory, so there is understandably considerable scope for error in this estimate.

Our expectations for the economy are considerably more pessimistic than many other forecasters, with the real divergence among forecasts arising not in the extent of the short-term hit to the economy but, instead, about how quickly the economy recovers again. By March 2022, we expect quarterly Gross Domestic Product (GDP), a measure of the economy's output, to be still 6.6% below its December 2019 level. In comparison, the trading banks' forecasts for March 2022 range from BNZ's prediction of 7.0% smaller to Westpac's rosy outlook of 3.2% bigger. Forecasts of the unemployment rate¹ also capture this spread: we are picking a 9.4% unemployment rate in March 2022, compared with a range of 8.4% (BNZ) to 5.2% (Westpac) for the trading banks.

In short, we view the current repercussions for the economy to not only be significantly worse than others expect, but also to endure for longer as structural adjustments are forced on the economy. Our view is that the New Zealand economy is entering a **U-shaped downturn** (see Graph 1) rather than the more optimistic V-shaped recovery being picked by Westpac and, to a lesser extent, ANZ and ASB. Although the government has stepped in quickly to try and help businesses through the lockdown, the wage subsidy and other measures will not be enough to keep all businesses going. The tourism² and hospitality sectors will be particularly heavily affected by extended

¹ The unemployment rate is calculated as the number of unemployed people as a percentage of the labour force. The labour force is the total of employed and unemployed people. A person is defined as unemployed when they are not in work, but are available for and actively seeking work.

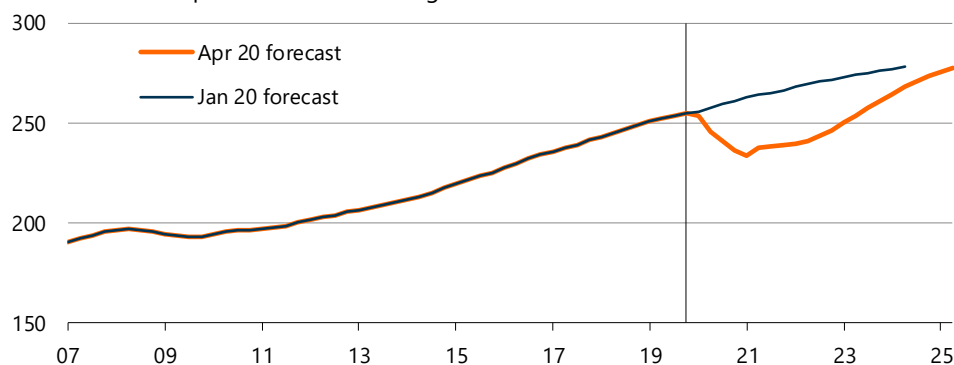
² Tourism is treated as a type of spending rather than an industry in its own right. Tourism spending is estimated by summing a proportion (%) of spending by tourists across the following industries: accommodation (70%), food and

border restrictions and will not recover to pre-pandemic levels within the foreseeable future. Many business failures are inevitable, and it will take time for the surplus labour and capital resulting from this downturn to be redeployed by other businesses.

Graph 1

This recovery will take time

GDP forecast comparison, annual running totals, 2009/10 \$b



Our key assumptions around the economy's outlook are as follows.

- We expect the Level 4 lockdown to be fully in place for only four weeks. However, significant restrictions (Level 3) are likely to remain across much of the country for another 3-4 weeks. Of course, there is considerable uncertainty about the scope and duration of extended or subsequent lockdowns, or post-lockdown restrictions.
- We expect some limitations on economic activity to remain in place over the following 6-9 months. At this stage, it is unclear exactly what or how stringent these restrictions might be. However, they are most likely to include borders that will be closed to non-New Zealanders for some time, easing back to a 14-day quarantine for foreign arrivals over time. While either of these measures are in place, they will prevent international tourist numbers from picking back up.
- We estimate that the economy is operating at about 65% of capacity during the Level 4 lockdown, based on our estimates that approximately 42% of output can continue to be generated by those people working from home and another 23% from essential services. Once the Level 4 lockdown has ended, our allowance for further significant restrictions is equivalent to Level 4 conditions remaining in place for a further fortnight.
- Further government support and stimulus for the economy will be forthcoming in coming months. Next month's 2020 Budget is likely to contain the biggest initiatives. However, we would expect other significant announcements at December's Half-Year Economic Update or the 2021 Budget, as the shape and magnitude of the required response from the government becomes clearer.

beverage services (41%), road, rail and water transport (9%), air and space transport (88%), other transport, transport support, and travel and tour services (21%), rental and hiring services (31%), arts and recreation services (17%), retail trade (15%), education and training (8%), all non-tourism related industries, imports sold directly to tourists to retailers (2%). Source: StatsNZ, Table 25, pg 51, Tourism Satellite Account: 2018

