CHiLD POVERTY ACTION GROUP

2009 New Years Primer

Introduction

This primer is intended to illustrate the likely economic climate within which Child Poverty Action Group (Inc) and other NGOs will work over the next twelve months. For 2009, it's difficult to know where to start, or what to include. New Zealand has a new government, the world economy is going down the gurgler faster than...well, a fast thing, and the economic crisis looks increasingly like it will be overtaken by an environmental one. Internationally, the mood of the electorate has turned to fury as taxpayers have watched corporate bad behaviour being rewarded by governments, while those same taxpayers are increasingly likely to be unemployed. In New Zealand the levers of local and national-level power are being wielded by an assortment of anti-intellectuals who, like Titanic survivors clinging to debris long after the ship has gone down, still hold close their delusions about the economic benefits of unregulated markets. At a time when governments are bankrupting themselves bailing out the excesses of those same unregulated markets, this seems like an odd stance, indeed.

The election result was expected but saw any existing, shaky focus on poverty largely lost amidst the fear and loathing generated by a focus on tax cuts and law and order. In late December, just as the election night blues were beginning to recede, the unease was rekindled by the news of the Israeli invasion of the Gaza strip. After three weeks of air raids and a ground offensive, the death toll had reached 1,200, and many thousands more had been injured. The slaughter of Palestine's civilians brought thousands of protesters onto the streets in cities around the world including, for the first time in many years, Auckland and Wellington.

However, public dissatisfaction needs more than a complex war on the other side of the world to keep it on the streets. As the last few years have shown, when people feel wealthy, even if only by spending other people's money, political activism goes out the window. But what happens if people feel poorer, start to lose their jobs, and find they can't zoom off overseas once a year as they assume they have the right to do? That's not at all clear, and may well depend on the extent to which the government is committed to protecting the income and social status of the middle class. The poor have been poor for years, and none of the policies, or indeed policy directions, announced by National are going to help them. But the upper-middle classes having their private schools shut down? Now *that's* a crisis.

The credit crunch that was under way this time last year has not come and gone leaving no trace behind, as was widely predicted in the respectable media. Rather, it has stalled growth in the developed world. In a globalised world no one escapes unscathed, and the so-called de-coupled East Asian economies have also taken a hit. China's growth has all but stopped in the space of twelve months, with 26 million jobless migrants now moving back to their under-developed, impoverished villages. Yep, that's right, 26 *million.* And that doesn't include the millions of informal sector workers who aren't included in official statistics.

And how are the world's ordinary citizens feeling about their till-recently healthy economies imploding like a soggy soufflé? Iceland, the first and perhaps the most spectacular victim of the credit crunch, has overthrown its government. In Greece the shooting of a young man by police resulted in riots, which quickly focused instead on the economy. Students in France have protested cuts to education; the former Soviet states of Eastern Europe – many of them "flat tax" supposed success stories – have exploded in civil unrest as their economies have screeched to a halt. In common with other countries, Eastern Europe has experienced a real estate boom, with many people financing their mortgages with Euros. These are now proving expensive to service as local currencies plunge in value. And twelve months after the assassination of Benzir Bhutto, the highly unstable Pakistan is also suffering economically. This has contributed to its appearance onto the U.S. military's list of weak and failing states potentially subject to "sudden and rapid collapse". Don't mention the nukes.

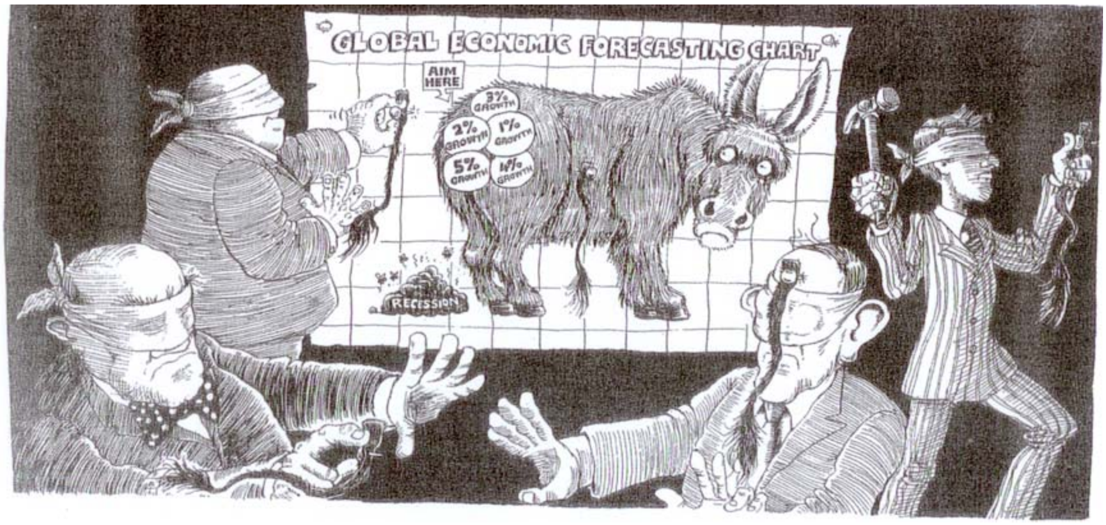
In essence, things got worse than elite opinion publicly admitted was possible, and they got much worse much faster than almost anyone thought. Still, there is no depression in New Zealand, right?

