SIGNIFICANT FINANCIAL FORECASTING ASSUMPTIONS - 9 YEAR PLAN 2025-34

Department: Finance

EXECUTIVE SUMMARY

1 The purpose of this report is to seek Council approval of financial significant forecasting assumptions (assumptions) that are to be used in the development of the 9 year plan 2025-2034 (the 9 year plan).

RECOMMENDATIONS

That the Council:

a) **Approves,** for the purposes of developing the 9 year plan 2025-34 and consulting with the community, the significant forecasting assumptions at Attachment A.

BACKGROUND

2 Schedule 10 (17) of the Local Government Act 2002 (LGA) provides the following:

A long-term plan must clearly identify—

(a) all the significant forecasting assumptions and risks underlying the financial estimates:
(b) without limiting the generality of paragraph (a), the following assumptions on which the financial estimates are based:
(i) the assumptions of the local authority concerning the life cycle of significant assets; and
(ii) the assumptions of the local authority concerning sources of funds for the future replacement of significant assets:
(c) in any case where significant forecasting assumptions involve a high level of uncertainty,
(i) the fact of that uncertainty; and
(ii) an estimate of the potential effects of that uncertainty on the financial estimates provided.

3 At its meeting on 25 November 2024, Council approved the first set of significant forecasting assumptions (climate change projections) for inclusion in the 9 year plan. This report seeks approval of the significant financial forecasting assumptions to be used in the development of the 9 year plan.

DISCUSSION

4 The financial assumptions presented at Attachment A include interest rates, inflation rates, and NZ Transport Agency Waka Kotahi (NZTA) funding assistance rate assumptions to be used over the 9 year period.

5 Where possible, external advice has been used to support the assumptions made. For example, the interest rate assumptions have been provided by Dunedin City Treasury Limited (DCTL), and the inflation rates proposed to be used have been provided by BERL (Attachment B).

6 We have assumed that the applicable funding assistance rate will be 51% throughout the 9 year period.

7 The interest rate assumptions provided by DCTL are shown below. The assumption for the 9 year plan will be calculated at 4.15% for years 2025-26 to 2028-29 (years 1-4) then 5.00% from years 2029-30 to 2033-34 (years 5-9).

Financial Year	Expected Interest Rate
2024-25	4.22%
2025-26	3.79%
2026-27	3.99%
2027-28	4.28%
2028-29	4.42%
2029-30	4.61%
2030-31	4.83%
2031-32	5.08%
2032-33	5.15%
2033-34	5.29%
5 Year Average	4.14%
10 Year Average	4.57%

8 Other financial assumptions made are based on Council's Accounting Policies, for example, the useful lives of significant assets.

OPTIONS

9 Council is required under the LGA to have significant forecasting assumptions as part of the 9 year plan. Options have not been presented but Council may decide to modify the significant forecasting assumptions.

NEXT STEPS

10 The Significant Forecasting Assumptions, with any amendment, will be used in the development of the 9 year plan.

Signatories

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Authoriser:	Carolyn Allan - Chief Financial Officer

Attachments

	Title	Page
A	Financial Forecasting Assumptions	
B	BERL Cost Adjustors	

SUMMARY OF CONSIDERATIONS

Fit with purpose of Local Government

This decision enables democratic local decision making and action by, and on behalf of communities, and promotes the social, economic, environmental and cultural wellbeing of the Dunedin communities in the present and for the future.

Fit with strategic framework

	Contributes	Detracts	Not applicable
Social Wellbeing Strategy	✓	☐	☐
Economic Development Strategy	✓	☐	☐
Environment Strategy	✓	☐	☐
Arts and Culture Strategy	✓	☐	☐
3 Waters Strategy	✓	☐	☐
Future Development Strategy	✓	☐	☐
Integrated Transport Strategy	✓	☐	☐
Parks and Recreation Strategy	✓	☐	☐
Other strategic projects/policies/plans	✓	☐	☐

The 9 year plan contributes to all of the objectives and priorities of the strategic framework as it describes the Council's activities, the community outcomes, and provides a long term focus for decision making and coordination of the Council's resources, as well as a basis for community accountability

Māori Impact Statement

The adoption of the Māori Strategic Framework signals Council's commitment to mana whenua and to its obligations under the Treaty of Waitangi. Mana whenua and Māori will have an opportunity to engage with the 9 year plan consultation process through a series of planned hui.

Sustainability

Major issues and implications for sustainability are discussed and considered in the Infrastructure Strategy and financial resilience is discussed in the Financial Strategy.

LTP/Annual Plan / Financial Strategy /Infrastructure Strategy

This report provides details of the assumptions being made to assist the development of the 9 year plan.

Financial considerations

Financial assumptions are provided in the report.

Significance

The 9 year plan is significant and will be consulted on using the Special Consultative Procedure.

Engagement – external

There has been no external engagement in the preparation of the draft assumptions. However information from BERL and DCTL has been use to inform the financial assumptions.

Engagement - internal

Staff from across Council are involved in the development of the 9 year plan.

SUMMARY OF CONSIDERATIONS
Risks: Legal / Health and Safety etc. The level of uncertainty for each of the assumptions made, and the effect of the uncertainty is included in the report.
Conflict of Interest There are not known conflicts of interest.
Community Boards Community Boards will be consulted on the 10 year plan 2024-34.

Financial forecasting assumptions

Assumption	Level of uncertainty	Reason for uncertainty	Effects of the uncertainty
Capital expenditure budget for renewals The levels of renewals budgeted in this 9 year plan and Infrastructure Strategy will ensure the long term integrity of infrastructure assets.	Low	Generally, the DCC can determine budgets for renewals, subject to market forces, and legislative and regulatory changes.	Long term deferral of renewals poses a risk of asset deterioration and compromise of network integrity and requires unbudgeted capital and/or operating expenditure.
Internal capacity and capability Ongoing improvements to work and procurement practices will allow delivery of operational and capital expenditure programmes and projects.	Low	Generally, the DCC can determine resourcing for programme and project delivery, subject to market forces.	Failure to adequately resource capital expenditure programmes and projects may impact on delivery, which may result in future unbudgeted capital and/or operating expenditures.
External capacity and capability Sufficient design, engineering and construction capacity, including availability of construction materials, exists to undertake contracted operational and capital expenditure programmes.	Low/ Medium	That other large-scale national or local projects (e.g. Christchurch or Dunedin Hospital rebuilds) impact on local industry capacity and capability.	Issues with the availability of contractors may cause delays or require unbudgeted capital and/or operating expenditures.
Useful lives of significant assets The useful lives of significant assets shown in accounting policies and asset management plans have been appropriately assessed.	Low	Appropriate practices are followed.	An unexpected failure of an asset due to an inadequate assessment of the remaining useful life may require unbudgeted capital and/or operating expenditures.
Fixed asset valuations Scheduled revaluations of assets and forecast asset values in the budget are based on the DCC's valuation policies, which are consistent with accounting standards for Public Benefit Entities.	Low	Revaluations are scheduled regularly to ensure minimal variation of asset values between valuations. The DCC's Statement of Accounting policies describes how potential variances are managed within the financial statements.	Revaluations are significantly different from the forecasts, which would impact depreciation.
Inflation Inflation adjustors are applied as per the price level adjustors schedule provided below.	Low	Inflation levels and prices may vary from those projected.	Unexpected inflation may require unbudgeted capital and/or operating expenditures.

Assumption	Level of uncertainty	Reason for uncertainty	Effects of the uncertainty
Borrowing Costs Interest on existing and new debt is calculated at 4.15% for years 2025-26 to 2028-29 (years 1-4), then 5.00% from years 2029-30 to 2033-34 (years 5-9).	Medium	There is uncertainty on the floating rate debt, but the expectation is that interest rates will stay relatively stable over the 10 year period.	Interest rates may vary from those projected and require unbudgeted financing expenditures.
Waka Kotahi New Zealand Transport Agency subsidy rates Revenue from the NZ Transport Agency Waka Kotahi (NZTA) is calculated at the normal funding assistance rate of 51% per annum. Subsidy rates vary depending on the nature of the work being completed.	Medium	Subsidy levels may vary from those projected and NZTA agency priorities areas may differ from the DCC's renewal and capital programme.	Subsidy revenue may be less than expected and require changes to levels of service and/or unbudgeted capital and expenditures.
Forecast return on investments The Financial Strategy will provide information on returns from Council-owned companies, the Waipori Fund and the Investment Property portfolio. The target from the Waipori Fund is inflation adjusted using the price level adjustor provided below. The return from Council-owned companies is not inflation adjusted.	Medium	Income from investments may vary from those projected.	Investment income may be less than expected requiring changes to levels of service and/or an increase in revenue.
Sources of funds for future replacement of significant assets The Revenue and Financing Policy outlines the funding sources for capital expenditure. The Financial Strategy outlines the use of debt and other sources to deliver the capital programme while limiting debt to within the debt limits outlined in the Financial Strategy.	Low	The timing and/or cost of the capital expenditure programme may vary.	Variation to the timing and/or cost of the capital expenditure programme may require changes to levels of service and/or an increase in revenue.

Price level adjustors schedule – BERL[1]

	2026	2027	2028	2029	2030	2031	2032	2033	2034
Index Value									
Roading	1061	1094	1126	1157	1188	1217	1247	1277	1305
Water	1091	1137	1183	1228	1270	1308	1344	1375	1406
Waste	1072	1108	1143	1177	1210	1242	1273	1303	1333
LGCI Opex	1062	1094	1124	1152	1180	1207	1234	1260	1286
LGCI Capex	1064	1096	1128	1158	1187	1215	1243	1271	1298
CPI	1325	1352	1379	1406	1433	1462	1493	1524	1556
Inflation Adjustors - Cumulative									
Roading	100.0%	103.1%	106.1%	109.0%	112.0%	114.7%	117.5%	120.4%	123.0%
Water	100.0%	104.2%	108.4%	112.6%	116.4%	119.9%	123.2%	126.0%	128.9%
Waste	100.0%	103.4%	106.6%	109.8%	112.9%	115.9%	118.8%	121.5%	124.3%
LGCI Opex	100.0%	103.0%	105.8%	108.5%	111.1%	113.7%	116.2%	118.6%	121.1%
LGCI Capex	100.0%	103.0%	106.0%	108.8%	111.6%	114.2%	116.8%	119.5%	122.0%
CPI	100.0%	102.0%	104.1%	106.1%	108.2%	110.3%	112.7%	115.0%	117.4%
Inflation Adjustors - Annual									
Roading		3.1%	2.9%	2.8%	2.7%	2.4%	2.5%	2.4%	2.2%
Water		4.2%	4.0%	3.8%	3.4%	3.0%	2.8%	2.3%	2.3%
Waste		3.4%	3.2%	3.0%	2.8%	2.6%	2.5%	2.4%	2.3%
LGCI Opex		3.0%	2.7%	2.5%	2.4%	2.3%	2.2%	2.1%	2.1%
LGCI Capex		3.0%	2.9%	2.7%	2.5%	2.4%	2.3%	2.3%	2.1%
CPI		2.0%	2.0%	2.0%	1.9%	2.0%	2.1%	2.1%	2.1%
Standard NZTA Subsidy Rate:	*51%*	*51%*	*51%*	*51%*	*51%*	*51%*	*51%*	*51%*	*51%*

[1] *Source: BERL - Cost adjustors 2024 final update, October 2024*

Cost adjustors 2024 final update

Taituarā

Whiringa-ā-nuku / October 2024

Authors: Urvashi Yadav and Hugh Dixon

Reference No: #6482 Whiringa-ā-nuku / October 2024

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1 Introduction

The economic indicators are now telling a cohesive story; the road to economic recovery will be slow. Prolonged higher interest rates are now having a widespread impact across the economy. The manufacturing and construction sectors have been particularly impacted, with activity and employment in sharp decline. The services sector has fared better, but activity has remained subdued amid low household and business spending.

On the bright side, inflation is declining fast, both domestically and internationally. Core inflation is now within the target range of 1-3 percent. As anticipated in the interim update, the Reserve Bank of New Zealand (RBNZ) has now started to loosen the monetary settings by slashing the Official Cash Rate (OCR) by 75 basis points in total over the last two OCR announcements. But it will take some time for the impacts of these cuts to start to dissipate through the economy. Unemployment will continue to increase and household and business budgets will remain constrained. The current trajectory will see economic activity slowing down further over the rest of 2024, with households bearing the brunt of the downturn. This could have implications for economic well-being in the communities.

Against this backdrop, the purpose of this report is to provide Taituarā with a set of robust economic forecasts of input costs for local government. Based on feedback from practitioners, we are continuing to provide an interim update in July, followed by a final update in October. The June 2024 numbers in this update are actuals, and the following years are projections.

The data released between the interim and final updates highlighted the faster than anticipated pace of decline in price increases for a number of series. Therefore, the final forecasts for 2024 have been adjusted from the interim update to reflect this change in macroeconomic conditions. The key changes have been to the near term forecasts which have been adjusted downwards to account for lower inflation.

We begin this report by describing the macroeconomic context in terms of global and domestic gross domestic product (GDP), the labour market, and inflation. In Section 3 we introduce the reader to the cost adjustors from a theoretical position. We then provide a brief description of our methodology, and some important caveats and considerations. Most importantly, the adjustors for this year do not include spending on the three waters infrastructure. As in the 2023 update, the Local Government Cost Indices (LGCI) for the 2024 year do not measure the same basket as the previous years, with the spending on water infrastructure removed. This means that direct comparison to previous years will result in significant error. We have provided two additional estimates: a “legacy” series, which includes the same basket of goods as previous years, and a series for just water infrastructure. In Section 5 we provide the index numbers and growth rates of our LGCI. We offer some conclusions in Section 6.

