



Aug
2020



David Norman – Chief Economist
david.norman@aucklandcouncil.govt.nz
021 516 103

Here we go again: Covid-19 Wave Two

- Auckland's ongoing solid economic performance and resurgent housing market and retail trade were interrupted by the first wave of Covid-19 infections and lockdowns.
- Despite thousands of job losses, the economic hit to Auckland and New Zealand from Wave One was smaller than many anticipated.
- But Wave Two is upon us, with more jobs lost as we move through another lockdown in Auckland.
- In addition to the wage subsidy, Auckland will need more support more in line with its share of the New Zealand population and tax take to bounce back from this further blow.

Those halcyon days

Just six months ago Auckland had an unemployment rate of 4%, GDP growth in the mid-2%^s, and nominal retail trade growth in the mid-4%^s. Even business confidence, divorced from reality for so long, began to turn up.

House prices were surging after three years going nowhere – bad news for those looking to buy, but a strong indicator of economic confidence.

But then...

A global pandemic ultimately led to bans on foreign arrivals. Attempts to get everyone arriving to self-isolate soon proved wishful thinking, and a stricter managed isolation/quarantine programme was put in place for New Zealanders. Arrivals through Auckland airport fell more than 95% in three months.



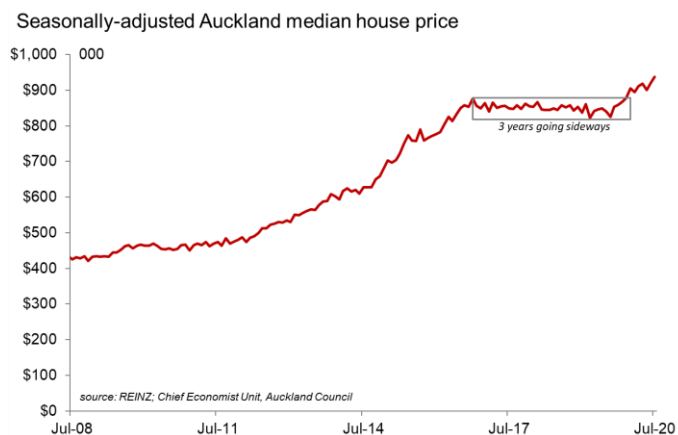
At Level 4 lockdown, an estimated 40-48% of work could not be done, and 33-40% of economic activity could not be generated. That was followed by more than two weeks at Level 3 (estimated 20% reduction in economic activity) and almost four weeks of Level 2 (estimated 10% reduction in economic activity).

Auckland lost more than 20,000 jobs. The unemployment rate probably rose closer to 6% than to the official estimate, which fell in June. Wage subsidies stood between workers and an even more precipitous plunge in employment. With wage subsidies set to come off in September – the right decision although one that would be tough for many – unemployment was set to nudge higher.

Less bad than we thought

Yet the Auckland and New Zealand economies stunned all comers with their resilience. The impact on livelihoods was real, but practically every economic indicator since late May was better than anticipated:

- Growth in jobseekers slowed sharply at Level 2.
- GDP fell much less than we anticipated in the March quarter, where a third of economic activity was not possible for a week.
- House prices hit a new seasonally-adjusted peak in June and then July and volumes returned to normal levels.
- Retail trade bounced strongly.
- Air New Zealand and then JetStar added domestic capacity much faster than they themselves appeared to anticipate (where else was anyone who still had a job going to go on holiday?).
- Resource and building consent applications returned to normal levels months ahead of expectations.
- Business confidence improved while remaining at weak levels.



Our own estimates of unemployment, which we initially thought could rise above 10%, had to be revised down sharply. We were anticipating a peak of 7% before Wave Two, still much worse than before the pandemic, but a lot better than we'd expected.

Here we go again

And then, in a flash, Auckland was back in Level 3 for an expected 18 days. There were some lessons learned in Wave One that will help:

- The share of people who can work at each level is higher than we at first feared, but hundreds of thousands still can't.
- Many organisations had weak IT systems or continuity plans; they've had months to get these into shape.
- The impacts of lockdown can be unpredictable –the timing of the rise in unemployment is not all directly tied to the period of lockdown, and the bounce back can be faster than we thought.