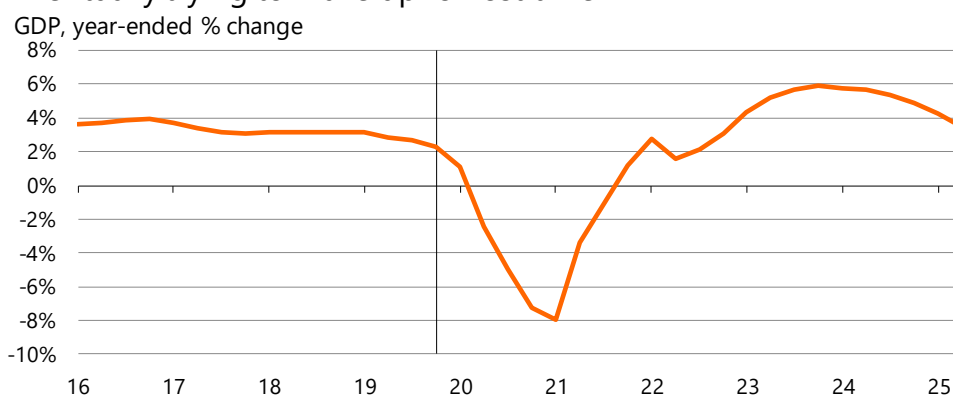
- The six-month mortgage holiday scheme arranged between the government and the trading banks will only delay an inevitable downturn in the housing market. We predict the number of forced sales will increase substantially once the scheme expires in September, particularly given our expectation that unemployment will continue rising until the second half of 2021. Downward pressure on property prices will be exacerbated by an overhang of newly constructed houses that were started prior to the pandemic, which developers will struggle to sell. We expect an 11% fall in house prices between June 2020 and December 2021.
- Businesses that have survived through the lockdown and are not directly affected by the collapse in tourism will remain under pressure throughout the following 12-18 months. A tighter rein on both business and household budgets will have a negative effect on demand conditions for many firms. Although the number of business failures is likely to be at its highest within the next 3-6 months, we expect to see a continuing stream of above-average insolvency numbers throughout 2021 as well.

Given these assumptions, we forecast that GDP growth will remain patchy until the first half of 2022. By that stage, COVID-19 is likely to have been controlled by a vaccine and overseas economies will be on the long road to recovery. International tourism will start to reappear and demand conditions for other exports will also improve, particularly those exports that are reliant on markets other than China. Government stimulus, in terms of both cash for households and spending on infrastructure, will also support accelerating economic growth. Businesses will become more confident about their own revenue prospects, leading to increased investment and hiring. Signs of a tightening labour market will also improve consumers' confidence and willingness to spend.

After an 8.0% contraction in the economy during the March 2021 year, we expect year-end growth to turn positive again by the end of 2021. There will be considerable underutilised resources in the economy that, in tandem with highly stimulatory fiscal policy, are likely to drive strong growth results in subsequent years. We forecast that GDP growth could get as high as 5.9%pa in 2023 (see Graph 2).

Graph 2

Eventually trying to make up for lost time



Over the three years to June 2025, we are predicting economic growth to average 4.8%pa. However, it is also worth noting that average growth between June 2019, before

the pandemic, and June 2025 will only be 1.6%pa. Even with rapid growth in the later years of our forecast period, we still predict the economy will be 1.8% smaller in 2025 than we were anticipating before COVID-19 came along.

Avoiding a repeat of the Great Depression

The current shock to the economy looks likely to be of a similar magnitude to the one experienced in the early 1930s at the start of the Great Depression, when the economy shrank by an estimated 12% between March 1930 and March 1933. One of the other defining features of the Great Depression was the length of the downturn – it was not until 1936 that the New Zealand economy recovered to be larger than it was in 1930. However, we see several important reasons to be optimistic that the current downturn can be arrested and reversed more quickly than the one that occurred 90 years ago. These factors include:

- the government's fiscal position
- a better understanding of the appropriate fiscal policy response to an economic downturn
- a broader and more generous welfare system
- the floating exchange rate
- the ability to independently set monetary policy
- New Zealand's export linkages to China.

Firstly, the government has entered the COVID-19 pandemic in a vastly superior financial position than its 1930s counterpart. Central government debt was equivalent to 160% of GDP in 1929, compared to gross debt of just 28% of GDP in 2019. Credit ratings agencies have previously indicated that the government could lift its net debt from its current level of 19% of GDP to about 50% of GDP during a crisis without any ratings downgrade.