2 Macroeconomic context

This section sets out the macroeconomic context for the 2024 cost adjustor forecasts. It provides an overview of the GDP, labour market, and inflation outlooks for the global and New Zealand economies.

2.1 GDP

Global outlook

The global economy grew by an estimated 2.6 percent in 2023, and the first half of 2024 started off on a positive note. This positivity was fuelled by increased global activity, mainly driven by increased exports from Asia. The key risk of runaway inflation has also been avoided in all advanced economies, prompting interest rate cuts by central banks sooner than previously expected. High interest rates have subdued economic activity over the past three years as monetary policy tightened aggressively to bring inflation under control. Given that monetary policy works with a lag of several months, activity is expected to remain subdued until the rate cuts start to take effect. However, the risk of a hard landing has been avoided. Over the rest of 2024, global economic growth is expected to stabilise within the 2.6 percent to 2.8 percent range, similar to the 2023 GDP growth rate. This is still lower than the average growth rate of 3.2 percent in the pre-pandemic period (2015 to 2019).

Table 1 World GDP growth forecasts

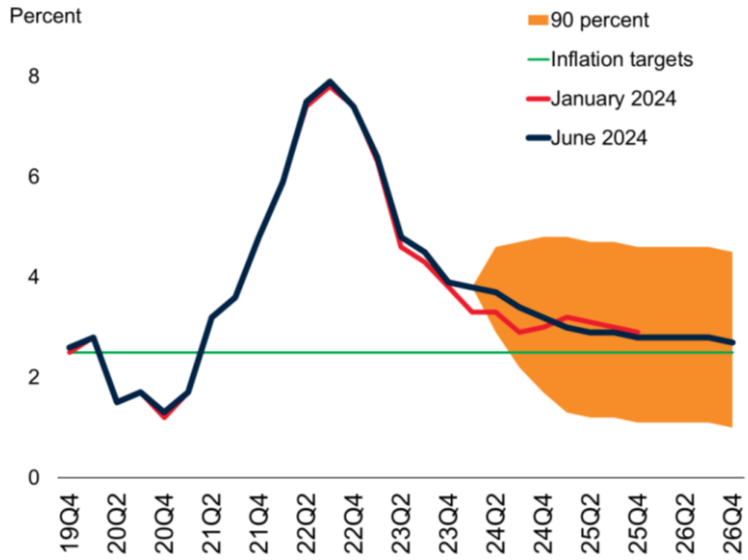
	GDP growth forecast (%)	
	2024	2025
OECD	3.1	3.2
World Bank	2.6	2.7
IMF	3.2	3.3
United Nations	2.7	2.8

From 2025 onwards global growth is expected to start ticking upwards, in the absence of any further unforeseen shocks such as an escalation of geopolitical tensions. World trade growth is expected to recover, in line with global GDP growth, for the first time in the post-pandemic era. This will be driven by increases in goods trade rather than services. There are significant risks during this outlook period, such as an increase in protectionist measures and geopolitical tensions globally. The outcome of the upcoming election in the United States of America (USA) will also be a decisive factor in the direction of trade growth over the next few years.

The growth trajectory of the Chinese economy is expected to diverge from that of the global economy, with GDP growth forecast to fall from 5.2 percent in 2023 to 4.8 percent in 2024. Weakening consumer demand and the brewing debt crisis are contributing to this divergence. As our most important trading partner, an economic downturn in China will inevitably flow on to the New Zealand economy as demand for our exports weakens.

On the plus side, in most advanced economies, inflation is receding faster than anticipated, prompting interest rate cuts by most central banks (Figure 1). Core inflation has largely moderated, however, services inflation remains elevated given its lower sensitivity to interest rates. Average oil prices have declined, but the risk of higher prices remains against the backdrop of heightened geopolitical tensions. Metal prices are likely to remain unchanged as demand for these commodities remains robust in the context of increased electrification and growth in renewable energy infrastructure.

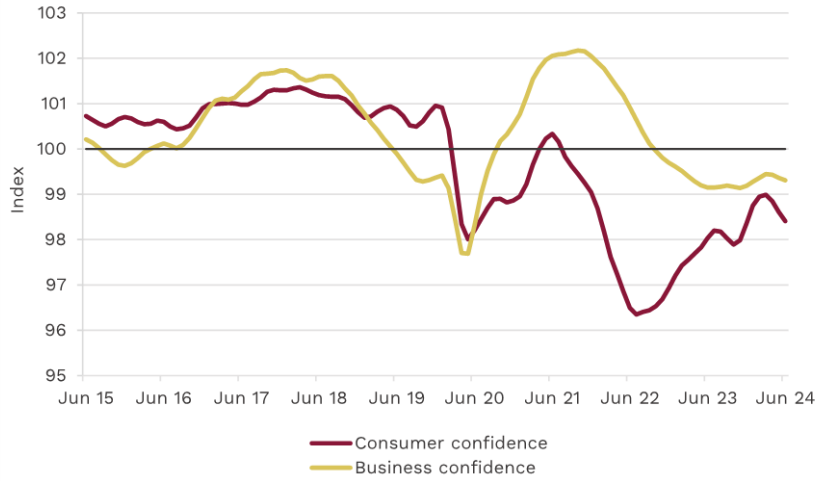
Figure 1 Global consumer price inflation



Source: World Bank

Households are becoming increasingly pessimistic as budgets remain constrained. As anticipated by central banks, the labour market is deteriorating and unemployment is increasing in most advanced economies. Declining job security and high interest rates have impacted consumer confidence, which remains low (Figure 2). Fiscal policy has also shifted into contractionary territory indicating lower support for households globally. However, recent interest rate cuts will provide some respite to households burdened by debts.

Figure 2 OECD standardised business and consumer confidence



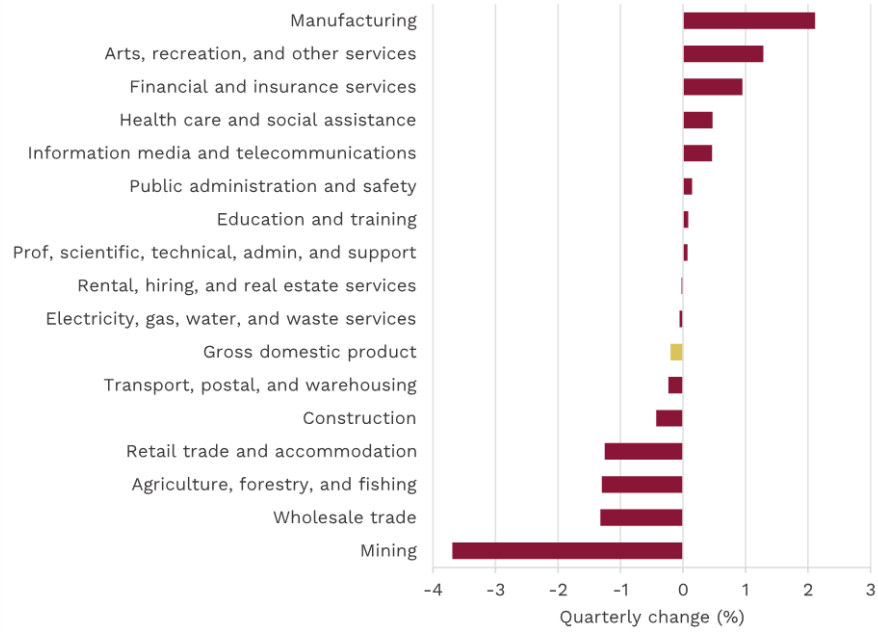
Source: OECD

Looking ahead, the rest of 2024 will be characterised by slow growth, declining inflation, elevated interest rates, and increasing unemployment. Once the effects of lower interest rates start to dissipate through the economy, we can expect economic activity to begin to recover. However, this is unlikely to happen until at least mid-2025.

Domestic outlook

The New Zealand economy shrank by 0.5 percent in the year to June 2024 (Figure 3). The quarterly decrease of 0.2 percent in June 2024 was preceded by a small increase in March 2024 (0.1 percent), zero growth in December 2023, and a contraction in the September 2023 (-0.4 percent) quarter. Stagnant GDP growth coupled with strong population increases over the past year has resulted in a sharp decline in GDP per capita, which fell by 2.5 percent quarter-on-quarter in June 2024. Output growth was weak in all three key sectors of the economy. The goods producing industries were among the few industries that experienced an increase of 1.0 percent in the latest quarter. The primary sector declined by 1.6 percent over the quarter, while the services sector remained stable over the quarter.

Figure 3 GDP by sector, quarterly % change



Source: Stats NZ

Sector-level output performance

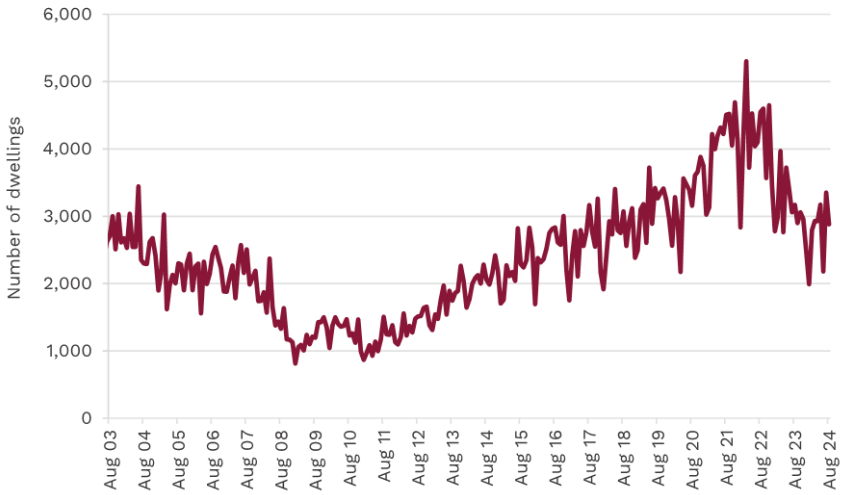
The **primary sector**, which accounts for around seven percent of national GDP, declined by 1.6 percent in the June 2024 quarter, and by 0.5 percent year-on-year. Performance was dragged down by the mining industry, which contracted by 3.7 percent during the quarter, while the agriculture, forestry, and fishing industries saw a smaller quarterly decline of 1.3 percent during this period. A 10.3 percent decline of the forestry and logging industry, in response to lower demand for exports, was the main driver of the decline. Agricultural output also declined, down by 0.4 percent. Fishing, aquaculture and agriculture, forestry and fishing support services was the only area which expanded in the June quarter, up 0.8 percent, after experiencing three quarters of decline in a row.

On an annualised basis, the **goods-producing sector** (accounting for 16 percent of GDP) contracted by 4.0 percent in the year to June 2024. The construction sector alone shrank by 3.5 percent over this period, while the manufacturing sector experienced a 2.1 percent decline in activity. The reduced levels of activity in the goods-producing industries can be explained by the fact that these industries are highly sensitive to interest rates. Rising borrowing costs have dampened consumers' appetite to undertake new construction projects, leading to a decline in the pipeline of work. Increased activity was seen in the June quarter from the wood and paper products, the textile, leather, clothing, and footwear, the petroleum, chemical, polymer, and rubber product, and the

transport equipment, machinery and equipment manufacturing industries. The other manufacturing industries contracted over the quarter following a drop in demand from households and other productive industries.

The number of new consents issued is a leading indicator of what is to come in the construction sector, as it reflects demand for the sector's output. The downturn in this sector is highlighted by the sharp fall in the pipeline of work (Figure 4). In the August 2024 year, the actual number of dwellings consented fell by 20 percent. The number of new dwellings consented per 1,000 residents was just 6.3, compared to 8.1 in the August 2023 year. The biggest annual decreases were in Wellington (down 39 percent), Waikato (down 26 percent), and Auckland (down 24 percent).

Figure 4 Number of new dwellings consented, monthly, seasonally adjusted



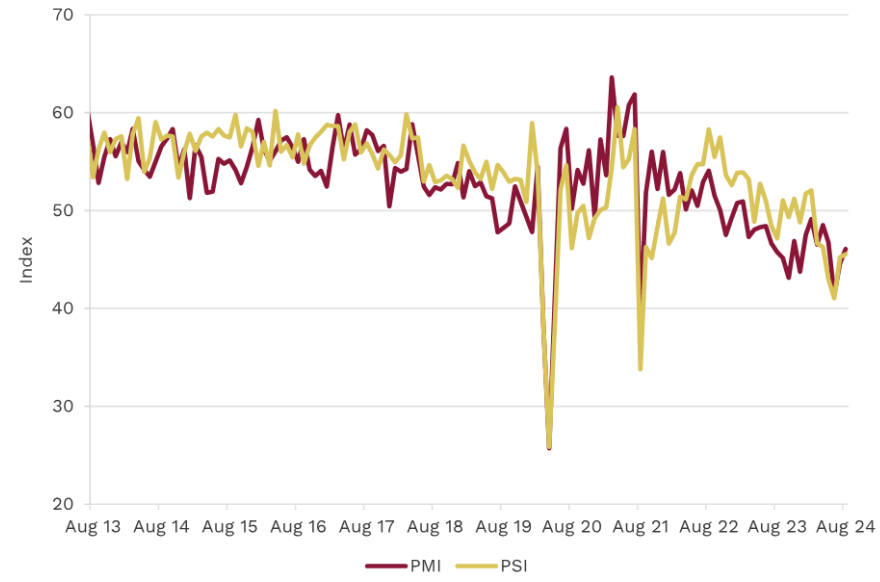
Source: Stats NZ

The latest publication of the Performance of Manufacturing Index (PMI) from October 2024 indicates that the manufacturing sector has been contracting for 19 consecutive months, although at a slower pace since June 2024. The October 2024 PMI was 46.9, below the 50 mark, which indicates a contraction (Figure 5). According to Business NZ, the proportion of negative comments from respondents stood at 63.5 percent in September, which was down from 64.2 percent in August. While all the sub-indices were still below the breakeven mark, production (48) and new orders (47.8) were inching closer to neutrality. The Quarterly Survey of Business Opinion (QSBO) for September 2024 highlighted that the manufacturing sector was the most downbeat, with a net 37 percent of the manufacturers surveyed feeling pessimistic about the general economic conditions over the coming months, compared to a net five percent for all businesses surveyed.