Still, from Day One of the new lockdown, people will have lost jobs. Businesses would have considered the prospect of another drawn out event and some will have decided to close. We estimate that during Wave One, level 3 cost around 250 jobs a day, with more to go once the wage subsidies end.

We estimate around \$60-\$75 million in GDP is lost each day that we are in Level 3. And each day in lockdown means that when we do open up, we do so from a lower level – with higher unemployment and lower GDP as a starting point. This affects the overall resilience of the economy as, in blunt terms, there are fewer employed people to buy things that create other jobs, and fewer businesses to employ new people.

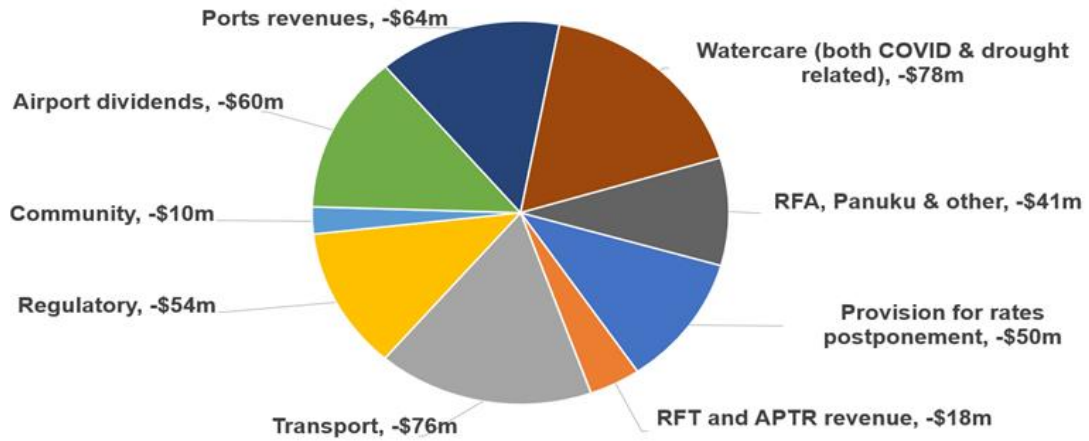
How the waves affect Auckland Council

When a business takes a hit like a seven-week lockdown as we saw in Wave One (Levels 4 and 3), their options are to eat into financial reserves if any, draw on government support if any (e.g. wage subsidies) and if they still can't make ends meet, they will try and wind up the business, devastating as it would be for that business owner and employees.

Governments, central and local, can't do that. Auckland Council still has to ensure rubbish is collected, resource and building consents are processed, water quality is monitored, civil defence services are in place, central government national policy statements are complied with, roads are useable, and that public transport is provided for essential workers under Levels 4 and 3 to get to work.

All this while revenues plummet through loss of the airport dividend; regional facilities, pools and other revenue-generating facilities being closed; and a reduction in building consent and inspection revenue, for example. Our most recent estimates are that Wave One led to a \$450 million loss in revenue.

Final cash revenue shortfall for the group in 2020/2021 is \$450 million against pre-COVID budgets



This revenue shortfall means that if we are to keep meeting operational needs of parks, rubbish collection, building inspections and a hundred other services, we can't spend as much on much-needed infrastructure as we had initially planned. And even at Level 2, more cleaning and distancing requirements add costs.

Wave Two makes these impacts even harder – more lost revenue, and less money available for much-needed infrastructure.

Auckland will need help

The extension to the wage subsidy, while national, will be skewed toward Auckland where most of the new restrictions have been imposed and thus business revenue losses will be largest.

But Auckland has been hit hardest by this unseen enemy through no fault of its own. Just as Aucklanders and other New Zealanders rallied to support Canterbury in the midst of its tragic earthquake experience, providing \$40 billion in government support, now Auckland will need more help from central government if it is going to keep delivering much-needed infrastructure and support employment recovery in Auckland.