Fiscal policymakers also have a much better understanding of the appropriate response to an economic shock than they did 90 years ago. The initial government reaction to the slump in activity in 1930 was to increase taxes and cut spending to try and maintain a balanced budget. Of course, such a response simply exacerbated the economic downturn. In contrast, the current government has taken firm action to try and reduce the magnitude of the downturn by borrowing to provide support for businesses in the near term. Further measures will undoubtedly be introduced by the government in coming weeks and months, with an aim to stimulate more activity once the worst of the COVID-19 pandemic has passed and the economy is able to recover.

Finally, regarding government policy, New Zealand has a much more comprehensive welfare system than existed in the 1930s. This safety net means that the consequences of unemployment are less disastrous for people than in previous generations. The current downturn will have a negative effect on job security and consumer confidence, with considerable flow-on effects into people's spending behaviour, but the hit to spending is likely to be less marked than in the 1930s. In addition, increased benefit payments by the government during the downturn are effectively an automatic fiscal stabiliser, helping to mitigate the worst of the economic downturn.

New Zealand's monetary policy framework is also considerably more conducive to supporting the economy than it was at the start of the Great Depression. At that time, New Zealand didn't have its own central bank or its own genuine currency and used a fixed exchange rate against the British pound. The initial brunt of the 1930 economic shock was borne by farmers, with the international economic downturn significantly negatively affecting demand for their products.

A depreciation in the exchange rate would have been an orthodox response, as it would have at least partly offset the drop in commodity prices that farmers experienced. However, at the time, a strong currency was viewed as a measure of sound economic management and financial prudence. It was not until early 1933, three years after the start of the downturn, that the government moved to formally devalue the New Zealand pound.

In contrast, the New Zealand dollar has fallen by as much as 17% this year against the US dollar. This drop is mitigating the negative effects of weaker global demand driving down international commodity prices and, potentially, export volumes. Of course, the decline in the New Zealand dollar is most pertinent for agriculture-related exports. The lower exchange rate is irrelevant for tourism operators, whose potential market will be close to zero as long as significant border restrictions remain in place.

Alongside the floating exchange rate, having our own central bank means we can also set interest rates independently. We have already seen the Reserve Bank slash the official cash rate by 75 basis points and undertake quantitative easing to bring down longer-term interest rates. These moves will only soften the downturn in the near-term, rather than stimulate growth. However, as demonstrated by the experience of the Great Depression, the alternative is incredibly unpalatable. Interest rates only edged down by about half a percentage point between 1929 and 1933, yet the CPI plunged 21% during this period. In other words, real interest rates were incredibly contractionary, and the real burden associated with massive levels of government and farm-related debt rose as prices fell (for both property and general goods and services).

One final factor that adds to our cautious optimism about the medium-term outlook is New Zealand's trade ties with China. China's strong action to bring COVID-19 under control is in stark contrast to the initial lack of decisive action across much of Europe and the US. As a result, we expect domestic demand within China to start returning towards normal much sooner than in many of the major developed economies.

We recognise that persistently weak demand conditions in Europe and the US will have negative implications for Chinese exports, manufacturing activity, and economic and income growth in China. Nevertheless, we believe that Chinese demand for food will remain relatively strong. Many of our dairy, meat, horticultural, and seafood exporters will still have well-functioning markets into which they can sell their products. Prices are likely to be softer given weak demand conditions around other parts of the globe, although as we have previously noted, this price effect is likely to be partly offset by a weaker New Zealand dollar.

The details of our forecast outlook

The remainder of our Forecast Story discusses our expectations for specific subcomponents of the New Zealand economy, and the key issues and risks we see for each of these variables.

Unemployment to threaten double digits

We are assuming that the COVID-19 pandemic will have massive consequences for the labour market. These effects will come through several channels and will result in a variety of different outcomes over an extended period.

Firstly, there will be job losses in industries that were being directly affected by COVID-19 before the lockdown occurred, such as tourism and hospitality. The government has signalled that New Zealand's borders are likely to remain largely shut until either a vaccine is available or until the risk of reimporting new cases of COVID-19 from overseas has diminished. But even if Europe and North America get their COVID-19 outbreaks under control sooner rather than later, issues for the tourism sector will remain. Airline capacity will be significantly below previous levels, people are likely to be cautious about long-haul travel, and the global economic downturn will limit tourism-related spending. In short, we could easily see employment³ declines of 25-40% in industries that are heavily reliant on tourism.

Secondly, there will be closures of firms that are not able to remain solvent throughout the lockdown. These businesses will typically be unable to generate revenue during this time, but will still face costs such as rent, wages, interest, or other fixed costs. The government has alleviated some of the pressure on firms with its wage subsidy scheme and business lending package. However, there will be many businesses that were only marginally financially viable before the pandemic, and their owners will choose to cut their losses by closing down. These firms could include many small businesses owned by baby boomers who are close to retirement, who will see little sense in pumping more money into their business to keep it afloat with limited future payoff.