The reduction in domestic demand, and consequently sales, has meant that the pricing power of firms in these industries has taken a hit. Declining profitability and a continuation of depressed

demand points to significant employment cuts on the horizon. A net 55 percent of manufacturers responding to the QSBO reported that they had laid off staff in the last quarter.

Figure 5 PMI and PSI



Source: Business NZ

The **services sector** (accounting for 77 percent of GDP) seems to have held up in the data so far, experiencing 0.3 percent growth in the June 2024 year. However, there are rapidly growing signs of weakness. The sector's output was unchanged in the June 2024 quarter, following a decrease of 0.2 percent in the March 2024 quarter. The biggest declines for the year came from wholesale trade (-4.9 percent); transport, postal, and warehousing (-4.4 percent); and retail trade and accommodation (-3.2 percent), while increases for the year came from public administration and safety (4.8 percent), rental, hiring, and real estate services (4.6 percent), and education and training (2.4 percent).

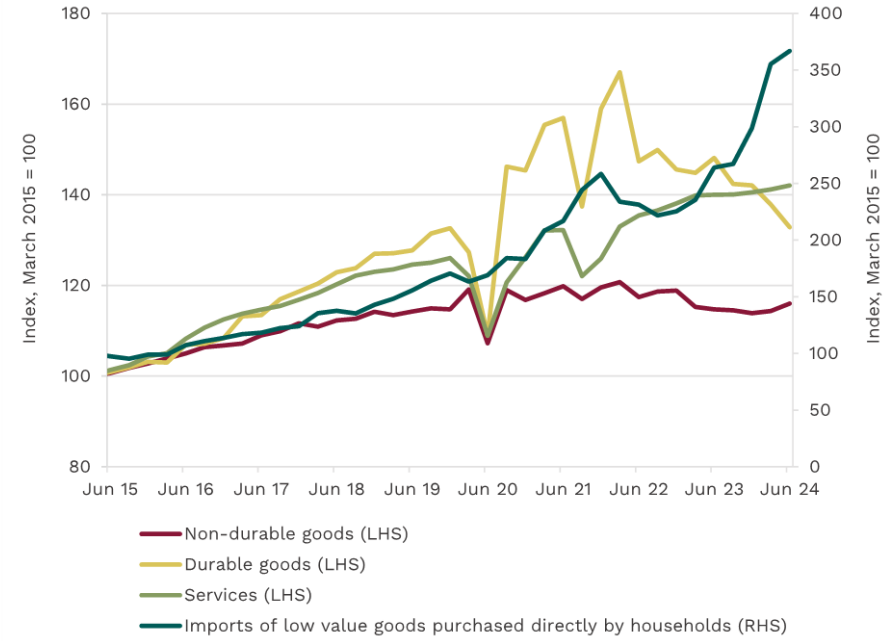
The Performance of Services Index (PSI) for October 2024 shows that a slight improvement may be on the way (Figure 5). The PSI reading for June was 45.5, which was a significant improvement from June's reading of 41. The PSI has been in contraction for six consecutive months, the longest continuous period of decline since the GFC. All five subindices remained in contraction, but showed signs of improvement. The retail trade industry had the weakest PSI reading in the services industries (36.8).

Expenditure breakdown

Expenditure GDP was unchanged during the June 2024 quarter (0.1 percent year-on-year). Household consumption expenditure rose by 0.4 percent during the quarter. Spending on services

accounts for over half of all household expenditure, and this grew by 0.6 percent during the quarter indicating a continuation in some ongoing household demand for services (Figure 6). By contrast, household spending on durable goods has been shrinking, falling by 3.7 percent in the last quarter. Similarly, spending on non-durables also seems to be trending downwards on the whole despite a 1.4 increase in June 2024. Households' imports of low-value goods (mainly from China) have skyrocketed with the entrance of new players in the market. Spending on these goods increased by 3.2 percent in the June 2024 quarter, following a 19 percent increase and a 12 percent increase in the previous two quarters.

Figure 6 Household consumption expenditure



Source: Stats NZ

Central government expenditure was unchanged during the quarter, although it is likely it will start to fall again given the current government's goal of reducing government expenditure. Local government expenditure was up by 1.0 percent. Business investment fell by 0.4 percent, particularly investment into plant, machinery, and equipment (-9.8 percent) and transport equipment (-6.8 percent).

On the trade front, exports of goods and services increased by 1.5 percent, driven mainly by a 13.9 percent increase in goods exports. Service exports, by contrast, were only up by 4.5 percent. Imports of goods and services increased by 4.3 percent during the quarter.

GDP outlook

With the decline in GDP in the June 2024 quarter, the question will be whether this decline will be continued into the September quarter, with a technical recession a possibility, or will activity manage to increase. The latest QSBO showed that businesses are downbeat, with investment and employment intentions dropping as a result of contracting profits. Household spending, although appearing robust, is unlikely to continue to grow, especially in the face of a loosening labour market. Migration, which has so far been a key driver of growth, is falling. This means demand, as well as supply (production), are both on the decline. We have pencilled in zero growth for the September 2024 year (Appendix B).

2.2 The labour market

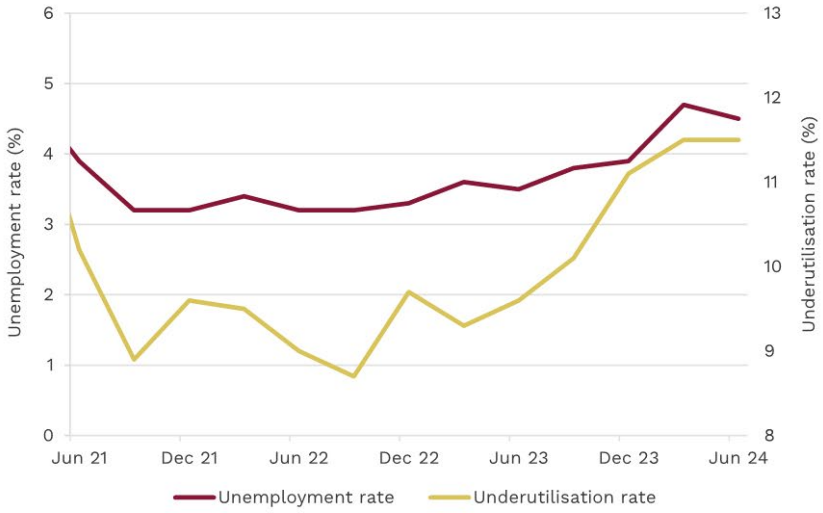
Despite tighter monetary policy settings, the labour market has held up surprisingly well until now. However, all indicators point to a rapidly softening labour market. In June 2024, the labour force participation rate fell from 71.8 percent to 71.3 percent, the lowest in two years. As competition for jobs increases, more people may become unemployed, or underutilised, while others exit the labour market altogether in favour of other activities such as education.

Spare capacity

After a period of unprecedented tightness in the labour market, the situation is turning as the Reserve Bank's efforts to lower economy-wide inflation are paying off. New Zealand, like most advanced economies, has not had rapid deceleration of inflation at the cost of detrimentally high unemployment. This is likely to be because employers have so far been holding on to their staff despite low activity, given the previous difficulties they experienced in finding workers. However, this may now be changing in the face of a prolonged period of subdued activity.

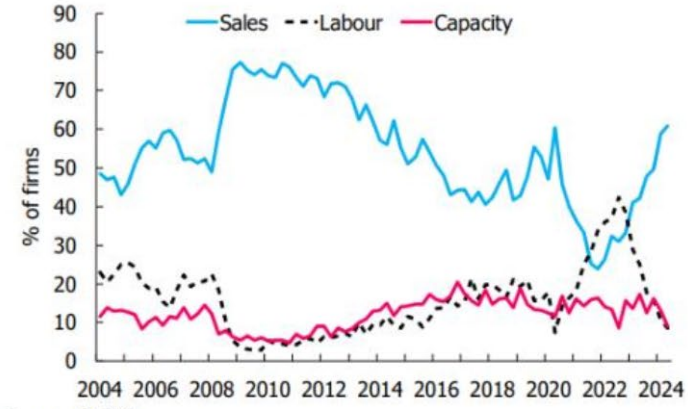
In the June 2024 quarter, unemployment stood at 4.6 percent, compared to four percent in the December 2023 quarter (Figure 7). As the effects of restrictive monetary policy continue to impact economic activity, unemployment is expected to continue to increase over the rest of the year. Underutilisation, another important measure of spare capacity, rose to 11.5 percent in the June 2024 quarter, up from 11.1 percent in December 2023.

Figure 7 Unemployment and underutilisation rates (%)



The number of online job advertisements also continued to fall, reflecting reduced demand for workers. Advertisements were down 33 percent over the June 2024 year. On a quarterly basis, the decline was 18.9 percent. Gisborne/Hawke's Bay (45 percent), Nelson/Tasman (26.7 percent), Northland (24 percent), and Bay of Plenty (21.5 percent) had the largest quarterly declines in jobs advertised online. Furthermore, according to the QSBO, labour is no longer the most constraining factor for businesses, indicating a drop in labour demand (Figure 8).

Figure 8 Economy wide factor constraints



Source: NZIER

Workers in the manufacturing and construction sectors, where activity is at particularly low levels, will continue to be the most impacted. The biggest quarterly declines in job advertisements were in the hospitality, health, and manufacturing industries. Looking ahead, further softening in the labour market is likely to continue. The Reserve Bank expects economy-wide unemployment to peak at 5.1 percent in 2025.

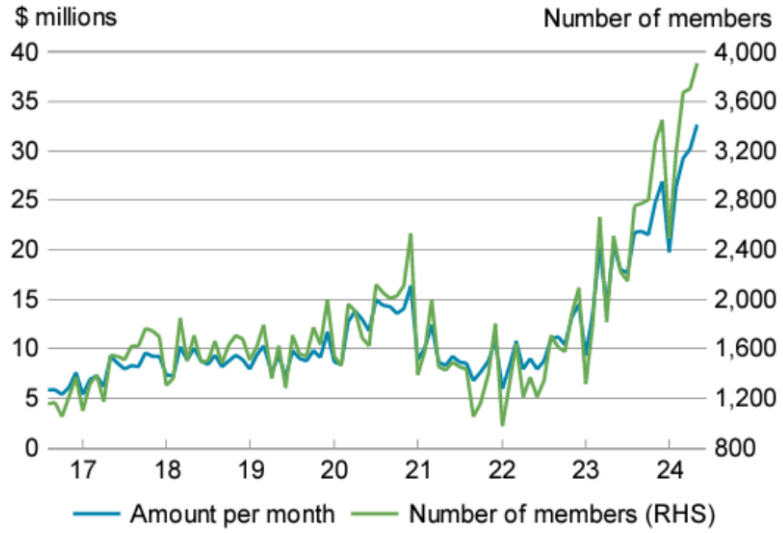
Negotiating power has now switched back to favour employers over employees, and we can expect labour costs to start declining once the effects of past wage negotiations and previous labour market tightness start to wear off. Labour costs increased by 4.3 percent during the June 2024 year, and 1.2 percent on a quarterly basis. Breaking down the data by occupation shows that no occupation saw a decline in labour costs for the quarter, while labour costs for health professionals (3.4 percent), and education professionals (2.8 percent) experienced the largest increases, reflecting the results of wage negotiations in these sectors.

Households are under increased financial pressure

Households are becoming increasingly pessimistic, with rising costs and the fear of unemployment looming. Consumer sentiment is at a 20-year low as high interest rates limit purchasing power. Financial hardship may also be spreading.[1] According to data released by Centrix, the number of consumers falling behind on debt repayments increased by 16,000 in May to 474,000 people. Mortgage repayments (44 percent) is the leading cause of these hardships, followed by credit card debt (29 percent), and personal loan repayments (19 percent). KiwiSaver withdrawals, on the grounds of financial hardship, reached a new record of $32.7 million in May 2024, up 60 percent on May 2023 (Figure 9). Households are increasingly pessimistic about job security and employment. The quarterly Westpac-McDermott Miller Employment Confidence Index fell by 2.2 points from 91.4 to 89.2 in the September 2024 quarter. This was the lowest reading since the country was emerging from the first Covid-19 lockdown in 2020. The biggest quarterly decline was seen in people's perceptions of current job opportunities, which fell by 14.3 points to a net -50.4 percent.