For context, Auckland has 34% of Auckland's population, generating around 38% of GDP and 40% of tax revenue. At this stage, the scale of additional help will be nowhere near what Canterbury needed, but it stands to reason that Auckland will need a share of funding for genuinely-shovel ready and other projects broadly in proportion to our size and contribution to New Zealand to help the region bounce back.

Auckland Economic Commentary

Shyamal Maharaj

Economist, Chief Economist Unit

- Auckland is nearly 40% of the national economy and with Auckland in level 3, the implications for New Zealand are large.
- We have learned that the labour market is not just the unemployment rate. Other measures show us the realities of the labour market and how it has fared under lockdown.
- People are crowding malls, spending on new TVs, but is this going to last?
- House prices seem to keep defying the odds, but are they actually?

After more than three months of being COVID-19 free, Wave Two struck New Zealand's largest city. Auckland went into level 3 lockdown to curb the spread of community transmission. Wave Two brings with it the prospect of more job losses for Auckland.

Auckland may not be a fan favourite for the rest of New Zealand, but the facts speak for themselves. Auckland is home to 34% of the country's population, and roughly 40% of the tax take and GDP. It goes without saying that Auckland's lockdown will reverberate across the national economy. This will also signal the policy responses needed to alleviate mounting pressures pre-lockdown such as a shortfall in housing and infrastructure.

Unemployment

The official unemployment rate for Auckland fell to 4.0% (seasonally adjusted) in the June 2020 quarter, despite all forecasts suggesting a rise was to come. But the unemployment rate is just one measure of the labour force. And importantly, what gets reported as unemployment can be limited by technical definitions.

Notwithstanding the suspicious headline figure, looking under the hood reveals a less rosy picture. The underutilisation rate rose to 10.7% from 9.9% from the same time last year (people were generally working less than usual) which aligns more with the realities we have seen. Underutilisation shows that people who could work under 'normal circumstances' were unable to.

Additionally, hours worked fell 10% nationally and the country's labour force participation rate fell to 69.7 (the lowest since 2016). The complexities of lockdown mean that the June numbers require careful interpretation.

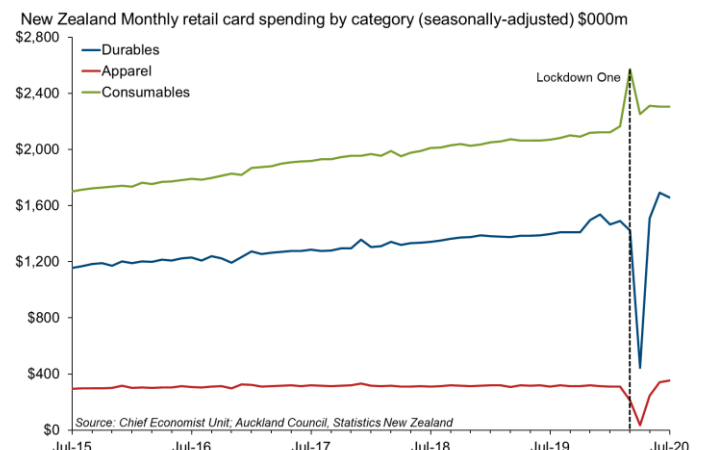
Regardless, job losses don't appear to be as bad as originally anticipated, in large part buffered by the wage subsidy scheme.

But Wave Two will lead to higher unemployment as businesses were already struggling to get ahead of Wave One. The extension of the wage subsidy may reduce the immediate blowback on employers, but the labour market is expected to certainly worsen.

Retail

The retail sector has arguably been hit the hardest, as we have seen discretionary spending from people ease significantly. Retail spending for Auckland fell 13.3% from the same time last year. Although this was very close to market expectations, what we can expect to see as Wave Two impacts are revealed in the data is a slower resurgence. Retailers have been hard hit since they rely heavily on the discretionary buying of clothing, café made coffees, three-course meals and cocktails.