The longer the lockdown continues, the greater the number of business failures is likely to be.

Even once the lockdown ends, the flow-on effects of these initial job losses and business failures will cause problems for other firms. Reduced levels of business investment and household spending will force less directly affected businesses to cut back staff hours or reduce employee numbers. Business and consumer confidence levels are likely to stay persistently low throughout 2020 and 2021, with job losses and business failures a continuing theme. A cascading effect of business closures is expected, with immediately unaffected firms facing lower activity levels over time as their customers stop trading.

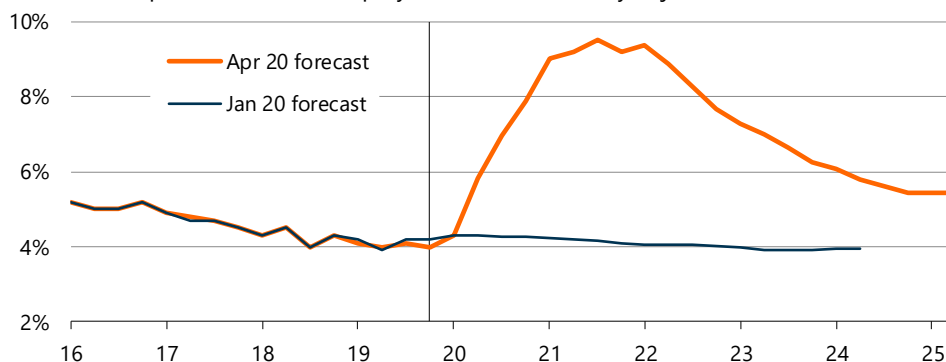
The labour market outcomes clearly show through in our forecasts. We are predicting a 12% fall in total employment between December 2019 and September 2021, including a 6.6% decline in the June 2020 quarter alone. The unemployment rate is forecast to climb from 4.0% to 9.5% by September next year (see Graph 3).

³ Includes both employees and the self-employed.

Graph 3

The labour market has a mountain to climb

Forecast comparison of the unemployment rate, seasonally adjusted



But even these stark numbers mask the full effect of the recession. Some workers will be forced to cut back their hours, reducing overtime or shifting from full-time to part-time work. In other words, underemployment or underutilisation of labour will rise in tandem with unemployment. Furthermore, some of those people who are no longer employed will not be counted as unemployed. Instead, some will simply drop out of the labour force as new jobs become too difficult to find, while others will seek out education opportunities to enable them to reskill. Both subgroups will contribute to a fall in the participation rate, which we predict could fall from 71% to 66%, its lowest level since 2001.

We anticipate that the rise in unemployment could take time to filter through into the economy as a result of the government's wage subsidy. Some firms that would otherwise have laid off staff will struggle through in the near term, with wage costs being largely borne by taxpayers. However, once the wage subsidy ends, further job losses will occur, with firms that are no longer viable operations becoming exposed by the lack of continued government support.

We see the risks to our labour market forecasts as balanced. Over the next two years, we might have overestimated the scale of likely business failures and job losses, which would suggest that the peak rate of unemployment could be lower than 9.5%. However, there is also a chance that an unemployment rate of close to 10% could take longer to recover from than we have allowed for, as people struggle to retrain or find new job opportunities. These sorts of structural issues could result in unemployment still being above our projection of 5.4% by the end of our forecast period in 2025.

Household caution set to stay

Consumer confidence was abruptly lower in March, but there will still be further significant drops to come as the effects of the lockdown on businesses become clearer and job losses mount. Household spending activity will fall sharply in the June quarter, primarily because consumers are unable to spend on many of the goods and services they would regularly purchase. We have allowed for a quarterly drop of almost 9%.

Spending will bounce back from this negative supply shock in the September quarter, but the extent of this rebound will be limited by the job losses and reduced incomes that have transpired in the meantime. And with unemployment continuing to climb until

a forecast peak of 9.5% in September 2021, a full recovery in household spending will take some time to occur.

