SIX MONTHLY REVIEW

INTRODUCTION

The recovery experienced in the economy during 1981, was primarily based on an expansion in domestic spending and stockbuilding as compared to earlier growth phases which were generally export-led. Towards the end of 1981 the recovery showed signs of weakening. Domestic activity has continued to level off over the first six months of 1982. Recent indicators suggest that the economy is entering a contractionary phase which is expected to continue for at least the remainder of 1982/83.

Factors which have contributed to the slow-down in activity currently being experienced include: a deteriorating balance of payments situation due to poor growth in export prices and volumes combined with a large increase in import volumes (mainly in response to the buoyant state of the economy during 1981); and the contraction of real personal disposable income because of the effect of the high rate of inflation on fiscal drag coupled with the wage freeze. A further deterioration in the employment situation is expected to accompany the slow-down in economic activity.

The buoyancy experienced in the real economy during 1981 was associated with a rapid expansion in the monetary and credit aggregates. More recently their rate of expansion has slowed significantly.

Although dropping slightly (to 16.6 per cent) in the year to September 1982, New Zealand's rate of inflation continues to diverge from that of our major trading partners. In the year to June 1982 the average rate of inflation reported for OECD countries had fallen to 8.6 per cent, while there was a 17 per cent increase in New Zealand's Consumers' Price Index (CPI) over this period. In response to the increased disparity the Government announced a wage and price freeze on 22 June 1982, effective for twelve months. Also included in the measures were an Interest on Deposits Order (IOD) and the discontinuation of the crawling peg exchange rate scheme introduced in 1979. It was replaced by a system in which, apart from technical adjustments, a fixed exchange rate relative to the basket of currencies of our main trading partners will be maintained.

The IOD regulations were imposed to directly control deposit interest rates. These rates had continued to increase despite the November 1981 Financial Services Regulations. Upward pressure on deposit rates arose as a consequence of competition for funds in an environment with high lending to deposit growth rates for most financial institutions, declining rates of growth of the monetary aggregates, and the withdrawal of funds from the private sector institutions through the sale of Inflation Adjusted Savings Bonds.

The growth rates of the main money and credit aggregates have declined sharply over recent months particularly in seasonally adjusted terms. The main factor causing the decline has been the contraction of the money base arising from the deteriorating current account deficit. The slower growth rates of the monetary aggregates can be expected to contribute to the slow-down in inflation expected to occur over the next nine months.

The Budget presented on 5 August 1982 contained few measures that will stimulate the economy significantly. The main one was the short-run boost to real personal disposable income provided by the tax scale changes effective from 1 October. The adjustments to the tax scales are unlikely to be sufficient to maintain a level of demand similar to that which drove the expansion experienced during 1981.

CONSUMPTION

The volume of retail turnover increased by 3.6 per cent in the year ended June 1982 compared with the previous June year. Most of this growth occurred in the first three quarters of the year as indicated by annual rates of increase (quarter over quarter) of 5.6, 4.3 and 3.5 per cent respectively for the September, December and March quarters, while for the June quarter the annual rate of increase was only 1.1 per cent. In seasonally adjusted terms turnover fell by 2.8 per cent in May 1982 from a month earlier, and while it recovered somewhat in June, increasing by 1.9 per cent over May, this was to some extent attributable to the expectation of indirect tax changes being announced in this year's Budget. It is felt that these statistics indicate the start of the expected decline in consumer expenditure brought about by the erosion of real disposable incomes.

The reduction in new car registrations which has occurred in July and August further attest to the general slow-down in consumer spending currently underway. Registrations in July and August decreased by 15.2 and 13.8 per cent, respectively, over their respective months in 1981. Apart from a small decline in March 1982 these are the first two months in which the annual running total of new registrations has decreased since November 1980. New registrations had been particularly high during the 1982 June year, with the total number of registrations over this period being 95,929 compared with 85,298 for the previous year.

Growth in hire-purchase finance in the 1982 June year in part supported the growth in consumption over this period. Total goods bought on hire-purchase in the year ended June 1982 amounted to $776.6 million, an increase of 24.1 per cent over the previous year.