Wave Two is likely to increase the risk to discretionary spending, especially for those facing uncertain job prospects. After Wave One, we observed people buying up a storm, crowding malls and spending heavily on durables like computers, TVs/sofas, and beds. Some argue this was due to pent up demand, but after the first few weeks in level 1 (really strong growth), the question remains how much pent up demand there still really is.



Perhaps with spending more time at home, people prioritised upgrading their beds and/or computers. People also generally spend more as house prices rise, which has been the case.

House prices

The Auckland median house price is defying all odds, retaining its strength. Prices in July set a new record in seasonally-adjusted terms. Interestingly, the number of homes sold in July was up an incredible 30% from July 2019, and 23% compared to June 2019. The recent strength means we have revised our price expectations. We still expect them to come off their highs, but by less than 5% as wage subsidies end and mortgage holidays wrap up, now extended to March 2021.

But is this a true reflection of the market, or is cheap money keeping the property market afloat? Some might argue this is mostly supported by expectations of mortgage rates remaining low for a long time. Another view is that people are confident in the long-term outlook and buying a house is a strong indicator of that.

But housing affordability has worsened despite historically low mortgage rates and as median incomes have fallen as a result of the pandemic and prices have surged. There is a strong chance that prices will continue to remain firmer than expected against the current economic backdrop.

Data summary provided by [Ross Wilson](#) - Analyst, RIMU

Note this data does not reflect the economic impact of the second round of lockdown.

Indicator	Jun-20 quarter	Mar-20 quarter	Jun-19 quarter	5-year average	Rest of New Zealand Jun-20 quarter
Employment indicators					
Annual employment growth (%pa)	-0.1%	1.0%	2.1%	2.6%	1.8%
Unemployment rate (%)	4.0%	4.8%	4.2%	4.6%	3.9%
Unemployment rate among 20 to 24 year olds (%)	8.5%	11.1%	7.3%	9.2%	8.0%
Unemployment rate among 15 to 19 year olds (%)	13.5%	16.6%	16.1%	19.8%	14.0%
Earning and affordability indicators					
Annual nominal wage growth (%pa)	-1.1%	3.1%	4.3%	1.9%	0.4%
Annual geometric mean rent growth (%pa)*	1.3%	2.7%	3.1%	2.9%	2.8%
Geometric mean rent to median household income ratio (%)*	27.4%	26.6%	26.8%	27.6%	25.0%
Annual median house price growth (%pa)*	9.2%	10.5%	0.0%	3.8%	9.2%
Mortgage serviceability ratio (relative to Dec-06)*	10.9%	15.1%	6.8%	0.0%	24.8%
Construction					
Annual new residential building consents growth (%pa)	5.3%	7.6%	13.4%	12.2%	9.9%
Annual m2 non-residential building consent growth (%pa)	-42.8%	-22.5%	19.0%	-0.2%	0.9%
International connections					
Annual Auckland Airport passenger movements (%pa)	-26.3%	-4.1%	3.0%	-1.0%	NA
Confidence					
Annual retail sales growth (%pa)	0.4%	4.6%	4.0%	4.9%	-1.6%
Quarterly Survey of Business Opinion (net optimists)	-59.0%	-66.3%	-34.5%	-10.5%	-65.4%
Westpac Consumer Confidence*	96.0	105.9	102.0	109.1	97.2

Sources: Chief Economist Unit, Auckland Council; Statistics New Zealand; Ministry of Business Innovation and Employment; Real Estate Institute of New Zealand; New Zealand Institute of Economic Research; Westpac; Reserve Bank of New Zealand. * Rest of New Zealand figures are for all of New Zealand including Auckland. Data is not seasonally-adjusted.

Disclaimer

This newsletter provides general information on economic issues in Auckland, and is not intended to be used as a basis for any particular course of action or as substitute for financial advice. The views and opinions expressed are those of the relevant author, and do not necessarily reflect the views of Auckland Council. Auckland Council disclaims all liability in connection with any action that may be taken in reliance of this newsletter, and for any error, deficiency, flaw or omission contained in it.

Find out more: visit the [Auckland Council Chief Economist Page](#) or contact us chief.economist@aucklandcouncil.govt.nz