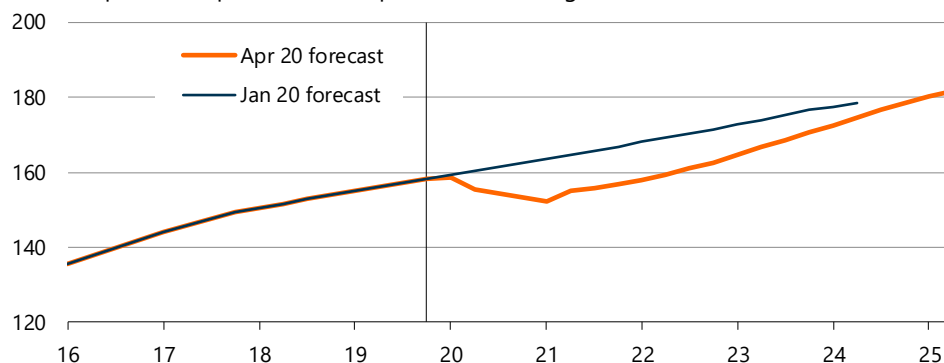
Discretionary spending will bear the brunt of more frugal household spending as consumers watch costs much more closely. Outside of food, housing costs, and other necessary goods and services, a humbler spending profile is likely to emerge. Even for those households who don't see hours cut or jobs lost, the severe downturn and threat of rising unemployment will see them conserve more of what they earn to provide a buffer if the worst occurs.

By mid-2022, we expect total household spending to be back at its pre-crisis levels, although there will still be ground to make up for the lost growth since early 2020 (see Graph 4). We expect spending growth to average 4.5%pa over the three years to June 2025 as the labour market tightens, household incomes recover, and population growth picks up.

Graph 4

Cutting back on discretionary spending

Fcst. comparison of private consumption, ann. running totals, 2009/10 \$b



We see two key risks to our spending forecasts. Firstly, in the near-term, the negative shock to household spending could be greater than we have allowed for – both in the June quarter, but also in the following year as unemployment rises. Secondly, from 2021 onwards, there is potential for additional government stimulus to boost household spending, via measures such as tax rebates or additional social welfare payments beyond what we have currently allowed for, to boost household spending. Any larger-than-expected government action to expedite the recovery in consumption during 2021 and 2022 would reduce the scope for such fast growth in spending later in the forecast period.

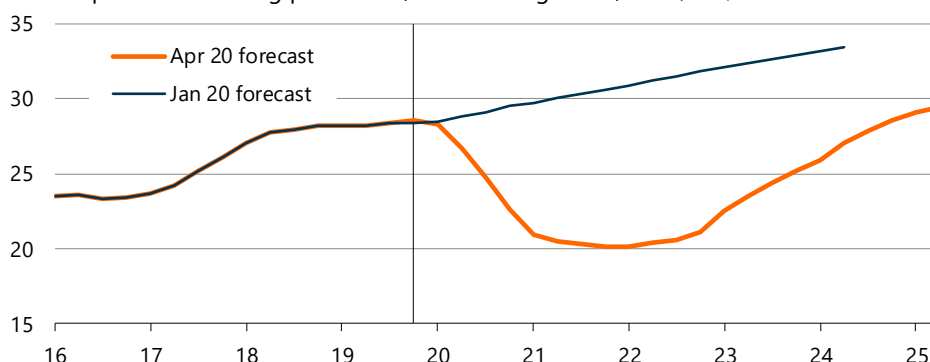
Cutting unnecessary business spending to preserve cashflow

With firms under severe cashflow pressure in the near-term, and business confidence likely to hit record lows, business investment will plunge over the coming year. We are predicting a 26% reduction in spending over the year to March 2021, surpassing the 24% decline that occurred in 2009. Smaller falls are likely to continue throughout most of 2021, as the flow-on effects of the COVID-19 lockdown and the collapse in tourism and hospitality activity keep weighing on demand conditions, business activity, and confidence levels (see Graph 5).

Graph 5

A huge hole in business investment

Fcst. comp. of non-building private inv., ann. running totals, 2009/10 \$b



We expect a recovery in business investment by late 2022, with growth holding in double digits during 2023 and 2024. This pick-up will be underpinned by improving demand conditions both domestically and internationally. It will also signify a reallocation of resources within the New Zealand economy away from businesses and industries that have suffered during the pandemic. New firms will be able to take advantage of stimulatory monetary and fiscal conditions to target new areas for growth. Demand for capital equipment by these businesses will be matched by their demand for workers, so the pick-up in investment spending is likely to coincide with the early stages of the labour market recovery.

Our projected decline in business investment over the next 1-2 years is not much larger than the one that occurred following the GFC, so the near-term risks to our forecast are on the downside. We have allowed for a relatively long trough in investment activity, and we see some scope for spending to pick up sooner if fiscal policies are successful in stimulating domestic demand and boosting confidence earlier during 2021.

A hit to trade, both in and out

New Zealand's tourism exports totalled \$16.2b during 2019, representing about 19% of total goods and services exports. As outlined above, we expect international inbound tourism is likely to be virtually non-existent for the next 12 months, with 14-day quarantine requirements or closed borders likely to discourage or prevent visitors from coming here. As a result, we are forecasting a 20% contraction in export volumes over the year to March 2021.

