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Westpac Institutional Bank

When rising tides don't lift all boats

Household Income Growth since 2008

- **Disposable household incomes have grown by an inflation-adjusted figure of around $6 billion since the 2008/09 recession.**
- **However, income changes to household groups have been uneven. The mortgage belt and tax payers received the largest disposable income boosts, while income from savings and business sources has gone backwards.**
- **Tax cuts and Government welfare payments have been a major source of aggregate household income growth.**
- **Over the next few years, we expect the profile of household income growth to change. The Government can no longer afford tax cuts and rising interest rates will benefit savers at the mortgage belt's expense. In addition, reinsurance funds associated with the Canterbury rebuild will be a major new source of income.**

Real disposable household incomes have risen despite the 2008/09 recession...

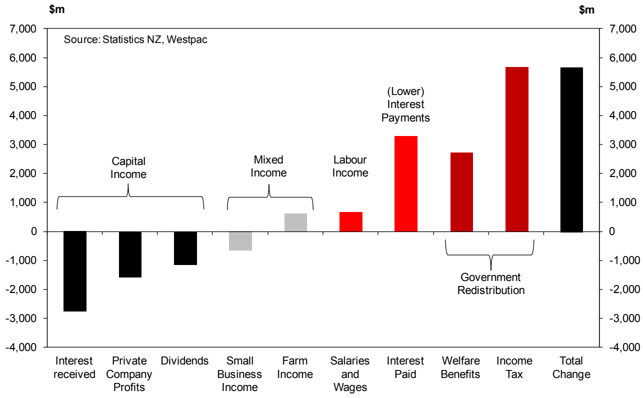
Statistics New Zealand's income measure of GDP shows that real gross disposable household incomes increased by $5.7 billion since the 2008/09 recession (Figure 1). This is a major step down from the stellar income growth of the mid 2000s, but is not too different from the growth experienced over the 1990s and early 2000s (see the black line in Figure 2).

The increase in household incomes is effectively thanks to the Government, via $6.3 billion worth of tax cuts and $2.7 billion worth of welfare benefit payments. Lower interest payments also contributed to the increase in household incomes. Increases in wages, salaries and farm incomes made small, but positive, contributions to household incomes.

In contrast, income from capital dived. Income from businesses (private company profits, dividends and small businesses other than farms) fell $3.3 billion, while interest received by households fell $2.7 billion.

Statistics NZ releases three breakdowns of GDP – production, expenditure and income. The income measure is rather unloved because it is released with such a long delay. We have given the series for the household sector a bit of TLC, using it to look at how gross disposable incomes by major source have changed at an aggregate level since the 2008/09 recession. The data have been adjusted for inflation. Note that total change includes income from other sources not shown in Figure 1.

Figure 1: Contributions to change in real gross disposable household incomes, 2008 to 2012



However, this analysis does not extend to how these incomes were spent or saved, so only captures one side of aggregate household welfare. Also, note from this point we use 'household incomes' as shorthand for 'real gross disposable household incomes' to help prevent the reader from getting too tongue-tied.

...though the distribution of income has changed

Interest rate falls have re-distributed aggregate household income from savers to borrowers. Interest payments fell by $3.3 billion[1], more than offsetting the $2.7 billion fall in interest received. The small net difference (+$0.6 billion) reflects that New Zealand households have borrowed more than they saved as well as the different maturity profile of household deposits and loans.

The mortgage belt have benefitted most from the lower interest bill as mortgages account for over 90% of household borrowing.

$6.3 billion boost to household incomes from tax cuts

Tax cuts lifted household incomes by $6.3 billion since the 2008/09 recession. This period includes tax cuts by both the Labour Government (in 2008) and the National Government (in 2010). Partially offsetting the tax cuts were higher tax payments, owing to an increase in taxable household incomes and some tax payers moving into higher tax brackets. Overall, the net effect of lower tax payments lifted household incomes by $5.7 billion.

Welfare benefit payments added a further $2.7 billion to household incomes. Most of this increase was due to an additional 70,000 people turning 65, and thus becoming eligible

1 Lower interest payments are defined as "income" by Statistics New Zealand because they free up money for households to spend or save.

for New Zealand Superannuation (NZS). Also, the number of Unemployment Benefit, Domestic Purposes Benefit, and Accommodation Supplement recipients increased. At the same time, NZS recipients benefitted as tax cuts lead to higher NZS payment rates.

Fiscal policy has effectively softened the blow from the shock to household capital and labour incomes following the recession.

...but it is payback time over the next few years

We expect that our call for rising interest rates from the late this year will begin to cramp the mortgage belt's style over the next few years. At the same time, savers' incomes will make a comeback roughly equal in magnitude (shorter average deposit terms may mean that savers' incomes rise faster initially).

With the Government looking to return to surplus and unable to afford further tax cuts, the Government will subtract from household incomes over the next few years. As the economy grows in 2013 and 2014, we expect tax payments to rise in line with rising taxable household incomes. Welfare payments will continue to rise, mainly as more baby-boomers turn 65, but by less than the increase in tax payments.

At the same time, insurance money will fund much of the Canterbury rebuild, boosting GDP growth and household incomes more generally. In particular, this growth will lift wages, salaries as well as business owners' incomes.

As we have seen before, rising household income growth may not be even. Figure 2 below shows how the distribution of income has changed over history. No doubt household incomes will continue to evolve over time, sometimes in mysterious ways.

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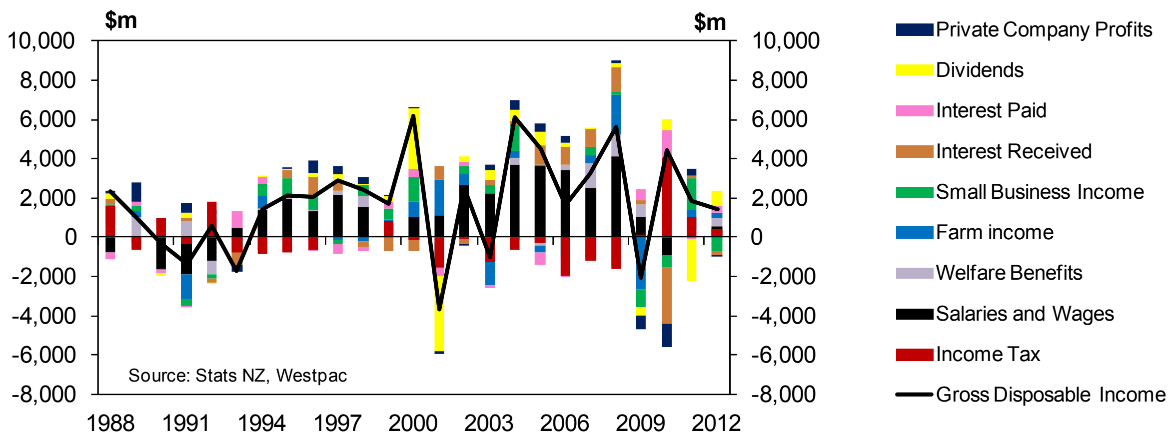
Economist

Figure 2: Contributions to annual change in real gross disposable household incomes



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