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CLIENT BRIEFING

Insights from the NZ, US, UK, Australian and Canadian experiences with wage-price spirals

August 2023

EXECUTIVE SUMMARY

Wage-price spirals have developed in NZ, the US, the UK, Australia, and Canada (and other countries) because of overly stimulatory monetary and fiscal policies in response to Covid. And in some countries, like NZ, excessive stimulus before Covid. A review of the experiences with inflation problems in these five countries provides no basis to expect any to escape the latest wage-price spiral, that is the largest in 30

years for most of them, without hard landings that could involve more than one recession. Soft landings that avoid a recession and involve a quite protracted period of low growth are possible if the central banks could operate monetary policy like a surgeon with a scalpel, but they use it like a sledgehammer. This is largely because of the reactive decision-making that played a big part in fuelling inflation to start with.



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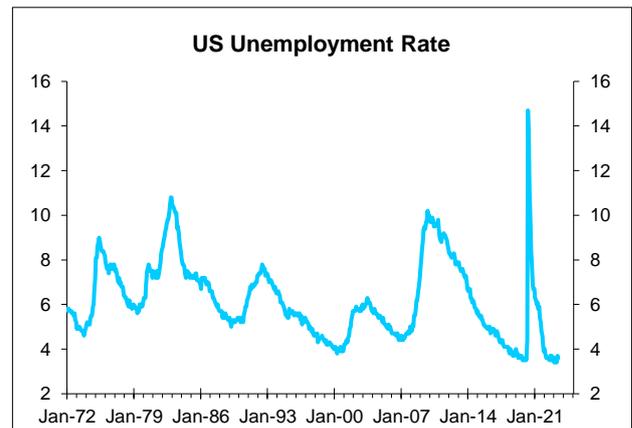
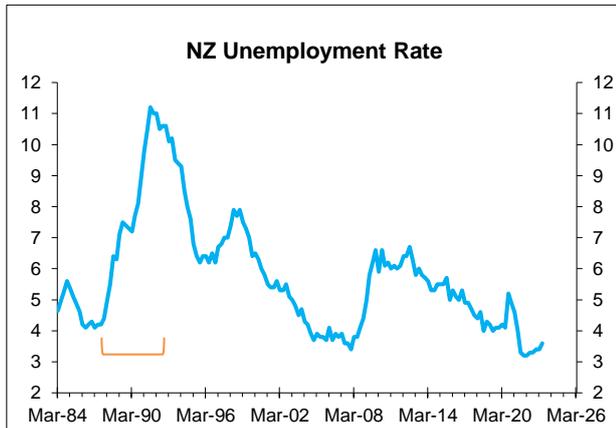
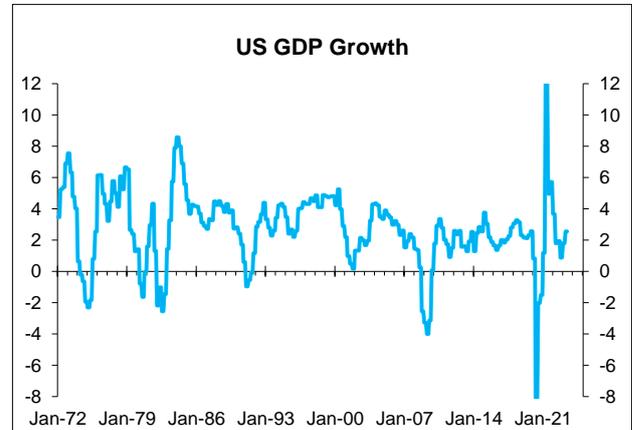
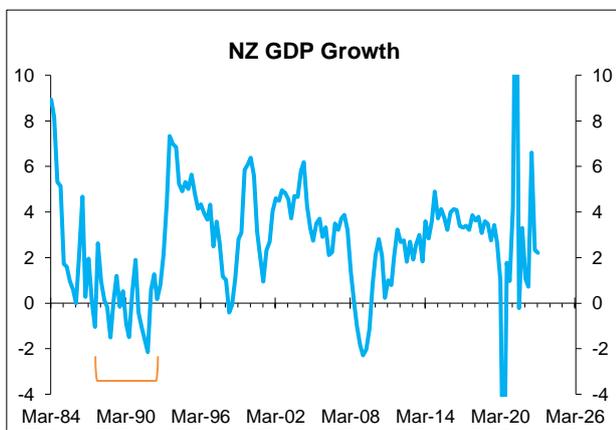
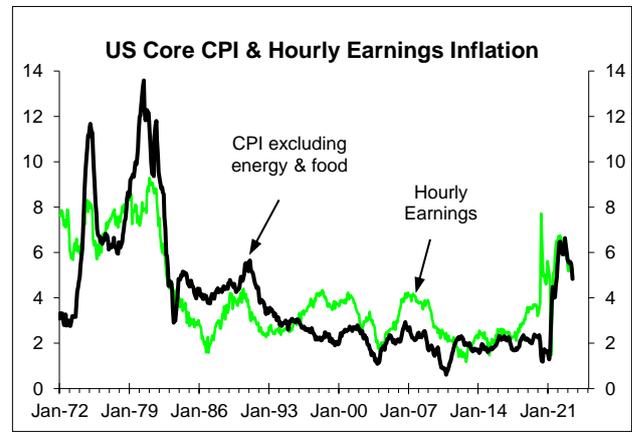
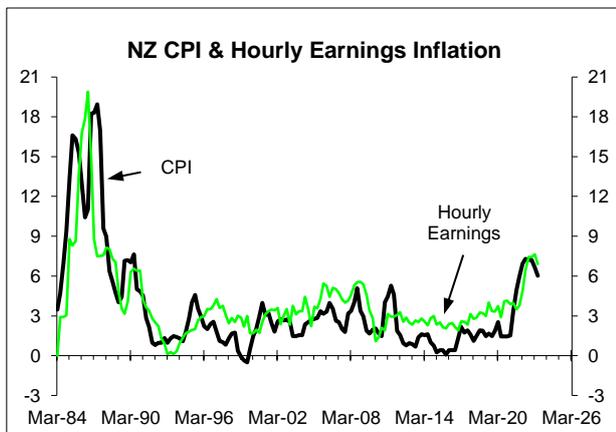
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NZ's wage-price spiral experience