Most of our commodity exports will be less heavily affected, notwithstanding a decline in trade volumes with China in early 2020 as their ports were largely shut down. The biggest exception will be forestry, with backlogs at ports and softer demand due to the global economic downturn expected to cement weaker export volumes. Non-food manufactured exports are also likely to temporarily dip thanks to a hiatus in production during the lockdown.

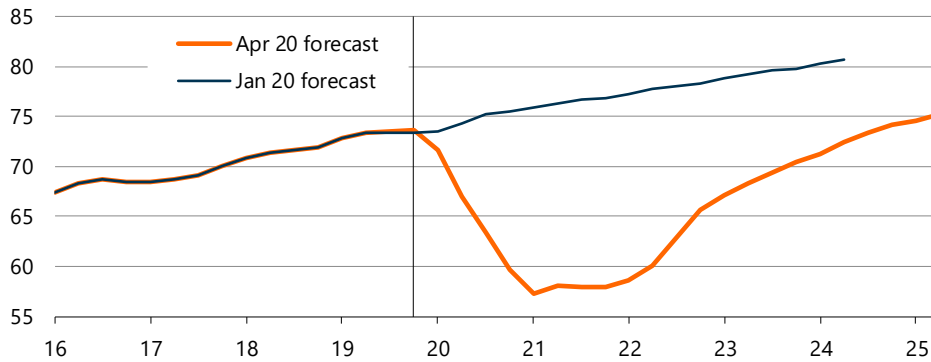
Although we are forecasting growth of up to 15%pa in export volumes during 2022 and 2023, we still expect volumes by mid-2025 to be about 9% below the levels they would have otherwise reached (see Graph 6). This result will be due to the lingering effects of the pandemic on international tourism, with reduced willingness to travel and less

capacity in the airline industry. With overseas economies set to shrink this year, the current global downturn will also have a dampening effect on international demand and lead to softer export volumes, even over the medium-term.

Graph 6

Tourism's loss a big hit to exports

Forecast comparison of export volumes, ann. running totals, 2009/10 \$b



Travel of New Zealanders overseas will be similarly affected to inbound tourism: non-existent for the next 6-12 months, followed by a gradual return towards “normal” as borders are reopened, quarantine restrictions are lifted, airline capacity is rebuilt, and lingering traveller concerns about COVID-19 fade.

Tourism imports are much smaller than exports, totalling \$6.7b over the last year, and representing 7.8% of total goods and services imports. Consequently, the direct effect of COVID-19 on imports will be smaller. These figures also demonstrate that increased spending on domestic holidays by Kiwis will be unable to fully make up for the decline in revenue due to the loss of foreign tourists.

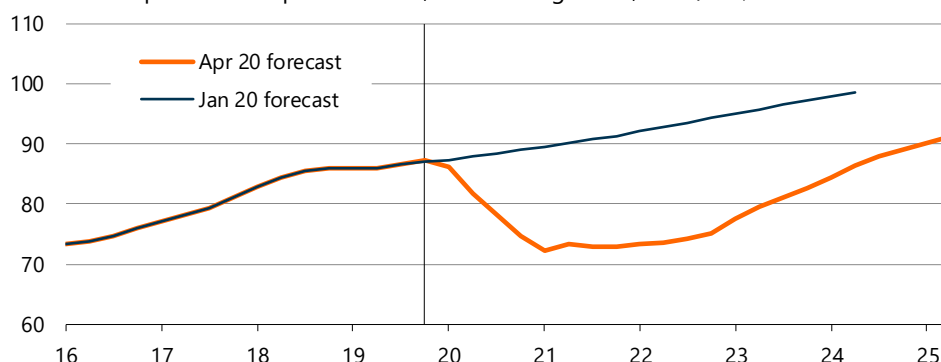
Alongside changing travel patterns, the downturn in New Zealand’s domestic economy will also weigh on import volumes. Lower household spending will reduce demand for consumption good imports (21% of total imports). Capital equipment imports are also likely to take a big hit (15% of total imports). In the wake of the GFC, the annual total of capital imports plunged 33% over an 18-month period. Given our anticipated decline in business investment spending, we are likely to see an even sharper fall in capital imports than we did during 2009.

We are forecasting a 16% contraction in total import volumes over the year to March 2021. We anticipate that the subsequent recovery in imports during 2022 and 2023 (see Graph 7) could be more muted than export growth for two reasons. Firstly, we expect a sustained change in New Zealanders travel patterns, with more holidays taken domestically and international travel taking a long time to return towards pre-pandemic levels. Secondly, business’ willingness to invest could remain weaker than normal for some time, dampening the recovery in capital imports.