[1] https://www.treasury.govt.nz/sites/default/files/2024-07/feu-5jul24.pdf

Figure 9 KiwiSaver withdrawals for financial hardship



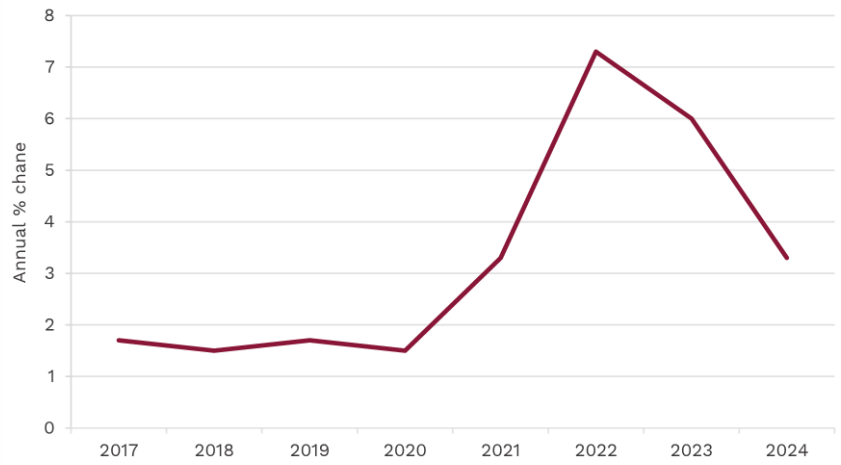
Source: IRD, NZ Treasury

2.3 Inflation

The inflationary outlook for 2024 is looking increasingly positive, with a maintained decrease in the global and domestic inflation rate, to the relief of inflation targeting regimes worldwide. In New Zealand, the official rate of consumer inflation is measured by Stats NZ's Consumers Price Index (CPI). The CPI tracks the price of a basket of household goods and services over time, reporting on a quarterly basis.

Key economic developments this year have occurred against the backdrop of decreasing inflation. Inflation decreases, domestic and globally, have been broad-based and have impacted nearly every sector. In June 2024, New Zealand's annual CPI inflation came in at 3.3 percent. This was quite a significant drop from the six percent annual rate of inflation recorded in June 2023. Much of the decrease in inflation was a result of a fall in the inflation rate for tradables, which reflects a slowdown in price increases internationally. Figure 10 shows the annual price levels changes; New Zealand's official inflation rate.

Figure 10 Annual inflation rate, June years (%)



Source: Stats NZ

With the inflationary outlook looking so positive, it might be time to start the price stability celebrations. The RBNZ, in its latest review of the OCR in October 2024, dropped the interest rate to 4.75 percent, after dropping it to 5.25 percent in September 2024. However, key aspects of the messaging suggest further rate cuts in November 2024 are likely. The Bank expressed confidence that the key economic indicators point to a reduction in underlying inflationary pressure. It also expects headline inflation to return to within the 1-3 percent target range in the second half of this year.

Internationally, the European Central Bank and the Bank of Canada have already started to cut rates, with the first cuts having been announced in June. The US Federal Reserve is expected to follow suit later this year. However, the RBNZ will be cautious in how strongly it cuts the OCR. Interest rates are unlikely to drop to the levels of 2020 and 2021 (Figure 11). The near-zero OCR during these years left little room for the Bank to spur aggregate demand in the economy to lift activity. It will not want to be in the same position again.

Global factors

Global inflation is now nearing target range for almost all inflation-targeting economies. Year-on-year inflation in the OECD (excluding Türkiye) was 2.7 percent in August 2024. It is important to note that declining inflation does not mean prices are falling, it just means that prices are rising at a slower rate. The lower rate of inflation is driven by falling commodity prices, decreasing energy costs, and supply chain recovery post-pandemic. The rest of this section will discuss key areas where price pressures are easing or have disappeared, and those that may constitute new or maintained risks.

The upside

Upward pressure from wages has subsided as the labour market weakens. This has, in part, been driven both by record high migration rates as well as by the strong growth in labour force participation rates. The EU, UK, USA, and Australia have all had rising migrant workforces over the past two years, leading to a strong labour market for employers. The decline in business activity is resulting in an even greater shift in the balance of power in employers' favour.

Other inflationary pressures have also become subdued. Oil prices have declined by over 10 percent since July as demand from major buyers, such as China, remains weak. The market also expects supply to exceed demand for oil over the next year. According to the OECD, if oil prices remain at their current level, global headline inflation could be reduced by around 0.5 percentage points over the coming year.

The downside

While goods price inflation has abated, services price increases will need to decline further to bring inflation back within target range. RBNZ research has shown that services price inflation is higher and more broad-based in New Zealand compared to other advanced economies. Therefore, return of inflation to target range depends, to a large extent, on the trajectory of prices for services.

Another factor that may maintain higher than desired levels of inflation is increasing geopolitical instability. Rising tensions could create inflationary shocks, which could flow through to higher oil prices, or disrupt shipping trade routes. Increasing trade tensions and retaliatory tariffs will also contribute to higher prices for consumers if the risk materialises.

Domestic factors

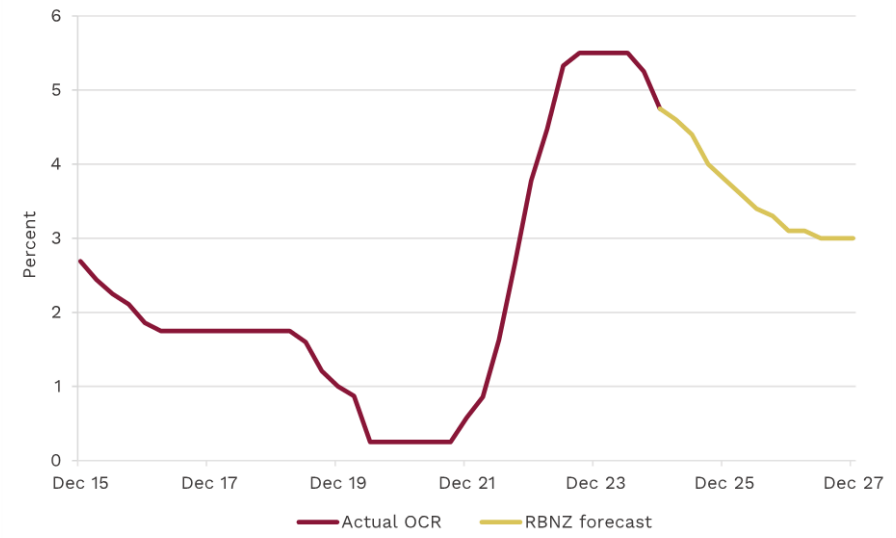
The worst of inflation is behind us. International factors, such as increased supply and lower energy prices have resulted in decreases to the pace of imported inflation. This has contributed to easing headline inflation in New Zealand. Low levels of GDP growth, and restrictive monetary policy, have also acted to subdue domestic demand and decrease demand-driven inflation.

The Reserve Bank, in their latest monetary policy statement, chose to drop the OCR down to 4.75 percent rate. While they noted in their statement that many of the international factors causing inflation have eased, domestic factors are now the primary drivers of inflation. There are also new risks, including the inflationary effects of the tax cut policy, and the risk of price setting behaviour.

The upside

The RBNZ and other industry forecasts have signalled confidence that the inflation rate will return to within target levels by the second half of 2024. The more open monetary policy, with the OCR being dropped to 4.75 percent, is the result of the achievement of the RBNZ's desired effects; a reduction in domestic demand and a lowering in the rate of consumer price inflation.

Figure 11 OCR and RBNZ forecast as of October 2024



Source: RBNZ and BERL analysis

The labour market also appears to be easing, with record high levels of immigration over the past year and a rising rate of unemployment. These two factors have contributed to the easing in the labour market, allowing job vacancies to be filled more easily, and the competitive wage bidding for workers to reduce. Annual wage cost inflation, as measured by the labour cost index, was 4.3 percent to the June 2024 quarter. The sectors with the highest wage cost inflation growth were the health care and social assistance sector, with an inflation rate of 8.1 percent. The education and training sector has also had significant wage cost increases of 7.8 percent overall, as has the public administration sector with 4.9 percent overall. However, this may be the result of a recent string of renegotiated pay packages for large areas of the public sector.

The biggest relief for New Zealand consumers will be likely to come from the reduced inflation rate of tradable goods. Food prices have decreased by 0.3 percent in the July quarter, the first decrease in six years. Other tradable goods and services are undergoing similar price decreases. This reflects an increased supply capacity both domestically and globally, as an abundance of goods and services eases cost pressures. The supply chain stabilisation, despite being tenuous, also helps decrease the cost of imports into New Zealand.

Insurance costs have also increased by 14 percent annually. This has contributed to inflation, as insurance companies pass costs onto customers. Insurers have had to readjust rates to reflect the increasing risks of insurance, including natural disasters and social changes. These factors should now be priced into insurance, so it is unlikely that the rate of insurance cost increases will continue to be so high.

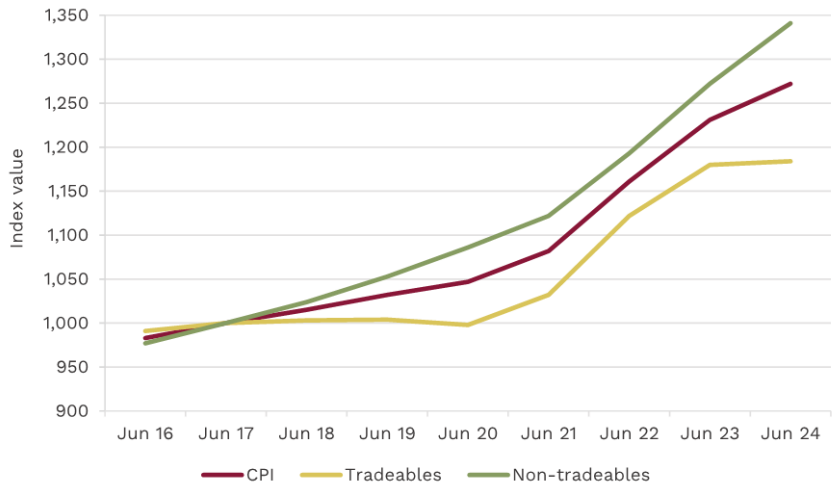
The downside

Despite the positive outlook for inflation, there are some risks that are worth consideration. Key amongst these are migration, non-tradable goods, government policy, and the unstable macroeconomic environment. These factors, alone or in combination, may prevent a return to optimal levels of inflation.

Immigration has an ambiguous inflationary impact, as it has a dual effect on the economy impacting both the demand and supply of goods and services. The relative impact depends on a range of factors. On the one hand, new migrants add productive capacity to the economy, contributing vital skills to be used by industry, allowing firms to increase the production of goods and services. In addition, migrants increase labour supply, easing the tight labour market and reducing wage inflation, as they compete with domestic workers for jobs. On the other hand, high immigration rates increase the demand for existing goods and services, such as housing and infrastructure. If supply remains unchanged, this new demand will bid up the prices, resulting in demand-pull inflation. Given that the capacity of the economy to produce new goods and services is declining, the significant increase in population over the past year may result in a higher risk of demand-pull inflation.

Non-tradables are also a point of concern for inflation rates. Non-tradables are the goods and services which are not easy to trade, for example housing and capital infrastructure. While tradables had an annual inflation rate of 0.3 percent in the June 2023 to June 2024 year, non-tradables inflation was 5.4 percent over the same period. This indicates that most of the inflation currently is being caused by non-tradables (Figure 12).

Figure 12 CPI, tradables, and non-tradables inflation. Index base: June 2017 quarter



Source: Stats NZ

Recent government policies, for example reintroducing interest deductibility on home loans, may increase demand for non-tradable goods and services. While much of fiscal policy is contractionary other aspects of policy might, in practice, contribute to an increase in domestic demand. The major unknown is the impact of the proposed tax bracket readjustments and whether they will have an inflationary effect on the economy.

3 Understanding the cost adjustors

In this section we summarise the main idea behind the cost adjustors and present a brief overview of our methodology.

3.1 What is the Local Government Cost Index?

The Local Government Cost Index (LGCI) is a composite index that measures the changes in the prices of a basket of goods and services that are purchased by local governments in New Zealand. The intention is to give local government administrators a robust, defensible, and replicable estimate of how costs faced by local government are expected to increase in the following 11 years, given the current macroeconomic conditions. This is useful for both the planning and the auditing process.

3.2 Cost adjustors versus CPI inflation

The CPI and the LGCI share a common purpose: to track the movements in the price level of a particular basket of goods and services used by their intended audience. The difference between the two is their intended audience.

The CPI is used by policymakers to understand the movements in the general price level as experienced by households. The intention of the CPI is to understand what households are experiencing in terms of the price increases in the goods and services they buy. The CPI tracks the price of a basket of goods and services purchased by the average household, for example food, power, fuel, and rent. This understanding is used to inform policymaking. The RBNZ conducts monetary policy in New Zealand through the tightening or loosening of the OCR. The OCR is the RBNZ's main policy tool to keep the CPI within the target range of 1-3 percent.

By contrast, the LGCI is designed to understand changes in local authority costs, i.e., it tracks the price of a basket of goods and services purchased by the average local authority. The mix of goods and services purchased by local authorities is markedly different from the basket of goods and services represented in the CPI. For example, some of the key inputs that local authorities purchase include staff labour, contractor services, physical infrastructure components, and maintenance services.

There are several macroeconomic drivers which are common to the CPI and LGCI, namely money supply growth, immigration, and the global macro environment. However, there are also drivers that are specific to the LGCI, and those that are specific to the CPI.

Historically, the LGCI has always grown more slowly than the CPI. This reflects the difference in bargaining power between local authorities and households. It also reflects and underscores the fact that the indices measure different baskets of goods and services and are built for different purposes.