Oil company petroleum deliveries can be used as a proxy for petrol consumption. In the March 1982 year total deliveries decreased by 5.9 per cent over a year earlier. Total deliveries have declined each March year since the 5.5 per cent increase in 1976/77. The decrease in 1981/82 is the largest over this period. This is somewhat surprising as the strong decline is in contrast to general movements in consumption in 1981/82. It is believed to be due to the increasing relative price of petroleum products and the increased availability of domestically produced alternatives.

In the New Zealand Institute of Economic Research (NZIER) June 1982 *Quarterly Survey of Business Opinion*, merchants, including both retailers and wholesalers, report only a slight slow-down in their sales during the June quarter, although a more dramatic slow-down in both domestic and overseas orders is reported.

Seventy-seven per cent of respondents singled out poor demand as the factor most limiting their ability to increase turnover. As for the future, 53 per cent of respondents expect the general business situation in New Zealand to deteriorate in the next six months, 43 per cent expect present conditions to continue, while only 3 per cent expect an improvement.

The tax scale changes to be implemented on 1 October may provide a short-term boost to consumption expenditure, but this injection to household disposable income will not be sufficient to counteract for very long the contractionary influence arising from the wage freeze for wage and salary earners and declining real farm incomes. The contraction of real household disposable income combined with the declining rates of growth of the main money and credit aggregates should effectively constrain growth in consumption expenditure for the rest of 1982/83 and on into 1983/84.

INVESTMENT

Investment expenditure experienced recovery in most areas during 1981, with growth in expenditure in some areas continuing into 1982. Investment indicators now indicate that a slow-down in activity is currently taking place. However, largely supported by the major projects, the overall level of investment this year is likely to remain fairly strong in relation to pre-1981 levels.

Residential building activity increased significantly during 1981, with the annual running total of new building permits issued increasing each month from 14,424 in February 1981 to 19,320 in May 1982. The number of new dwelling permits issued in June, July and August 1982 decreased by 2.5, 11.4 and 11.3 per cent respectively from the same months of the previous year. By August the annual running total had fallen to 18,954. A similar, though more erratic, trend has been displayed in non-residential construction. The annual total of permits issued for other buildings declined marginally in the four months to July 1982, while the value of permits issued decreased by 0.2 per cent in the four months to July over the same period in 1981 (a significant fall in real terms).

A reduction in the availability of mortgage finance is one of the factors behind the reduction in the level of building activity. Many of the major financial institutions are being forced to reassess their lending policy in the light of the slow-down in deposit growth and their current high lending to deposits ratios.

The reduction in net permanent and long-term emigration currently being experienced should increase the longer-term demand for new dwellings. In the year to August 1982 it is provisionally estimated that there were 4,852 net long-term and permanent emigrants. This compares with 22,226 for the year ended August 1981.

After improving sharply in the second half of 1981, some plant and machinery investment indicators have weakened during 1982. A strong annual increase of 30.9 per cent in surveyed import orders for machinery and electrical equipment for the six months ended December 1981 was reflected in an equally strong 44.9 per cent annual increase in actual imports (cdv) of machinery and electrical equipment in the six months ended March 1982. As surveyed orders have declined by 9.8 per cent in the three months ended July 1982 (compared with the same period a year earlier), a contraction in actual imports of machinery and electrical equipment appears likely in the forthcoming months. However, not all indicators point to a decline in imports — surveyed import orders for transport equipment over the three months ended July 1982 were still 25.1 per cent higher than a year ago. But most of this growth came about during the month of May with only marginal increases being recorded in the following two months.

The Department of Statistics quarterly survey of manufacturing shows that in the 1982 June quarter additions to fixed assets, previously referred to as gross capital expenditure, increased by 72.3 per cent over the 1981 June quarter. This continues the strong growth experienced in the year to March 1982.

Low growth in farm incomes, particularly for sheep and beef farms, combined with input prices rising by almost 20 per cent in 1981/82, imply low levels of farm investment in the current year. Without the aid of SMP payments, investment in traditional areas of agriculture would probably fall significantly. Expectations of only small nominal increases in prices for wool and meat also provide a disincentive for investment in these traditional areas of agriculture. Until there is a recovery in the world economy, the prospect of poor returns in these areas remains. Recent forecasts of developments in the international economy have become more cautious and some are now suggesting a prolonged period of recession beyond 1982. Hopes that growth will resume in 1983 are now focussed on a rebuilding of stocks and renewed economic activity in the United States.

