



Budget 2021 - Economy

What is the continued impact of COVID-19?

Given the exceptional uncertainty following the COVID-19 pandemic, the New Zealand economy has proved to be more resilient than anticipated. This provides hope that the intergenerational cost of the pandemic may not be as severe as previously thought.

GDP

Following the 11.0% GDP contraction in the June 2020 quarter, the economy demonstrated a rapid recovery in the second half of 2020, bringing activity close to pre-pandemic levels. The economy is expected to strengthen, by the end of the 2021 financial year, GDP is expected to have increased by 2.9%, and continue to rise broadly at this level in outyears.

While overall positive, there still remains a high degree of divergence between the different sectors of the economy. The continued absence of international visitors outside the travel bubble contributed to a 1.0% quarterly decline in December 2020 quarter GDP, felt largely by the tourism sector.

Unemployment

Unemployment fell to 4.7% in the March 2021 quarter and is expected to further decrease to 4.2% in June 2025. This shows a promising trend for the unemployment of New Zealanders post COVID-19. In the near future,

unemployment is forecast to rise slightly as the number of people entering the labour force exceeds the number of people entering employment. However, these figures are not fully reflective of inherent trends in day-to-day working as there has been higher underutilisation and a fall in hours worked, suggesting spare workforce capacity and increased employment being driven by people entering part-time work. Given the tight state of the labour market, we expect wage inflation to increase.

Inflation

Inflationary pressures from resilient domestic demand, supply chain disruptions and the rising cost of new homes have supported price growth, with CPI inflation reaching 1.5% in the March 2021 quarter. Inflation is expected to continue rising in 2021, peaking at 2.4% in the September quarter as a result of temporary price pressures. Inflation is forecasted to fall below 2.0% in 2022 as global supply chains normalise and there is spare capacity in the economy, which is expected to remain for some time. There will be a rise in inflation from 2023, reaching 2.0% in early 2024 in line with historical Treasury projections.

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