3.3 Three waters infrastructure

Given the ongoing uncertainty around the ownership of water infrastructure by local councils, we have continued with the modelling approach used last year. Therefore, in this year's update, we adjust the balance of the LGCI to remove the components that measure the cost of water infrastructure. This means that the 2024 LGCI update is not comparable to previous years' updates where water infrastructure was not removed from the indices. We provide both the LGCI, as well as an estimate of the water infrastructure component of the LGCI, to assist local authorities in financial planning and reporting. We also provide an estimate of the LGCI using the legacy basket of goods, which is comparable to prior years. We call this the "legacy LGCI".

We stress that, because we have removed the three waters infrastructure costs and rebalanced the LGCI, it is not possible to compare the 2024 update of the LGCI to pre-2023 LGCI on its own.

The LGCI's new basket

This adjustment to account for three waters means that the LGCI in the 2024 update now measures a different basket of goods and services compared to the LGCI from previous updates pre-2023. The index still measures the cost increases for local authorities, but because the basket of goods and services local authorities buy has changed, so too has the LGCI.

We can make another comparison to the CPI. Periodically, Stats NZ will re-adjust the weights of each good and service (apples, beer, petrol, toys, etc.) in the basket of the "average consumer". These adjustments are based on surveys conducted by Stats NZ on how consumers allocate their spending over these goods and services. We have, in essence, completed a similar exercise. With some assumptions about how local authorities will allocate their budgets now that the expenditure associated with three waters is no longer in scope, we have created a new basket for the "average local authority".

4 Understanding our forecasts

4.1 What it means to model price indices

Econometric modelling can often appear arcane and impenetrable. The perception that the econometric model is a black box gives users of the data a great deal of confidence in the results. However, it also creates some unjustified expectations.

The models we choose to use come from a rich history of academic research into probability theory and statistics. This literature stretches back into the mid-20th century. The earlier research focused on the theoretical properties of the models. As access to computers and advanced statistical software has increased, we find that the latter research looks more into applying these models, and numerical optimisation. It is accurate to say that the models have been rigorously tested and found to be robust, in the pure sense of the word, by decades of research.

In our view, these models are the best currently available. While there are some alternatives (especially in the "black box" category) these come with trade-offs that we find undesirable. We apply these models to data that is sourced either from New Zealand official statistics, or official statistics of other jurisdictions (in the case of oil prices). These are all publicly available sources, and are the only sources we know to exist that describe the input prices for local authorities.

Recently, alternative estimates of how local authorities' costs will evolve over time have been made available. We will not speak to the methodology behind these estimates except for noting that the input data used for whatever model is ultimately chosen must have been sourced from Stats NZ. The value add of the LGCI is the reduction in duplication of effort by different local authorities employing different cost forecast methodologies through the provision of a consistent set of estimates.

4.2 Methodological overview

This section provides a brief overview of the methodology used to develop and forecast the cost adjustor series.

Input data

The process begins with eight price indices measuring the input prices incurred by local authorities. These eight indices make up the LGCI basket:

- Producer Price Index (inputs) – local government and administration
- Producer Price Index (inputs) - arts and recreation services
- Producer Price Index (inputs) - water, sewer, drainage, and waste services
- Capital Goods Price Index - earthmoving and site work
- Capital Goods Price Index - pipelines
- Capital Goods Price Index - reclamation and river control
- Labour Cost Index - private sector wages

- Labour Cost Index - local government wages

The basket of goods and services without three waters infrastructure excludes the following series:

- Producer Price Index (inputs) - water, sewer, drainage, and waste services
- Capital Goods Price Index - pipelines
- Capital Goods Price Index - reclamation and river control

The following macroeconomic explanatory variables are used within the modelling process:

- Unemployment
- Oil prices
- Residential consents
- Non-residential consents
- CPI
- Real GDP
- Broad money (M2).

In previous years, we have relied solely on tier one statistics provided by Stats New Zealand, or data compiled by the RBNZ, for domestic series. This year, following feedback from local government professionals, our projections were informed by series created by other Crown agencies, such as Waka Kotahi. The Waka Kotahi series we considered as part of this year's analysis included:

- Construction index
- Professional services index
- Construction other than structures index.

These were not explicitly modelled as these series are constructed using the same Stats NZ indices already used within our models. However, the forecasts of these were used to inform our judgement on the performance of the roading, transport, and labour components of the LGCI, and any adjustments required. This process ensures a better alignment of these components with other estimates used by local government professionals.

Modelling

A model is built for each of the five input price indices that contains some combination of the explanatory variables. We decide which variables to include in each model using a robust statistical method. As explained later in this section our forecasts include some subjectivity. Every model contains at least CPI, GDP, and unemployment as explanatory variables.

In the 2024 update we have adjusted our methodology to allow for the disruption caused by the pandemic in 2020. With this new model structure, the macroeconomic variables were found to have high explanatory power in our statistical tests, adding statistical robustness to our estimates.

Forecasting

We forecast the explanatory variables using a combination of well understood statistical techniques, and subjective economic forecast techniques. These forecast values are plugged into the statistical models of the input price indices to create forecasts of these five indices.

Input price indices to adjustors

We combine our five input price indices (actual values and forecast values) into five cost adjustor indices:

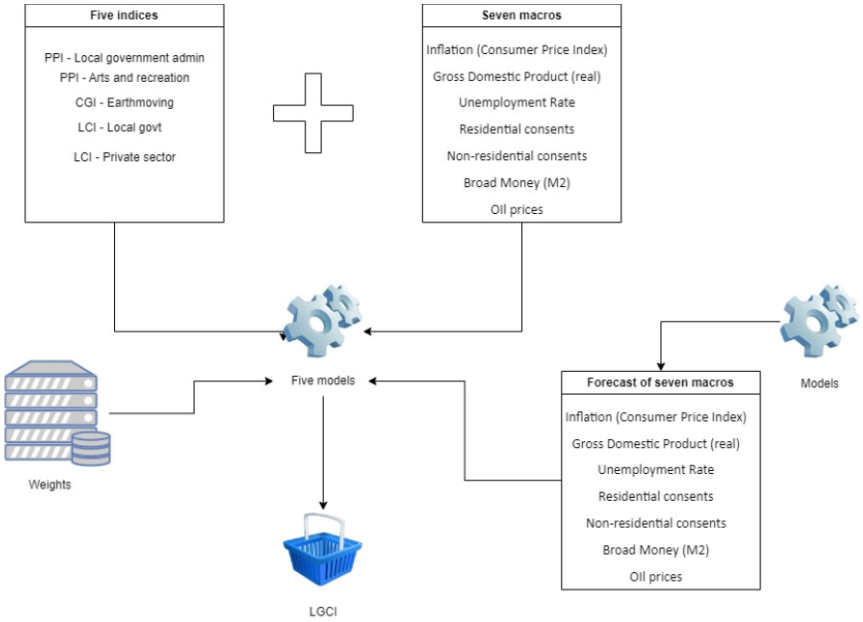
- Planning and regulation
- Roading
- Transport
- Community
- Waste.

Each adjustor index is a linear combination of input price indices, with weights taken from an analysis of local government financial statements to understand the cost structures of local government. These five adjustors are further combined into three aggregate indices:

- Capital expenditure (Capex)
- Operating expenditure (Opex)
- Total.

The methodology is summarised is Figure 13.

Figure 13 LGCI methodology overview



4.3 Caveats

Price increases compound

In everyday discussions, and particularly in the news media, it is common to refer to the rate of CPI inflation slowing down, especially after periods of high inflation. It is important to remember that a low rate of increase in the CPI does not undo any previous increases in the actual prices of goods and services. It is still an increase, and the price increases compound each year.

This is also true of the LGCI. Our forecasts in this update show the rapid increases in costs experienced between 2021 and 2024. They then show that the rates of increase start to fall to what our model indicates is a long run structural norm. However, this does not mean that costs faced by local government will fall, it only means that the prices will increase more slowly. It also does not undo the significant cost increases that occurred between 2021 and 2024.

Uncertainty increases over time

The model behind our forecasts utilises a process based on past observations of a given variable to explain present, and forecast future, observations. This process means that uncertainty in early forecast periods ripples through later forecast periods and is amplified as it does so. We suggest that the first few years of the forecasts are taken as being reasonably likely, while the latter few periods (particularly from the year 2028 onward) be taken as indicative.

Subjectivity in forecasting

When designing the model for each price index, we include macroeconomic variables, such as GDP, unemployment, and CPI inflation. We then forecast these variables using a combination of subjective economic analysis, and statistical modelling. We do so because our forecasts of the LGCI are intended to be a balance of statistical modelling augmented by subjective and informed economic forecasts.

Comparison to previous updates is not advised

We reiterate that because we have rebalanced the basket of the LGCI to remove spending on water infrastructure, this year's LGCI is a completely different product. This means that direct comparison to pre-2023 forecasts will result in significant error.

Insurance costs are not explicitly included

As of 2024, local authorities are experiencing significant cost increases in insurance premiums. The LGCI is not designed to model costs at a granularity sufficient to account for this effect. However, the raw data we use to construct the LGCI (the producer price indices) does include insurance premiums as an input. Thus, the effect of these price increases is, to some extent, reflected in the series. We refer the reader to methodology documentation produced by Stats NZ available at https://www.stats.govt.nz/methods/producers-price-index-concepts-sources-and-methods

5 Indices and adjustors

5.1 Price indices

Table 2 Local Government Price Indices, 1996 – 2035, index values

	Index values (2024 = 1000)							
Year	PPI inputs - Local government administration	PPI inputs - Arts and recreation services	PPI inputs - Water, sewer, drainage, and waste services	CGI- Earthmoving and site work	CGI - Pipelines	CGI - Reclamation and river control	All Salary and wage rates - Local govt sector	All Salary and wage rates - Private sector
1996	480	517	346	400	363	524	516	533
1997	475	523	347	389	363	528	526	545
1998	479	537	350	390	372	534	535	554
1999	479	543	354	390	374	526	542	562
2000	496	551	375	404	392	534	549	569
2001	521	573	402	433	414	556	560	580
2002	530	587	393	453	422	569	575	592
2003	538	602	407	459	433	584	588	605
2004	559	618	430	479	459	592	600	618
2005	584	636	448	503	503	617	613	635
2006	614	660	498	517	532	642	637	653
2007	626	680	515	552	547	663	654	674
2008	689	721	565	581	565	705	684	697
2009	694	739	582	618	626	730	701	716
2010	703	746	603	632	634	740	716	727
2011	720	760	621	656	670	755	731	741
2012	736	769	645	699	690	778	749	757
2013	756	774	656	721	611	793	763	770
2014	766	781	664	744	636	808	777	784
2015	769	785	690	755	666	830	794	798
2016	772	799	708	775	661	836	807	811
2017	788	813	716	803	671	841	821	824
2018	805	831	728	807	741	846	836	841
2019	831	846	762	840	736	861	851	860
2020	839	859	783	849	758	875	869	875
2021	861	875	808	860	796	894	879	894
2022	926	928	891	932	916	944	908	925
2023	970	963	943	978	975	984	954	965
2024	1000	1000	1000	1000	1000	1000	1000	1000
2025	1026	1036	1059	1032	1035	1015	1040	1035
2026	1052	1063	1118	1067	1071	1031	1076	1068
2027	1078	1089	1178	1106	1110	1050	1111	1100
2028	1104	1114	1236	1144	1146	1069	1142	1129
2029	1127	1135	1293	1182	1182	1089	1172	1158

2030	1149	1156	1348	1220	1216	1108	1200	1185
2031	1171	1178	1393	1256	1250	1128	1226	1211
2032	1193	1199	1435	1293	1283	1147	1252	1237
2033	1216	1220	1470	1329	1315	1167	1277	1262
2034	1238	1241	1504	1364	1346	1186	1301	1286
2035	1260	1262	1538	1399	1378	1206	1324	1309