The aggregate inventories to final sales ratio in New Zealand was largely unchanged between 1980/81 and 1981/82, although there were sectoral differences. The ratios in the retail, wholesale and manufacturing sectors generally declined over this period. The seasonally adjusted retail stock to sales ratio declined from 0.57 in the 1981 June quarter to 0.54 in the 1982 June quarter. From the 1981 March quarter to the 1982 March quarter the seasonally adjusted ratio in the wholesale sector fell from 0.62 to 0.60, while over the same period the ratio in the manufacturing sector (excluding the primary food group) fell from 0.85 to 0.78.

Stocks in these sectors make up approximately 60 per cent of total measured stocks in the economy. The decline in these ratios probably occurred because the buoyancy in the economy over this period was treated by decision makers in these sectors as a temporary phenomenon, and so they did not fully maintain their stocks to sales ratios. If this is the case then some recovery can be expected in the stock ratios of these sectors with the slow-down in economic activity currently underway. This stock behaviour was one of the reasons why the unemployment rate continued to increase in a period in which suppliers of the domestic market were experiencing strong demand.

Although the aggregate ratio of inventories to final sales changed very little between 1980/81 and 1981/82, substantial stockbuilding occurred during 1981/82. (Stockbuilding is the aggregate contribution of inventories to growth in GDP, and is measured by the second order change in the level of inventories relative to the level of the previous year's GDP). In other words, the nominal increase in the level of inventories in 1981/82 was significantly larger than the increase in 1980/81. There is likely to be an increase in real stock levels in 1982/83, but this increase is not expected to be as large as that which occurred in 1981/82, so the contribution of inventories to growth in GDP is expected to be negative in 1982/83.

THE GOVERNMENT SECTOR

Government expenditure and receipts were $11,196.5 million and $9,378.2 million in 1981/82, respectively. This resulted in a budget deficit of $1,818.3 million, which was 19.2 per cent higher than the deficit of $1,524.9 million in 1980/81. The forecast deficit for 1982/83 is $1,879.0 million. In real terms this is tighter than the outcome for 1981/82, being only a 3.3 per cent increase in nominal terms over a period in which forecasts of the rate of inflation are in the region of 13 per cent. However, the deficit for 1982/83, at 6.8 per cent of estimated GDP, still represents a large net injection into the economy. The full year effect of the tax cuts announced in this year's Budget will not be felt until 1983/84, and the deficit in that financial year may therefore be more expansionary than that for 1982/83 unless there are other policy changes that reduce government expenditure or increase revenue.

The Budget deficit is only one measure of the impact of the government sector on the economy, and not necessarily the best measure. Other alternative measures are discussed in an article titled 'Government Expenditure and Revenue', published in the October 1982 *Bulletin*.

INCOMES

Wage and salary earners experienced real increases in pre-tax income in the year to June 1982, but a decline is currently underway and is expected to continue for at least the length of the wage-price freeze. Agricultural operating surplus (or net income) was down in real terms in the 1982 March year, although some groups, such as dairy farmers, experienced increases. A further decline in real agricultural operating surplus is expected in 1982/83. Other operating surplus, which includes other personal income and company income, is estimated by the NZIER to have increased by 23 per cent in 1981/82, a significant increase in real terms. Overall, real household disposable income, which excludes company income, rose by 1.2 per cent in the year to March 1982 but is estimated to have fallen by about 2 per cent over the June year. Contributing to this decline has been the substantial fiscal drag that was occurring prior to the tax scale changes effective from 1 October.