How long and deep does a recession have to be before it becomes a depression?

There is no universally agreed on definition of a depression – "we don't know what one looks like, but we'd know it if we saw it" seems to be the prevailing dictum.

Given the accuracy of economic forecasting over the last eighteen months, that's not exactly reassuring. Nor is that fact that business websites have recently started fretting over this very question. The definition that appears to be frontrunner at present is "a 10 percent decline in real GDP over the course of a year or more." New Zealand has had three quarters of GDP shrinkage, but total change in GDP for the year to September was only minus 0.1%, so we have some way to go before being in a full-blown depression. Still, the number of unemployed has already the highest in five years. If those who are "discouraged" from seeking work and who work part-time but would like to work full-time are added in, the unemployment rate rockets up to almost 9%.

Figure 1: The science of economic forecasting



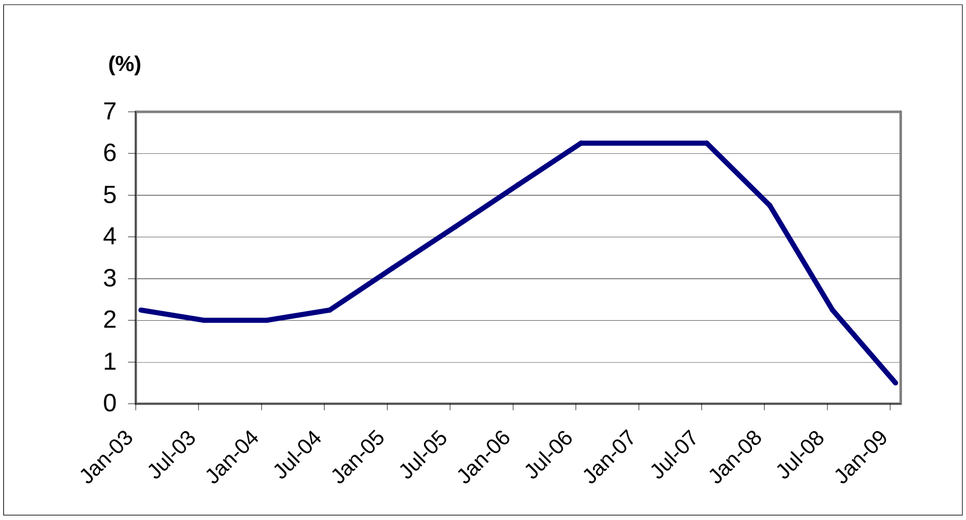
Source: Guardian Weekly

The good news is that New Zealand's "plain vanilla" banking system does not appear to be collapsing in quite the same way as that of the US or the EU. The bad news is that the borrow-and-spend binge of recent years has left New Zealand vulnerable to overseas capital markets, with a very high current account deficit of around 8% of GDP. The dollar is falling, and the country's sovereign debt has been downgraded. Banks may be able to roll over debt, but it will be more expensive. This is one reason they have been reluctant to pass on the Reserve Bank's interest rate cuts. They can pass them on for short-term debt, but are more constrained for longer-term debt sourced from overseas.

The curious ineffectiveness of monetary policy

Which brings us to one of the key issues for the world's monetary authorities, and that is that monetary policy isn't working. In theory, when interest rates, which are controlled by the central bank, are reduced then this lowers the cost of borrowing. Consumers and businesses borrow more to consume or invest, and all this purchasing activity gets the economy bubbling along again. *Voila*! The recession is but a fading memory. (Unless you're one of the ones who fails to recover, in which case you're still broke when the next recession rolls round. Some social agencies deal with these people already on a daily basis).

Figure 2: Federal Reserve Primary Interest Rates



Source: Federal Reserve, www.federalreserve.gov

Figure 2 shows the Federal Reserve's wholesale interest rates since January 2003, when the last recession was deemed to be over, and interest rates started rising again. As in New Zealand, consumption fuelled by borrowing and an overheated housing market allowed US policymakers to ignore structural weaknesses in the economy and ignore rising inequality. Yet by mid-2007 it was clear that the wheels were starting to come off. The Dow – a reasonably accurate barometer of the US economy's health – had started to fall, and quickly. House prices had been falling for some time, and unemployment was creeping up, despite the Bush administration's best efforts to mop up surplus labour with two imperial wars. It was also becoming clear that the big banks were in trouble, largely as a result of their "innovative" packaging of dodgy mortgages.

Publicly in denial that the contagion would spread, the Fed cut its benchmark interest rate in mid-2007. That didn't work, and in late 2007 data showed manufacturing had all but ground to a halt, with unemployment also up sharply. There were fears of a slowdown in spending over the Christmas period as consumers were hit with rising food and oil prices, bumped up by speculators fleeing money markets. In response, the Fed cut interest rates again.