Table 3 Local Government Price Indices, 1996 - 2035, pa % changes

	pa % changes							
Year	PPI inputs - Local government administration	PPI inputs - Arts and recreation services	PPI inputs - Water, sewer, drainage, and waste services	CGI-Earthmoving and site work	CGI - Pipelines	CGI - Reclamation and river control	All Salary and wage rates - Local govt sector	All Salary and wage rates - Private sector
1996	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
1997	-1.0	1.2	0.4	-2.7	0.0	0.7	1.9	2.2
1998	0.8	2.6	0.9	0.3	2.5	1.3	1.6	1.7
1999	0.0	1.3	1.2	0.0	0.5	-1.5	1.5	1.6
2000	3.6	1.5	5.9	3.7	4.8	1.5	1.3	1.3
2001	5.0	3.9	7.3	7.2	5.6	4.1	2.0	1.9
2002	1.7	2.5	-2.3	4.5	1.8	2.3	2.6	2.1
2003	1.4	2.5	3.6	1.5	2.6	2.7	2.3	2.2
2004	3.9	2.6	5.5	4.4	6.0	1.4	2.0	2.2
2005	4.5	2.9	4.3	5.0	9.6	4.2	2.1	2.6
2006	5.1	3.9	11.0	2.7	5.8	4.0	3.9	2.9
2007	2.0	2.9	3.4	6.7	2.8	3.3	2.7	3.2
2008	10.0	6.0	9.7	5.3	3.4	6.2	4.5	3.4
2009	0.7	2.5	3.0	6.3	10.8	3.6	2.5	2.7
2010	1.3	0.9	3.6	2.4	1.2	1.4	2.1	1.5
2011	2.4	2.0	3.1	3.7	5.7	2.0	2.2	2.0
2012	2.3	1.2	3.8	6.5	3.0	3.1	2.4	2.1
2013	2.7	0.6	1.7	3.1	-11.6	1.9	1.9	1.8
2014	1.3	1.0	1.2	3.3	4.2	2.0	1.8	1.8
2015	0.5	0.5	4.0	1.5	4.7	2.7	2.2	1.8
2016	0.4	1.8	2.6	2.7	-0.7	0.8	1.7	1.6
2017	2.1	1.7	1.0	3.6	1.4	0.6	1.7	1.6
2018	2.2	2.3	1.8	0.6	10.5	0.6	1.8	2.1
2019	3.2	1.7	4.6	4.0	-0.6	1.7	1.8	2.2
2020	1.0	1.6	2.8	1.1	2.9	1.6	2.1	1.7
2021	2.6	1.9	3.1	1.3	5.0	2.2	1.1	2.2
2022	7.5	6.1	10.3	8.5	15.1	5.6	3.4	3.4
2023	4.8	3.7	5.8	4.9	6.5	4.2	5.1	4.3
2024	3.1	3.9	6.1	2.2	2.5	1.6	4.8	3.6
2025	2.6	3.6	5.9	3.2	3.5	1.5	4.0	3.5
2026	2.5	2.6	5.6	3.4	3.5	1.6	3.5	3.2
2027	2.5	2.5	5.3	3.6	3.6	1.8	3.2	3.0
2028	2.4	2.2	5.0	3.5	3.3	1.8	2.8	2.7
2029	2.1	1.9	4.6	3.3	3.1	1.9	2.6	2.5
2030	2.0	1.9	4.2	3.2	2.9	1.8	2.4	2.4
2031	1.9	1.8	3.4	3.0	2.8	1.8	2.2	2.2
2032	1.9	1.8	3.0	2.9	2.6	1.7	2.1	2.1
2033	1.9	1.8	2.4	2.8	2.5	1.7	2.0	2.0

2034	1.8	1.7	2.3	2.6	2.4	1.7	1.9	1.9
2035	1.8	1.7	2.3	2.6	2.4	1.7	1.8	1.8
20 year average % pa	*2.5*	*2.4*	*4.1*	*3.1*	*3.7*	*1.9*	*2.6*	*2.5*

Table 4 Local Government Price Indices, cumulative change

	Cumulative change (since 2024)							
Year	PPI inputs - Local government administration	PPI inputs - Arts and recreation services	PPI inputs - Water, sewer, drainage, and waste services	CGI- Earthmoving and site work	CGI - Pipelines	CGI - Reclamation and river control	All Salary and wage rates - Local govt sector	All Salary and wage rates - Private sector
2025	2.6	3.6	5.9	3.2	3.5	1.5	4.0	3.5
2026	5.2	6.3	11.8	6.7	7.1	3.1	7.6	6.8
2027	7.8	8.9	17.8	10.6	11.0	5.0	11.1	10.0
2028	10.4	11.4	23.6	14.4	14.6	6.9	14.2	12.9
2029	12.7	13.5	29.3	18.2	18.2	8.9	17.2	15.8
2030	14.9	15.6	34.8	22.0	21.6	10.8	20.0	18.5
2031	17.1	17.8	39.3	25.6	25.0	12.8	22.6	21.1
2032	19.3	19.9	43.5	29.3	28.3	14.7	25.2	23.7
2033	21.6	22.0	47.0	32.9	31.5	16.7	27.7	26.2
2034	23.8	24.1	50.4	36.4	34.6	18.6	30.1	28.6
2035	26.0	26.2	53.8	39.9	37.8	20.6	32.4	30.9

5.2 Adjustors

The following tables summarise three versions of the LGCI adjustors. We recommend using the updated version of LGCI, without water infrastructure.

LGCI without water infrastructure

Table 5 Local Government Cost Adjustor, 1996 – 2035, index values

Index values (2024 = 1000)

Year	Planning & regulation	Roading	Transport	Community	Waste
1996	480	444	467	480	457
1997	477	437	463	481	456
1998	482	440	466	489	461
1999	483	441	468	494	465
2000	498	456	483	504	475
2001	521	482	506	527	495
2002	532	496	519	543	513
2003	540	504	527	555	523
2004	560	523	546	572	538
2005	583	547	569	591	557
2006	611	568	594	612	576
2007	625	593	613	636	602
2008	681	635	662	672	632
2009	690	657	677	696	659
2010	700	669	688	706	673
2011	717	689	706	724	693
2012	735	719	729	744	723
2013	754	739	748	756	741
2014	766	756	762	769	760
2015	772	764	770	777	774
2016	778	777	778	793	791
2017	795	799	797	811	812
2018	810	809	811	824	821
2019	835	838	836	844	845
2020	845	847	846	857	859
2021	864	863	864	871	869
2022	923	929	924	927	921
2023	968	974	970	967	967
2024	1000	1000	1000	1000	1000
2025	1029	1030	1030	1035	1036
2026	1057	1061	1059	1066	1072
2027	1085	1094	1090	1097	1108
2028	1113	1126	1120	1127	1143
2029	1138	1157	1147	1154	1177
2030	1162	1188	1174	1182	1210

2031	1186	1217	1200	1208	1242
2032	1210	1247	1227	1235	1273
2033	1234	1277	1253	1261	1303
2034	1257	1305	1278	1287	1333
2035	1280	1334	1304	1313	1362

Table 6 Local Government Cost Adjustor, 1996 – 2035, pa % changes

Pa % changes

Year	Planning & regulation	Roading	Transport	Community	Waste
1996	0.0	0.0	0.0	0.0	0.0
1997	-0.6	-1.5	-0.8	0.2	-0.2
1998	0.9	0.6	0.8	1.9	1.0
1999	0.3	0.2	0.3	1.0	0.8
2000	3.2	3.4	3.2	2.0	2.3
2001	4.6	5.7	4.9	4.5	4.2
2002	2.0	3.0	2.4	3.0	3.5
2003	1.6	1.5	1.6	2.2	1.9
2004	3.6	4.0	3.7	3.0	3.1
2005	4.2	4.6	4.2	3.4	3.4
2006	4.7	3.8	4.4	3.6	3.4
2007	2.4	4.3	3.1	3.9	4.6
2008	8.8	7.2	8.1	5.7	4.9
2009	1.3	3.4	2.2	3.5	4.3
2010	1.5	1.8	1.7	1.5	2.2
2011	2.4	3.0	2.6	2.5	2.9
2012	2.6	4.3	3.2	2.9	4.4
2013	2.6	2.8	2.7	1.5	2.5
2014	1.5	2.3	1.9	1.8	2.6
2015	0.8	1.1	1.0	1.0	1.8
2016	0.7	1.6	1.1	2.1	2.2
2017	2.2	2.8	2.4	2.3	2.6
2018	2.0	1.3	1.7	1.7	1.2
2019	3.0	3.5	3.1	2.4	2.9
2020	1.2	1.1	1.2	1.5	1.6
2021	2.3	1.9	2.1	1.6	1.2
2022	6.9	7.6	7.0	6.5	5.9
2023	4.9	4.8	4.9	4.2	5.0
2024	3.3	2.7	3.1	3.4	3.5
2025	2.9	3.0	3.0	3.5	3.6
2026	2.7	3.0	2.9	3.0	3.5
2027	2.7	3.1	2.9	2.9	3.4
2028	2.5	3.0	2.7	2.7	3.2
2029	2.2	2.7	2.5	2.5	2.9

2030	2.1	2.6	2.4	2.4	2.8
2031	2.1	2.5	2.3	2.3	2.6
2032	2.0	2.4	2.2	2.2	2.5
2033	2.0	2.4	2.1	2.1	2.4
2034	1.9	2.2	2.0	2.0	2.3
2035	1.9	2.2	2.0	2.0	2.2
20 year average % pa	*2.6*	*2.9*	*2.7*	*2.7*	*3.0*

Table 7 Local Government Cost Adjustors, 2025 – 2035, cumulative change

Cumulative change (since 2024)

Year	Planning & regulation	Roading	Transport	Community	Waste
2025	2.9	3.0	3.0	3.5	3.6
2026	5.7	6.1	5.9	6.6	7.2
2027	8.5	9.4	9.0	9.7	10.8
2028	11.3	12.6	12.0	12.7	14.3
2029	13.8	15.7	14.7	15.4	17.7
2030	16.2	18.8	17.4	18.2	21.0
2031	18.6	21.7	20.0	20.8	24.2
2032	21.0	24.7	22.7	23.5	27.3
2033	23.4	27.7	25.3	26.1	30.3
2034	25.7	30.5	27.8	28.7	33.3
2035	28.0	33.4	30.4	31.3	36.2

Table 8 Local Government Aggregated Cost Adjustor, 1996 – 2035, index values

Index values (2024 = 1000)

Year	OPEX	CAPEX	Total
1996	470	463	468
1997	467	461	465
1998	472	466	470
1999	475	468	473
2000	488	481	486
2001	511	504	509
2002	524	518	522
2003	534	528	532
2004	552	546	550
2005	573	567	571
2006	597	589	595
2007	617	612	616
2008	662	652	659
2009	679	673	677
2010	691	685	689
2011	709	704	707
2012	732	729	731
2013	749	747	749
2014	764	762	763
2015	772	772	772
2016	783	784	783
2017	802	804	802
2018	815	816	815
2019	839	840	839
2020	850	852	851
2021	866	866	866
2022	924	925	924
2023	968	969	969
2024	1000	1000	1000
2025	1032	1032	1032
2026	1062	1064	1063
2027	1094	1096	1094
2028	1124	1128	1125
2029	1152	1158	1154
2030	1180	1187	1182
2031	1207	1215	1209
2032	1234	1243	1237
2033	1260	1271	1263
2034	1286	1298	1290
2035	1312	1325	1316

Table 9 Local Government Aggregated Cost Adjustor, 1996 – 2035, pa % changes

Pa % changes

Year	OPEX	CAPEX	Total
1996	0.0	0.0	0.0
1997	-0.5	-0.5	-0.5
1998	1.1	1.1	1.1
1999	0.5	0.5	0.5
2000	2.8	2.7	2.8
2001	4.7	4.8	4.7
2002	2.6	2.9	2.7
2003	1.8	1.8	1.8
2004	3.4	3.4	3.4
2005	3.9	3.9	3.9
2006	4.1	3.9	4.0
2007	3.4	3.8	3.5
2008	7.2	6.6	7.0
2009	2.6	3.1	2.8
2010	1.7	1.8	1.7
2011	2.6	2.7	2.7
2012	3.3	3.6	3.4
2013	2.4	2.4	2.4
2014	1.9	2.1	2.0
2015	1.1	1.2	1.1
2016	1.4	1.6	1.5
2017	2.4	2.5	2.4
2018	1.7	1.5	1.6
2019	3.0	3.0	3.0
2020	1.3	1.3	1.3
2021	1.9	1.7	1.8
2022	6.7	6.7	6.7
2023	4.8	4.8	4.8
2024	3.3	3.2	3.2
2025	3.2	3.2	3.2
2026	3.0	3.1	3.0
2027	3.0	3.1	3.0
2028	2.8	2.9	2.8
2029	2.5	2.6	2.5
2030	2.4	2.5	2.4
2031	2.3	2.4	2.3
2032	2.2	2.3	2.2
2033	2.1	2.2	2.2
2034	2.1	2.1	2.1
2035	2.0	2.1	2.0
20 year average % pa	*2.7*	*2.8*	*2.8*

Table 10 Local Government Aggregate Cost Adjustors, 2025 – 2035, cumulative change

Cumulative change (since 2024)

Year	OPEX	CAPEX	Total
2025	3.2	3.2	3.2
2026	6.2	6.4	6.3
2027	9.4	9.6	9.4
2028	12.4	12.8	12.5
2029	15.2	15.8	15.4
2030	18.0	18.7	18.2
2031	20.7	21.5	20.9
2032	23.4	24.3	23.7
2033	26.0	27.1	26.3
2034	28.6	29.8	29.0
2035	31.2	32.5	31.6

Legacy LGCI

Table 11 Legacy Local Government Cost Adjustor, 1996 – 2035, index values

Index values (2024 = 1000)

Year	Planning & regulation	Roading	Transport	Community	Water and environment
1996	474	444	467	480	394
1997	472	437	463	481	395
1998	477	440	466	489	399
1999	477	441	468	494	402
2000	493	456	483	504	419
2001	515	482	506	527	443
2002	526	496	519	543	445
2003	535	504	527	555	457
2004	554	523	546	572	477
2005	579	547	569	591	500
2006	607	568	594	612	537
2007	622	593	613	636	556
2008	673	635	662	672	596
2009	687	657	677	696	623
2010	697	669	688	706	639
2011	716	689	706	724	660
2012	734	719	729	744	685
2013	746	739	748	756	685
2014	759	756	762	769	699
2015	768	764	770	777	722
2016	773	777	778	793	735
2017	788	799	797	811	746
2018	807	809	811	824	765
2019	829	838	836	844	789
2020	840	847	846	857	807
2021	861	863	864	871	830
2022	924	929	924	927	907
2023	970	974	970	967	957
2024	1000	1000	1000	1000	1000
2025	1028	1030	1030	1035	1028
2026	1056	1061	1059	1066	1053
2027	1085	1094	1090	1097	1082
2028	1113	1126	1120	1127	1110
2029	1138	1157	1147	1154	1133
2030	1163	1188	1174	1182	1156
2031	1187	1217	1200	1208	1179
2032	1212	1247	1227	1235	1203
2033	1236	1277	1253	1261	1226
2034	1259	1305	1278	1287	1250
2035	1283	1334	1304	1313	1275