Official wage rate statistics show that pre-tax salary and wage incomes rose slightly in real terms during the year to June 1982. The nominal weekly wage index, which measures movements in award rates, rose at an average annual rate of 17.3 per cent over this period. This represents an average effective increase (before tax) of 1.2 per cent after adjustment for inflation. Over the same period actual wage rates, as measured by the prevailing weekly wage index, rose by 17.7 per cent, an average effective rise after adjustment for inflation (but before tax) of 1.5 per cent. The Labour Department's quarterly employment information survey for May 1982 showed that average weekly earnings also rose slightly in real terms. In the twelve months to May 1982 average weekly earnings excluding overtime rose by 17.4 per cent to $265.97, while average weekly earnings including overtime rose by 17.6 per cent to $285.27. Over the same period both average ordinary time hours and overtime hours worked per week rose marginally, increasing from 36.9 to 37 hours and 2 to 2.1 hours, respectively.

In the June quarter 1982 both the nominal weekly wage and the prevailing weekly wage indices actually declined marginally in real terms over the corresponding quarter of 1981, the falls being 1.4 and 0.7 per cent respectively, although such declines are not unusual and are generally caused by different timing in wage agreements and general wage orders from year to year. However, in the face of the twelve month wage and price freeze introduced on 22 June 1982 a further decline is expected in real pre-tax wage rates. This is because the effect of the freeze will be more sudden and effective on wage rates than on prices; in addition, import price increases and some officially sanctioned price increases are being passed on to the consumer.

The effect on disposable income will be alleviated partially by the large cuts in direct taxation to be effective from 1 October 1982, although this effect will in turn be partially offset by the indirect tax changes announced in the 1982 Budget. Middle income households will benefit most from the tax scale changes, while some low income households will actually pay more tax. A single taxpayer on $300 a week, which is about the average weekly earnings, will gain $10.34 a week, or $537 a year. The estimated cost of foregone tax revenue from the changes for 1982/83 is $400 million, while the net full-year cost is estimated to be $915 million. The tax cuts will temporarily serve to halt the decline in the real level of disposable income, but will not be sufficient in themselves to avoid a significant drop in real disposable wage and salary income in the 1983 March year. This fall is expected to continue at least until the beginning of the 1983/84 wage round late in 1983.

Mutton, beef and wool markets were weak during 1981/82, while dairy prices remained high. In the September 1982 *Quarterly Predictions* the NZIER estimates that agricultural operating surplus, including the Supplementary Minimum Price Scheme payments (SMPs), only increased by 8 per cent in the 1982 March year, a decline of approximately 7 per cent in real terms. This estimate is based on an 18.5 per cent increase in input prices and a marginal increase in input volumes, combined with a 2.5 per cent decline in the volume of gross agricultural production and only a 10.5 per cent increase in output prices. Weak prices for meat and wool are expected to continue during 1982/83, while dairy product prices may weaken because of the re-emergence of large international dairy stock-piles. With no increase in the prices offered with the SMP scheme for 1982/83, the NZIER forecast only a 9 per cent nominal increase in agricultural operating surplus.

Social welfare beneficiaries whose benefits are index-linked (the main group being National Superannuation recipients) will not be directly subject to an income freeze in 1982/83. The main effect of the wage-price freeze on their incomes will not be felt until the 1983/84 adjustments because of the lag in the adjustment process.

The Department of Statistics quarterly manufacturing survey shows that in the manufacturing sector the average ratio of profit to sales (excluding the primary food group) increased by 17.4 per cent in the March 1982 year over a year earlier. This is a substantial increase, but is mainly the result of the slump in profitability in 1980/81. The ratio increased only slightly by 1.3 per cent from 1979/80 to 1981/82. The survey for the June quarter of 1982 suggests some weakening in manufacturers' profitability.

The respondents to the NZIER June 1982 *Quarterly Survey of Business Opinion* on average expect a decline in profitability in the September quarter relative to the June quarter. Such a decline is expected because of reduced demand resulting from declining real household disposable incomes.

The wage and price freeze will clearly dominate developments in the incomes arena over the immediate future, although for the agriculture sector the weakness in the international economy is of more concern. As some price increases are taking place, and generally price increases are likely to be harder to police than wage increases, the freeze could have a significant impact on income distribution.