Graph 7

Imports are pulled lower as well

Forecast comparison of import volumes, ann. running totals, 2009/10 \$b



The risks to our forecasts for both exports and imports lie, if anything, on the upside, particularly over the medium term. Given that we are currently in the midst of the pandemic, it is unclear how sustained an effect current events will have on international travel behaviour.

Government to the rescue

Fiscal policy has the biggest role to play in cushioning the economy's downturn and then generating momentum heading into the recovery. In broad terms, this support and stimulus can happen via three channels.

- Increased government spending on purchasing goods and services (government consumption)
- Transfers of money to individuals or businesses (which shows up in private consumption or business investment)
- Increased government spending on assets such as infrastructure (government investment)

Notwithstanding the fact that the overall size of government would normally be expected to expand more quickly under a Labour administration than under National, we don't anticipate any step change in government consumption. The most obvious area of potential increase in spending is the health sector, where more funding will obviously be needed in the short term to facilitate the response to the COVID-19 pandemic.

The government's wage subsidy package and welfare benefit increases come within the transfers category, increasing the government's outlays, but with the money not being used to purchase goods or services. Similarly, any future tax cuts, rebates, or handouts of money to households will also come within this category. This money does not show up in government consumption, but it will affect the government's financial position and results in a larger fiscal deficit in coming years.

The government's current focus is, rightly, on trying to reduce the financial stress on households and businesses caused by the initial economic shock of the lockdown – in other words, smoothing the downturn path. Limiting business insolvencies or failures will

make it easier for the economy to recover once trading conditions start returning to normal.

Once the worst of the shock is over, then the government's efforts must turn to measures that will help rekindle aggregate demand and stimulate a pick-up in growth. We expect these measures to concentrate on shoring up households' financial positions, which will be negatively affected in the meantime by job losses, other temporary reductions in income, and hits to wealth caused by falling house prices, KiwiSaver balances, and other investor losses.

The government should also consider measures that encourage businesses to commit to new investment and hiring. Stimulus measures for households and businesses will need to kick in during 2021, although it could be 2022 before we start to see the real fruits in terms of better economic outcomes.

Finance Minister Grant Robertson has also emphasised the potential role that infrastructure has to play in the recovery. We understand the government is looking for a wide range of infrastructure projects that it can fund over coming quarters to boost economic activity, including projects that would normally be funded by local government or the private sector. The focus is on "shovel-ready" projects, with particular attention being paid to smaller projects, so that work can be undertaken across a wide range of areas to try and generate a reasonably broad-based recovery.

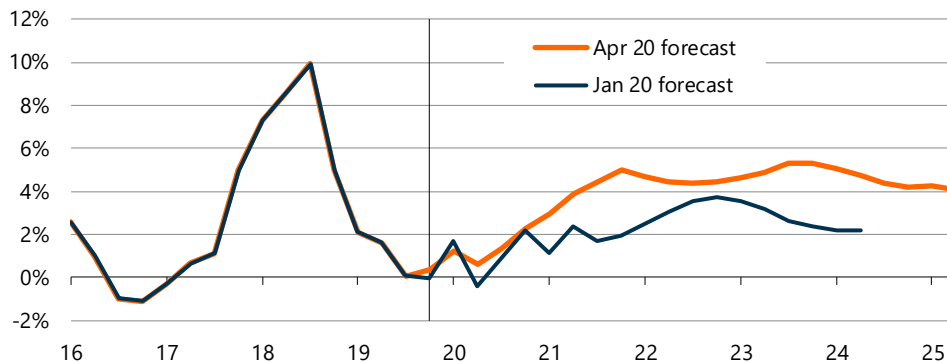
This spending by central government shapes as a timely injection of cash for local councils that have been struggling to fund their required infrastructure investment. Central government money will help expand network infrastructure to meet the strong population growth of recent years, as well as replace critical network assets that have reached the end of their working life.

In the short-term, government investment will be constrained by the hiatus in projects caused by the lockdown. We predict that growth in spending will then accelerate towards 5%pa during 2021, with growth averaging 4.5%pa over the four years to June 2025. By the end of the forecast period, we expect the volume of government investment to be almost 10% greater than we had allowed for in our January forecasts.

Graph 8

Investing for growth

Forecast comparison of government investment, year-end % changes



Evolving our forecasts as decisions play out

We will continue to track the COVID-19 pandemic and response throughout the next few months, providing our views as circumstances change and decisions are made by key local, national, and international leaders.

For New Zealand, understanding when the lockdown will end, and how businesses can operate under lower COVID-19 alert levels, will provide greater clarity about the economy's near-term direction.

Internationally, developments in both the health and economic responses to COVID-19 will allow us to better determine the global growth path and how it will affect New Zealand.