Table 12 Legacy Local Government Cost Adjustor, 1996 – 2035, pa % changes

	pa % changes				
Year	Planning & regulation	Roading	Transport	Community	Water and environment
1996	0.0	0.0	0.0	0.0	0.0
1997	-0.5	-1.5	-0.8	0.2	0.2
1998	1.0	0.6	0.8	1.9	1.2
1999	0.2	0.2	0.3	1.0	0.6
2000	3.2	3.4	3.2	2.0	4.1
2001	4.6	5.7	4.9	4.5	5.8
2002	2.0	3.0	2.4	3.0	0.4
2003	1.7	1.5	1.6	2.2	2.9
2004	3.6	4.0	3.7	3.0	4.4
2005	4.5	4.6	4.2	3.4	4.8
2006	4.8	3.8	4.4	3.6	7.3
2007	2.5	4.3	3.1	3.9	3.6
2008	8.3	7.2	8.1	5.7	7.2
2009	2.1	3.4	2.2	3.5	4.5
2010	1.5	1.8	1.7	1.5	2.6
2011	2.6	3.0	2.6	2.5	3.3
2012	2.6	4.3	3.2	2.9	3.7
2013	1.6	2.8	2.7	1.5	0.0
2014	1.7	2.3	1.9	1.8	2.0
2015	1.2	1.1	1.0	1.0	3.3
2016	0.6	1.6	1.1	2.1	1.8
2017	2.0	2.8	2.4	2.3	1.4
2018	2.4	1.3	1.7	1.7	2.6
2019	2.7	3.5	3.1	2.4	3.1
2020	1.3	1.1	1.2	1.5	2.4
2021	2.5	1.9	2.1	1.6	2.8
2022	7.4	7.6	7.0	6.5	9.3
2023	5.0	4.8	4.9	4.2	5.5
2024	3.1	2.7	3.1	3.4	4.4
2025	2.8	3.0	3.0	3.5	2.8
2026	2.7	3.0	2.9	3.0	2.5
2027	2.7	3.1	2.9	2.9	2.8
2028	2.6	3.0	2.7	2.7	2.5
2029	2.3	2.7	2.5	2.5	2.1
2030	2.2	2.6	2.4	2.4	2.0
2031	2.1	2.5	2.3	2.3	2.0
2032	2.0	2.4	2.2	2.2	2.0
2033	2.0	2.4	2.1	2.1	2.0
2034	1.9	2.2	2.0	2.0	2.0
2035	1.9	2.2	2.0	2.0	1.9
20 year average % pa	*2.6*	*2.8*	*2.7*	*2.7*	*3.0*

Table 13 Legacy Local Government Cost Adjustors, 2025 – 2035, cumulative change

	Cumulative change (since 2024)				
Year	Planning & regulation	Roading	Transport	Community	Water and environment
2025	2.8	3.0	3.0	3.5	2.8
2026	5.6	6.1	5.9	6.6	5.3
2027	8.5	9.4	9.0	9.7	8.2
2028	11.3	12.6	12.0	12.7	11.0
2029	13.8	15.7	14.7	15.4	13.3
2030	16.3	18.8	17.4	18.2	15.6
2031	18.7	21.7	20.0	20.8	17.9
2032	21.2	24.7	22.7	23.5	20.3
2033	23.6	27.7	25.3	26.1	22.6
2034	25.9	30.5	27.8	28.7	25.0
2035	28.3	33.4	30.4	31.3	27.5

Table 14 Legacy Local Government Aggregated Cost Adjustor, 1996 – 2035, index values

Index values (2024 = 1000)

Year	OPEX	CAPEX	Total
1996	453	442	450
1997	451	441	448
1998	456	445	453
1999	458	447	455
2000	473	462	469
2001	496	486	493
2002	506	496	503
2003	516	506	513
2004	536	525	532
2005	559	548	555
2006	586	576	583
2007	605	596	602
2008	650	639	647
2009	670	661	667
2010	682	673	679
2011	701	693	698
2012	723	717	721
2013	733	727	731
2014	747	742	745
2015	759	754	757
2016	769	766	768
2017	784	782	784
2018	801	798	800
2019	824	822	823
2020	837	835	836
2021	856	854	855
2022	921	921	921
2023	967	966	967
2024	1000	1000	1000
2025	1034	1035	1034
2026	1067	1070	1068
2027	1100	1106	1102
2028	1133	1141	1136
2029	1164	1174	1167
2030	1194	1206	1198
2031	1223	1237	1227
2032	1251	1266	1256
2033	1278	1295	1283
2034	1304	1322	1310
2035	1331	1350	1337

Table 15 Legacy Local Government Aggregated Cost Adjustor, 1996 – 2035, pa % changes

pa % changes

Year	OPEX	CAPEX	Total
1996	0.0	0.0	0.0
1997	-0.4	-0.4	-0.4
1998	1.1	1.1	1.1
1999	0.4	0.5	0.4
2000	3.2	3.3	3.2
2001	5.0	5.2	5.1
2002	2.0	2.0	2.0
2003	2.0	2.1	2.0
2004	3.7	3.8	3.7
2005	4.3	4.3	4.3
2006	4.9	5.0	5.0
2007	3.2	3.6	3.3
2008	7.4	7.2	7.4
2009	3.0	3.4	3.1
2010	1.8	1.9	1.8
2011	2.8	2.9	2.8
2012	3.1	3.4	3.2
2013	1.5	1.5	1.5
2014	1.9	2.0	1.9
2015	1.6	1.7	1.6
2016	1.3	1.5	1.4
2017	2.1	2.1	2.1
2018	2.1	2.0	2.1
2019	2.9	3.0	2.9
2020	1.6	1.6	1.6
2021	2.3	2.2	2.3
2022	7.6	7.8	7.7
2023	4.9	5.0	5.0
2024	3.4	3.5	3.4
2025	3.4	3.5	3.4
2026	3.2	3.4	3.2
2027	3.2	3.3	3.2
2028	3.0	3.2	3.0
2029	2.7	2.9	2.8
2030	2.6	2.8	2.6
2031	2.4	2.5	2.4
2032	2.3	2.4	2.3
2033	2.2	2.2	2.2
2034	2.1	2.1	2.1
2035	2.0	2.1	2.1
20 year average % pa	*2.9*	*3.0*	*2.9*

Table 16 Legacy Local Government Aggregate Cost Adjustors, 2025 – 2035, cumulative change

Cumulative change (since 2024)

Year	OPEX	CAPEX	Total
2025	3.4	3.5	3.4
2026	6.7	7.0	6.8
2027	10.0	10.6	10.2
2028	13.3	14.1	13.6
2029	16.4	17.4	16.7
2030	19.4	20.6	19.8
2031	22.3	23.7	22.7
2032	25.1	26.6	25.6
2033	27.8	29.5	28.3
2034	30.4	32.2	31.0
2035	33.1	35.0	33.7

Water infrastructure only

Table 17 Water infrastructure cost adjustor, index value, pa % change, and cumulative change

	Water infrastructure		
Year	Index values (2024 = 1000)	Pa % changes	Cumulative change (since 2024)
1996	394	0.0	
1997	395	0.2	
1998	399	1.2	
1999	402	0.6	
2000	419	4.1	
2001	443	5.8	
2002	445	0.4	
2003	457	2.9	
2004	477	4.4	
2005	500	4.8	
2006	537	7.3	
2007	556	3.6	
2008	596	7.2	
2009	623	4.5	
2010	639	2.6	
2011	660	3.3	
2012	685	3.7	
2013	685	0.0	
2014	699	2.0	
2015	722	3.3	
2016	735	1.8	
2017	746	1.4	
2018	765	2.6	
2019	789	3.1	
2020	807	2.4	
2021	830	2.8	
2022	907	9.3	
2023	957	5.5	
2024	1000	4.4	
2025	1045	4.5	4.5
2026	1091	4.4	9.1
2027	1137	4.3	13.7
2028	1183	4.0	18.3
2029	1228	3.7	22.8
2030	1270	3.5	27.0
2031	1308	3.0	30.8
2032	1344	2.7	34.4
2033	1375	2.3	37.5
2034	1406	2.2	40.6
2035	1437	2.2	43.7
20 year average % pa		*3.6*	

6 Conclusion

The worst of inflation is now behind us, and the CPI is expected to be within the 1-3 percent target range of the RBNZ by the end of 2024. Input prices for producers and capital asset prices are also increasing at a slower rate and price increases for these peaked in 2022 or 2023. The construction and manufacturing sectors are in contraction as high interest rates have dampened demand for the outputs of these sectors. The pricing power of producers is falling, and profit margins are shrinking.

Given that all the key economic indicators point to a weak economy, the RBNZ has shifted its stance sooner rather than later in a bid to avoid an overly restrictive economic environment. Thus, it began OCR cuts in both September and October and may follow this with further cuts this year. But monetary policy works with a lag of several months. Until the impacts of looser monetary settings take effect, economic conditions are set to deteriorate further. Unemployment will increase as firms cut production, and household budgets will continue to shrink as employees lose negotiating power in the labour market.

Overall, the rest of 2024 and the first half of 2025 will be characterised by a period of declining inflation, rising unemployment, and low to no GDP growth. Local government will continue to play an important role in supporting the well-being of households as economic conditions deteriorate.