PRODUCTION

The volume of manufacturing production (excluding primary foods), as measured by an index derived from the Department of Statistics quarterly manufacturing survey, rose strongly during 1981/82, increasing at an average annual rate of 8.6 per cent over 1980/81 after declining at an average annual rate of 6 per cent during 1980/81. This strong growth is expected to be eroded during 1982/83 as a result of contracting real incomes and a subsequent fall in real annual consumption expenditure. The index for the June 1982 quarter shows a lower annual increase of 5.1 per cent. Manufacturing sales also grew strongly over 1981/82. In that year surveyed manufacturing sales were $15,978 million, an increase of 25.8 per cent over the previous year. But the June 1982 quarter also shows a declining rate of growth here, with a 20.2 per cent increase over the June 1981 quarter.

The increased production resulted in an increase in the number of hours worked in the surveyed industries, with total hours worked in 1981/82 increasing by 3.3 per cent over the previous March year. The total number of hours worked has shown a positive annual increase in each quarter since the 1981 September quarter (before which it had shown negative annual growth for five quarters), but once again the figure for the June 1982 quarter suggests a weakening, with the annual increase reduced to 2.9 per cent.

THE LABOUR MARKET

In the year to May 1982 the estimated total labour force increased by 1.4 per cent, while estimated total employment (being the estimated total labour force less registered unemployed and those employed on either public or private sector special employment schemes) only increased by 0.7 per cent. The net result was an increase of 13.6 per cent in the total of registered unemployed plus people employed on special work schemes. This brings the percentage of the estimated labour force unemployed or employed on special work programmes to 5.5 per cent at the end of May 1982, compared with 4.9 per cent a year earlier. The output growth recorded in 1981/82 did not reduce unemployment. It is expected that the number of people unemployed or employed under the special job creation programmes will continue to climb over the next twelve months, due mainly to the expected slow-down in economic activity and reduced emigration to Australia. While the overall employment market is expected to be weak, there will be strong demand from the major investment projects for certain specialised skills.

In August 1982 there were 50,474 registered unemployed (47,735 seasonally adjusted) of which 30.4 per cent or 15,369 had been registered for thirteen weeks or more, and 32,715 were receiving the unemployment benefit. There were also 32,144 people employed under either private (14,156) or public (17,988) sector job creation programmes in August 1982. This is an increase of 7,943 over the level in August 1981, and brings the total registered unemployed and those employed on special job creation programmes to 82,618 (78,264 seasonally adjusted), an increase of 10,821 or 15.1 per cent over the total in August 1981.

MONETARY CONDITIONS

Rates of increase in the main money and credit aggregates have slowed significantly over recent months. The slow-down has been generated primarily by a widening in the current account deficit which has resulted from a combination of a weakness in some export items, strong growth in import volumes and continued deterioration in the invisibles account.

The narrowly defined money supply (M1) and the money supply and selected liquid assets of the public (M3), are estimated to have increased by 9.8 and 10.8 per cent respectively in the year to August 1982. Respective rates of increase a year earlier were 14.3 and 17.9 per cent. In the year to August 1982 it is estimated that domestic credit and private sector credit grew by 14.8 and 18.9 per cent respectively. This compares with 17 and 26.2 per cent respectively a year earlier.

The reductions in the money and credit aggregates in seasonally adjusted terms in recent months have been much sharper than the annual growth figures indicate. In the last three months for which figures are available (June-August 1982), M3 grew by only 1 per cent in seasonally adjusted terms while private sector credit grew by 2.6 per cent. The current account deficit deteriorated rapidly over these three months and was the major reason for the sharp slow-down in monetary growth. The impact on the fiscal deficit of the 1 October tax cuts should lead to some modest recovery in seasonally adjusted monetary growth, provided the balance of payments does not deteriorate further.

As has been mentioned, the contraction in the rate of growth of the money base and the deposits of the financial institutions came about mainly as a result of the increasing current account deficit. But the growth in Government debt sales to the public also had an effect (particularly Inflation Adjusted Savings Bond issues). In this situation, with high lending to deposits ratios, the institutions were forced to compete for funds by bidding up interest rates on deposits. For example, the weighted average of rates on transferable certificates of deposit (for six months and under) was 14.1 per cent at the end of November 1981 and increased to a peak of 18.5 per cent at the end of April 1982. Selected finance company interest rates of one year and three years increased from 14.5 per cent and 15.3 per cent to 16.3 and 17.3 per cent respectively between November 1981 and April 1982. Lending interest rates were largely stabilised by the November 1981 strengthening of the Financial Services Regulations.