And again. And again after that. But what no one seemed to have figured out is that although interest rates affect capital flows as funds look for arbitrage opportunities, most developed countries have little productive economic activity to fall back on, and once consumers get nervous and snap their wallets shut (or become unemployed) there's little to keep the economy rolling. In the US and Great Britain up to 4% of GDP is the financial sector, and when that part of the economy effectively vanished in the first half of 2008, then interest rates became irrelevant. If monetary policy were working as planned, firms would be investing but they're not – in fact, the latest figures from New Zealand show a massive slowdown in investment expenditure. As Figure 2 shows, interest rates are now 0.5% yet the US economy is continuing to spiral downward, dragging the world with it. It's like watching a slow motion train wreck. The only problem is, no one knows when it will stop.

Holy cow! It's Infrastructure Man!

In New Zealand we've had a mind-numbing barrage of meaningless prattle about the recession. It's been quickly adopted by the new government keen to use it as Trojan horse to push through policies they've actually been harping on about for years. Sadly, National's policies bear little resemblance to anything that might help real people get through a downturn, unless by accident. One feeble attempt at some kind of bailout measure has been the introduction of another tier to the welfare system through ReStart, however that will be of no benefit to the already-poor or any other workers jettisoned as the economic boat begins to take on ever more water. And work-for-the-dole plans for sole parents have yet to be abandoned. Instead, the Minister has said: "The Government is committed to work testing as we believe paid work is the route to independence and well-being for most people, and is the best way to reduce child poverty." Perhaps someone needs to point out to the Minister that similar policies overseas are already facing problems as jobs disappear into the ether.

This seeming obliviousness to what is happening in the real world poses a disturbing question: Does the new administration have any idea what is going on, or do they know we are deeply in the poo and are keeping quiet because they don't know what to do? Which is preferable?

In the meantime, the Resource Management Act is being reformed to limit the rights of the public to object to infrastructure projects, or to even be notified about them. Nick Smith tried to put this objectionable development as a step forward for ordinary homeowners applying for resource consents to build a deck. Decks, however, are not the issue. The issue is supermarkets with vast carparks and no traffic control plans, power stations, and roads. There is little doubt the reforms have been designed to facilitate National's "infrastructure" projects which, we have now been told by a Prime Minister almost delirious with relief, will get "New Zealanders back to work and into work quickly".

Predictably, a lot of money is going to roading, although not nearly enough, according to lobbyists such as the Council for Infrastructure Development. Pity this corporate welfare will cost those back-to-work New Zealanders billions of dollars for projects that will soon be made redundant by the advent of peak oil.

If the country is going to preserve a few jobs by building infrastructure, why not focus on more and better quality low-income housing? Building the 68 planned state houses is not going to ease any housing shortages unless they're all in Gisborne, nor is it going to keep many people in work for long. And, as David Cunliffe has been unkind enough to point out, this by no means makes up for the 300 state houses that will no longer be built in Hobsonville (John Key's electorate, by happy coincidence), or the 1,500 homes not built as a result of the cancellation of the Hope programme (The Hope homes were to be built on Crown land so whether they were ever anything more than a twinkle in the former Minster's eye remains a moot point).

New Zealand's children bear the brunt, again

How long will it take to get through this? The honest answer is "no one knows". Punters are now picking the economy will start to pick up late 2009-2010. A few such as Rod Oram, one of the few commentators who has consistently sounded a warning that we are facing a serious downturn, are less optimistic. History suggests that it will be several years before the economy bottoms out after the meltdown in financial and sharemarkets. So a recovery is unlikely much before 2011.

How bad will it get? What should child advocates, in particular, prepare themselves for? Treasury is talking about 8% unemployment, and this seems a fair call for 2008. Some parts of the US already have 9% unemployment, and are predicted to go as high as 15-17%. If New Zealand's official unemployment peaks at 8% it will be a miracle. Given the government's need to keep ACT on side, many low-income families with children will probably be left hanging around the bottom of a social ladder whose rungs have mysteriously vanished. Or find they have had the rug pulled from underneath them. Or whichever metaphor pops out of some spokesperson's mouth next. With the economic and social dislocation of the 1990s being reprised, and no realistic solutions on offer to protect the vulnerable, it is probable that hospitalisation rates for children will increase, as will household overcrowding and income inequality. The social and economic marginalisation of the country's poorest children looks set to continue, with the inevitable social fallout being dealt with by calls for ever-increasing numbers of prisons and police. In other words, there will be no shortage of work for children's advocates.

Where will any anti-recessionary spending, assuming there is some, be focused? Building roads, irrigation schemes for farmers, subsidising telcos with broadband investment (a welcome addition to our productive capacity, surely), propping up private schools and pre-school facilities, and paying private sector ideologues to write reports on "cutting bureaucracy" and "reducing compliance costs". Remember, welfare is only bad when it goes to those who actually need it. The voluntary and NGO sector will have to fight to ensure the interests of their constituents don't fall completely by the wayside.