Our regular weekly commentaries and economic data release notes to clients will provide our most up-to-date views on how the economy is continuing to evolve.

COVID-19 effects by broad industry

This section outlines the expected economic effects of the COVID-19 pandemic and response on some of New Zealand's key industries.

Accommodation and food services

Accommodation and food services will be arguably the most heavily affected part of the economy by the COVID-19 pandemic and its aftermath. The disappearance of international tourism and declines in domestic tourism and other discretionary spending are key factors in the industry's contraction. Activity will continue to be severely constrained under COVID Alert Level 3, while post-Level 3, domestic travel will remain restricted because of general economic conditions.

Retail and wholesale trade

Retail and wholesale trade has experienced a significant drop in demand under Level 4, and restrictions will remain in place under Level 3 as well. These effects are not being felt equally, with supermarkets enjoying periods of higher-than-usual demand. Other businesses that can sell online will be able to operate under Level 3, although we do not expect spending patterns during this period to be normal. The declines in tourism activity and other discretionary spending will also be felt disproportionately by retailers selling more luxury or higher-end products.

Transport, postal, and warehousing

Transport, postal, and warehousing has been significantly affected by the pandemic. The largest effects are on air transport and scenic and sightseeing transport due to the downturn in tourism activity. As is the case for accommodation and food services, these effects will continue long after the lockdown ends. Other parts of the transport and logistics industry have been weakened by factors such as reduced commuter travel and cutbacks in distribution and freight requirements caused by the lockdown. Some of these effects will start to reverse out with a pick-up in online spending outside Level 4, but this positive influence on activity is likely to be outweighed by the reduction in overall spending caused by the weaker labour market and incomes.

Arts and recreation services

Arts and recreation services are suffering the twin effects of a reduction in discretionary spending, including spending by tourists, and restraints on what services and products can actually be offered to consumers. Performing arts, professional and community sports, horse racing, casinos, and other entertainment and events will continue to be constrained at Alert Levels 2 and 3, with restrictions on gathering numbers at both indoor and outdoor events. Ongoing border restrictions are also set to disrupt the ability of promoters to run events where they are reliant on entertainers or sportspeople coming into New Zealand from overseas.

Construction

Construction activity was close to peaking even before the COVID-19 pandemic occurred. Rising unemployment, falling house prices, slower population growth, and tighter bank lending conditions will all weigh on activity over the next 1-2 years across both the residential and non-residential subindustries. Prospects for infrastructure look more promising given the government's desire to use this channel to try and stimulate the economy's recovery. We also note that strong growth in the population and building stock over recent years has increased the baseline level of maintenance work that needs to be done, mitigating the downturn for those parts of the industry that tend to be less cyclical.

Professional, scientific, and technical services

Professional, scientific, and technical services is the fourth-largest industry by employment in the New Zealand economy. So despite the industry being less directly affected by COVID-19 than many other industries, the forecast drop in job numbers is still large. Cost-cutting by firms and a reduction in business numbers across the economy will negatively influence demand for services within this industry across the board. Areas that are likely to be most heavily affected include those subindustries that are closely linked with construction activity.

Non-food manufacturing

Non-food manufacturing tends to be less labour-intensive than many other industries, but the downturn in the global economy will have a significant negative effect on demand for the industry. Manufactured exports are expected to be squeezed by weak demand conditions across much of Europe, North America, and Australia. The Global Financial Crisis also demonstrated the strong links between parts of non-food manufacturing and building work within New Zealand. Consequently, the forecast downturn in construction activity will also contribute to a decline in employment and output in this industry.

Administrative and support services

Administrative and support services are expected to mirror broader economic trends in business activity, with cost cutting, business failures, and the weak labour market negatively affecting this industry. Given the downturn in tourism, travel agents will be by far the most heavily hit, with modest declines in employment across other parts of the industry.

Information media and telecommunications

Information media and telecommunications activity will also come under pressure, despite the short-term boost to selected businesses from the increase in remote working that has taken place. Traditional media such as newspapers and magazines were already under significant pressure prior to COVID-19. Substantial drops in advertising revenue have exacerbated this situation and will lead to job losses, despite

government support. Significant job losses in areas such as libraries, movie theatres, and some parts of telecommunications are also possible.

Financial and insurance services

Financial and insurance services will be squeezed by the downturn in economic activity. Lockdown conditions are likely to have increased the amount of work being done electronically across parts of this industry, and this shift could potentially hasten the trend towards reduced job numbers for some occupations. More difficult business and financial market conditions could also negatively affect the viability of some firms in this industry. However, we note that the overall strength and robustness of the financial system is much better than it was between 2006 and 2010 when the industry grappled with the finance company collapses and the Global Financial Crisis.