Although easing somewhat since April, the upward pressure on deposit rates remained. In response to this pressure, on 22 June 1982 as part of the general wage and price freeze the Government introduced the Interest on Deposits Order 1982 (IOD), as well as making some minor adjustments to the Financial Services Regulations. The IOD Regulations introduced a schedule specifying the maximum rates of interest that banks, savings banks, building societies and finance companies are permitted to pay on deposits. The main changes to the Financial Services Regulations were to broaden the scope of the regulations to include suppliers of credit who had more than $100,000 in outstanding loans (previously $2 million), and changes which mean that hire-purchase lending and leasing clearly come within the regulations. Subsequent to the introduction of the IOD Regulations interest rates offered on deposits appear to have stabilised, while rates that exceeded the imposed limits showed an initial decline. The weighted average of rates on transferable certificates of deposit (6 months and under) have stabilised at just below 16.5 per cent since early July, while selected finance company interest rates of one year and three years decreased from 16.4 and 17.3 per cent in June 1982 to 15.8 and 16.7 per cent, respectively, in August 1982.

PRICES

The CPI rose by 16.6 per cent in the year to September 1982, slightly lower than the 17 per cent rise in the year to June 1982. The latter was the largest annual percentage change for two years, (since the increase of 18 per cent in the year to June 1980) and followed a decline in the annual rate of inflation to 15 per cent in the year to June 1981. With the downturn in activity now being seen and tightening credit conditions the first evidence of an expected downturn in inflation is now appearing.

Housing costs (i.e. rental and home purchase costs) contributed most to the upsurge in the rate of inflation, increasing by 26.3 per cent in the year to September 1982, compared with an increase of 17.6 per cent a year earlier. Housing was the only group of the Consumers' Price Index that increased at a faster rate than the all-groups index. Within the September quarter itself, increases in indirect taxes and some government charges have also had a substantial effect on the CPI.

The expected rate of inflation for 1982/83 depends vitally on the outcome of the wage-price freeze currently in force. The price freeze aside, the slower growth in the monetary aggregates currently being experienced and expected to continue throughout 1982/83, the declining rates of inflation of our major trading partners, the termination of the devaluation of the exchange rate in relation to the basket of currencies and generally weaker demand conditions all point to a lower rate of inflation in 1982/83. In their September 1982 *Quarterly Predictions* the NZIER forecasts that the CPI will increase by 12.6 per cent in the year to March 1983.

THE EXTERNAL SECTOR

The OET current account deficit has continued to deteriorate. In the year to August 1982 the deficit stood at $1,825.5 million, compared with a deficit of $729.5 million for the year ended August 1981. This brings the deficit to approximately 6 per cent of GDP, a figure which is of some concern in the light of the continued weak demand expected for New Zealand's major agricultural exports in the immediate future and the strain that will be put on the external accounts by the major investment projects. The deterioration in the deficit was primarily the result of a decline in the balance of trade, although there was also a further deterioration in the balance on invisible transactions.

The OET trade surplus for the year to August 1982 was $143.0 million, compared with a surplus of $954.8 million in the year to August 1981. The decline was due to a significant upsurge in the volume of imports, late receipt of some export proceeds, and slow growth in export volumes. These volumes were adversely affected by weak international demand, while the rapid growth in import volumes resulted from the high level of domestic activity experienced over the period in both consumption expenditure and investment. In the September 1982 *Quarterly Predictions* the NZIER estimates that the volume of goods exported in the 1982 March year increased by 4 per cent over the previous year, while the volume of goods and services imported increased by 11.5 per cent (with the volume of goods imported growing at a faster rate than the volume of services). Overall, in the year to August 1982 OET export receipts increased by only 4 per cent, while OET import payments increased by 19.6 per cent.

Decreases in receipts for meat and wool contributed to the lower growth in export receipts for the year ended August 1982. Among commodity groupings which showed growth, the most significant gains were registered by other primary products which mainly includes receipts for fish and fruit (+29.9 per cent), manufactured exports (+17.9 per cent), and dairy products (+12.3 per cent).