Appendix A Price indices actual and forecast values

Figure 14 PPI inputs – local government administration

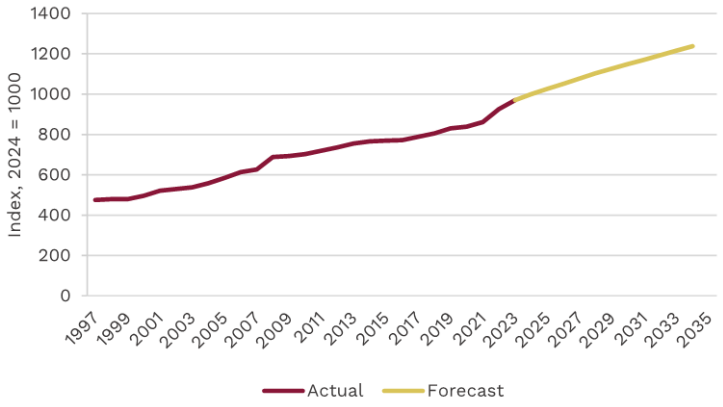


Figure 15 PPI inputs – arts and recreation

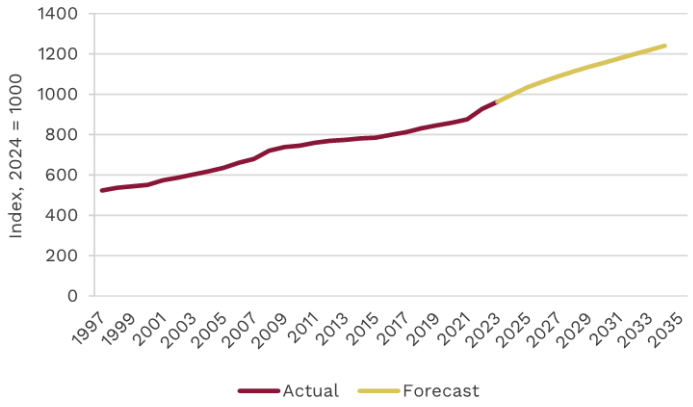


Figure 16 PPI inputs – water, sewer, drainage, and waste services

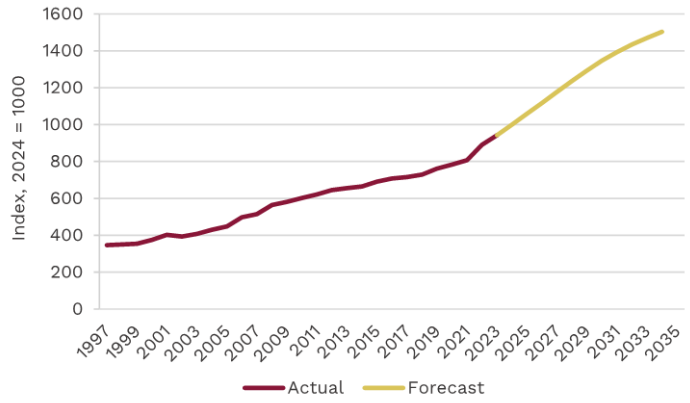


Figure 17 CGI – earthmoving and site work

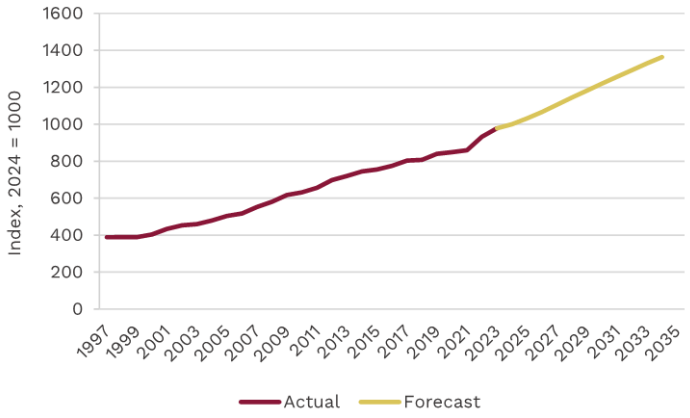


Figure 18 CGI – reclamation and river control

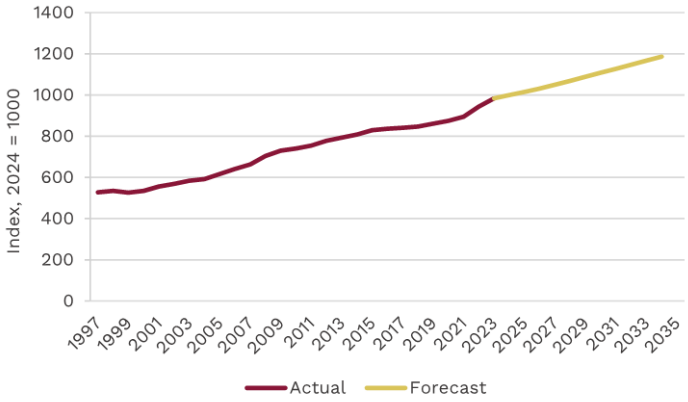


Figure 19 CGI – pipelines

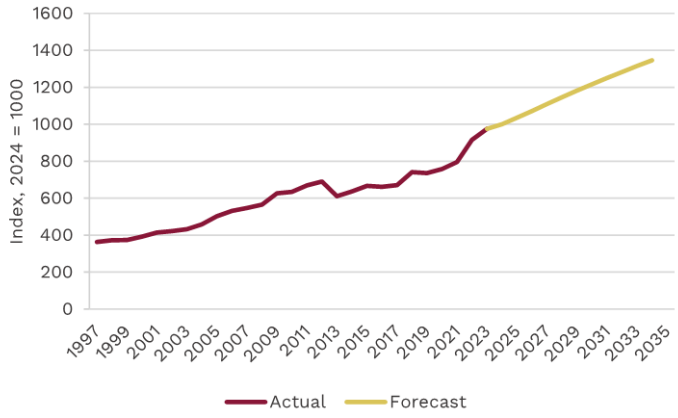


Figure 20 Local government wages

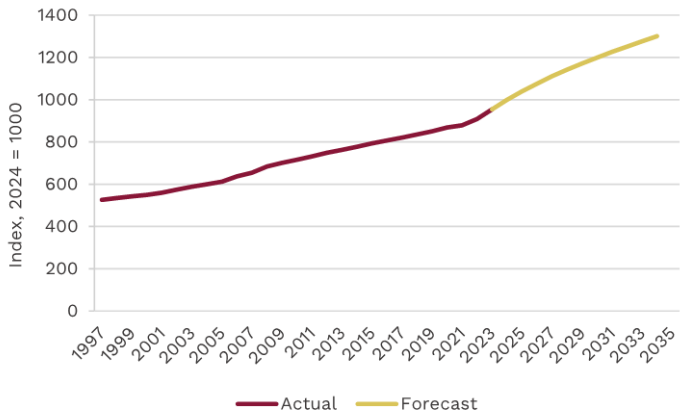
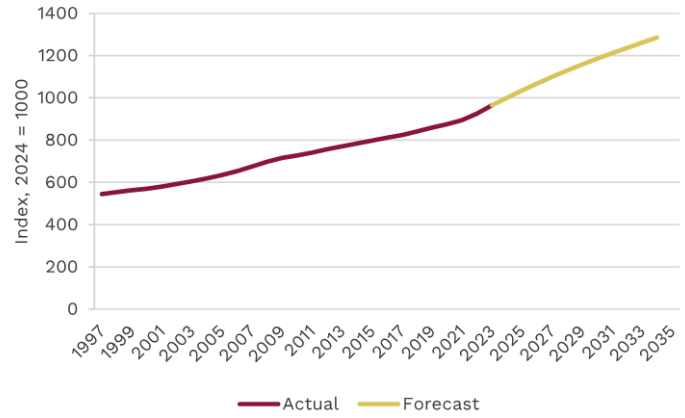


Figure 21 Private sector wages



Cost adjustor series

These series are linear combinations of the above eight indices. They describe the price trajectory of baskets of goods bought by local government.

Figure 22 LGCI transport

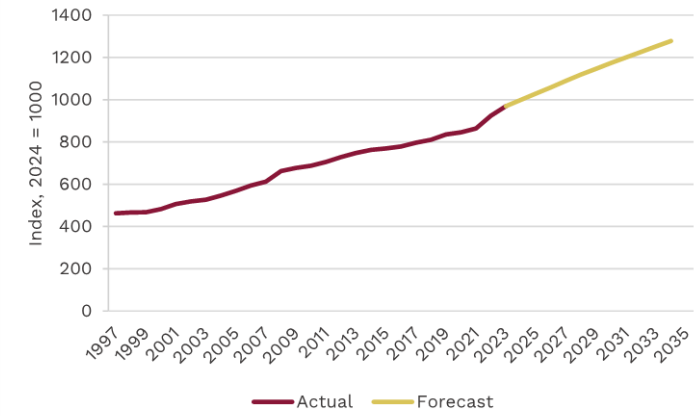


Figure 23 LGCI community

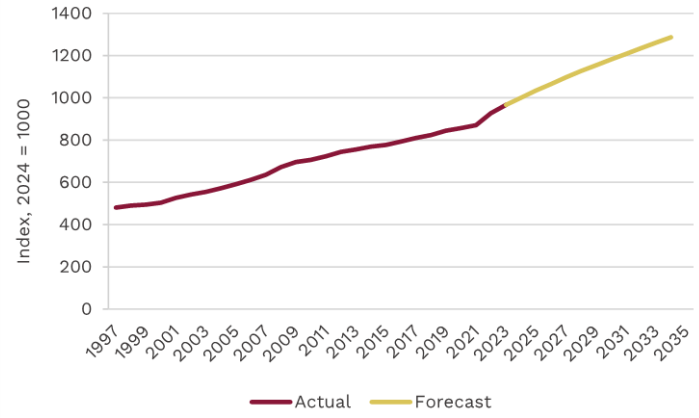


Figure 24 LGCI waste

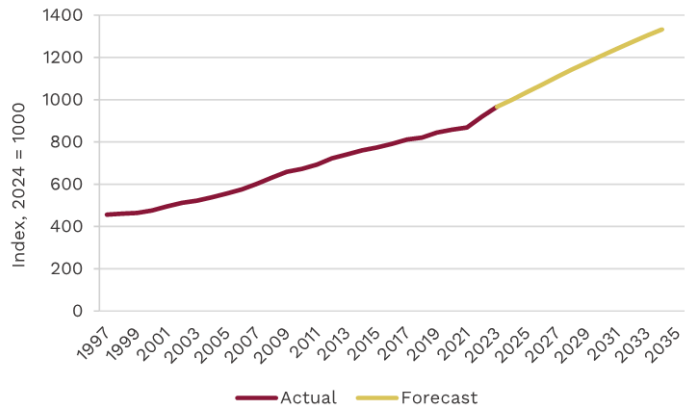


Figure 25 LGCI planning and regulation

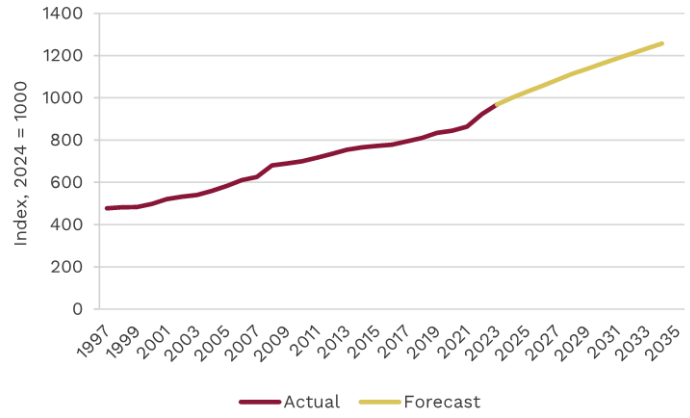


Figure 26 LGCI roading

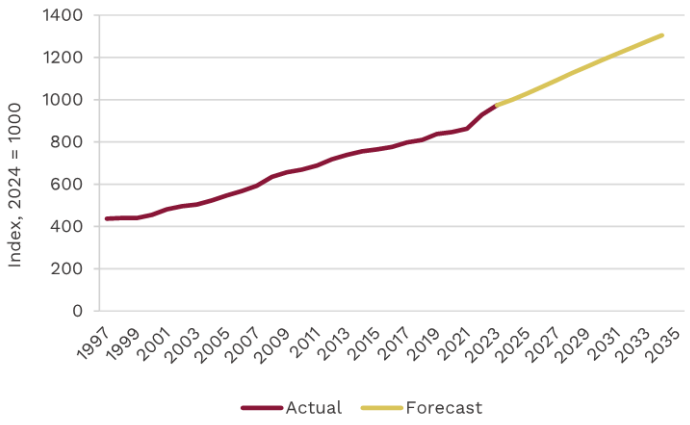
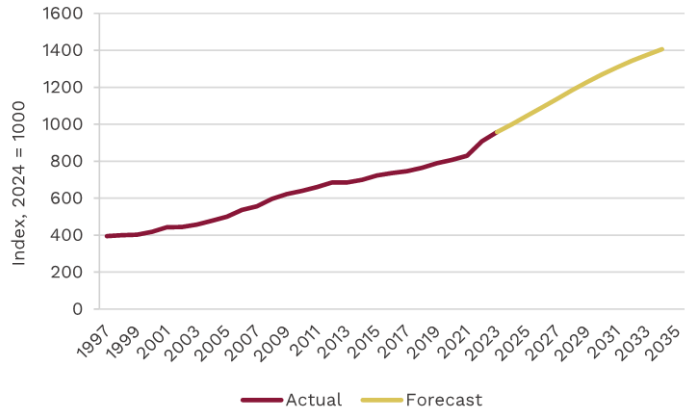


Figure 27 LGCI water infrastructure



Aggregate adjustor series

Figure 28 LGCI OPEX

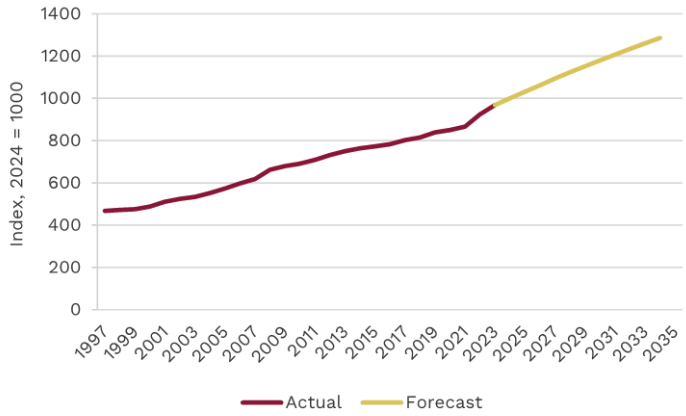


Figure 29 LGCI CAPEX

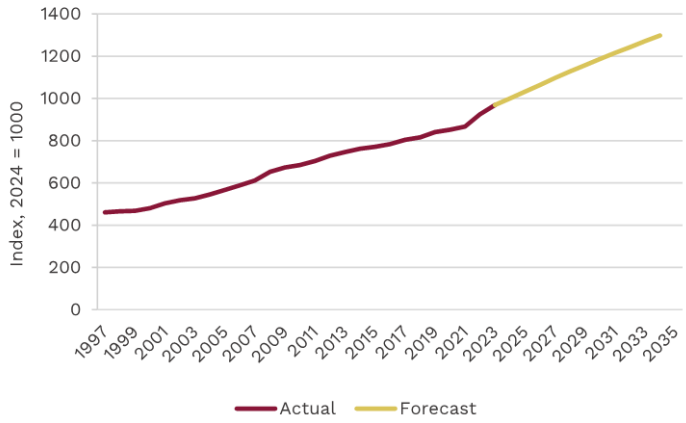
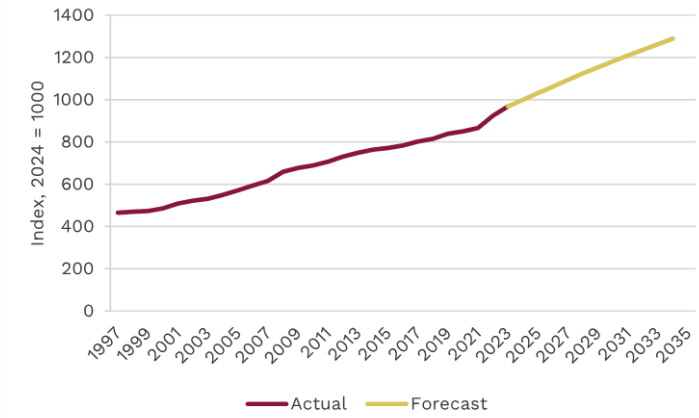


Figure 30 LGCI total



Appendix B Macroeconomic forecasts

Table 18 BERL macroeconomic forecasts

Year to June	Real expenditure GDP (% pa change)	Unemployment rate	CPI	CPI (% pa change)
2023 (actual)	1.3	3.6	1231	6.0
2024 (actual)	-0.2	4.65	1272	3.3
2025	1.2	5.5	1298	2.0
2026	1.9	5.2	1325	2.1
2027	2.3	4.6	1352	2.0
2028	2.8	4.4	1379	2.0
2029	3.1	4.3	1406	2.0
2030	3.3	4.2	1433	1.9
2031	3.4	4.1	1462	2.0
2032	3.3	4.1	1493	2.1
2033	3.3	4.1	1524	2.1
2034	3.3	4.0	1556	2.1
2035	3.3	4.0	1588	2.1