In the year ended August 1982 the OET balance on invisibles deteriorated to a deficit of $1,968.5 million, from $1,684.3 million the previous year. Invisible receipts grew at a faster rate than invisible payments, (23.2 per cent as compared to 19.7 per cent), but because of the much larger payments base the invisibles deficit still widened.

The official capital account (including IMF transactions) showed an inflow of $1,462.4 million for the year ended August 1982, up significantly from the inflow of $817.9 million the previous year. The major factors behind this were the increases in Government borrowing and other official receipts from $1,084.0 million and $195.1 million, respectively, in the year to August 1981 to $1,754.6 million and $786.1 million in the year to August 1982. There was also a large increase in Government debt repayments which increased from $98.6 million to $828.3 million.

The net private capital inflow increased substantially from $63.5 million to $427.2 million. This was the result of private sector capital receipts increasing from $486.1 million in the year to August 1981 to $1,128.9 million in the current August year. The main reason for the increase was capital flows related to the various large scale investment projects, in particular the aluminium smelter extensions and the expansion of the Marsden Point oil refinery. Official overseas reserves increased by $150.9 million to $917.9 million over the August 1982 year.

The outlook for the remainder of the 1983 March year includes continued weakness in the trade balance. Contributing to this weakening trade balance will be poor international prices for many of our exports. Export volumes are expected to grow in the region of 4 per cent, the same as for 1981/82. The falling domestic demand in the second half of 1982/83 should reduce growth in import volumes over that period, but the strong growth in the first half of 1982/83 combined with the impact of the major project imports will mean the net effect for the year will be another sizeable increase in import volumes. Some deterioration in the terms of trade, resulting from the combined effect of slow growth in export prices because of weak international demand, and a moderate increase forecast for import prices, is also likely to contribute to the deficit. The trade balance will hopefully improve in 1983/84 as export prices pick up and lower demand for imports follows the slow down in domestic demand.

CONCLUSION

During the first half of 1982/83 economic activity has levelled off following the relatively buoyant conditions of 1981. Most recent indicators suggest a downturn in activity is underway. This slow-down is the result of both internal and external factors. Internally, the high rate of inflation and fiscal drag, combined with the restraint on wages, is producing a significant reduction in real disposable incomes and consumer spending, which will be only partially and temporarily offset by the income tax cuts in October. The NZIER *Quarterly Survey of Business Opinion* tends to confirm this with a slow-down in the growth of output and orders being reported in all parts of the private sector. Externally, weak export prices, combined with the higher growth of import volumes, have contributed to a rapid deterioration in the current account deficit. In the current year, returns to meat and wool exporters are expected to fall in real terms for the second year in succession, while dairy product prices may weaken because of the re-emergence of large international dairy stock-piles. Thus, there seems little prospect of significant economic growth during 1982/83. The NZIER forecast no increase in real GDP in 1982/83.

It seems unlikely that the international economy, and in particular the American economy, will experience sustained recovery in 1982/83. International recovery appears to be a necessary condition for sustained growth in the New Zealand economy as any internally encouraged recovery is likely to further aggravate the balance of payments and the problem of inflation at much higher levels than most of our trading partners.

The current balance of payments situation and the fiscal constraint currently being observed imply that monetary and credit conditions should remain firm for some time ahead. There is therefore little prospect of a reduction in unemployment in the short-run at least. Instead, the slow-down in economic activity being experienced, combined with a reduction in net migration losses, point to the possibility of further increases in the short-run in the number of people unemployed or employed in special employment programmes.

Overall, the prospects for 1983/84 look little better at this time, although there are some forecasts of the elusive recovery in the international economy appearing by late 1983. One of the few areas which is likely to show improvement in the remainder of 1982/83 and into 1983/84 is the rate of inflation. The slower rates of growth of the monetary aggregates, assisted by the wage, price and exchange rate freeze, should all exert downward pressure on the rate of inflation. The path of post-freeze inflation is more difficult to predict and will depend crucially on how prices and wages behave as the freeze expires.