NZ had a major wage-price spiral in the 1980s (the 1970s can't be shown because data aren't available) shown in the first chart. It took a series of recessions and a major increase in the unemployment rate to break that wage-price spiral (the highlighted areas in the second and third charts). NZ had a modest wage-price spiral in the 2000s that required a sizeable recession and a large increase in the unemployment rate to tame. NZ had a minor wage-price spiral in the mid-1990s that took a mini recession and moderate increase in the unemployment rate to fix. The current wage-price spiral is quite a bit larger than that in the 2000s but quite a bit smaller than that in the 1980s with obvious implications from economic prospects.

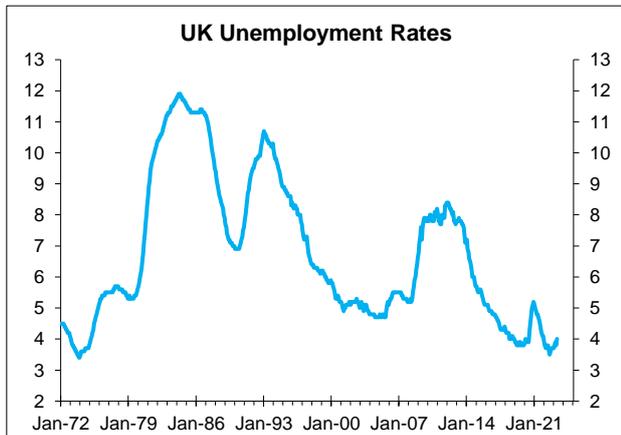
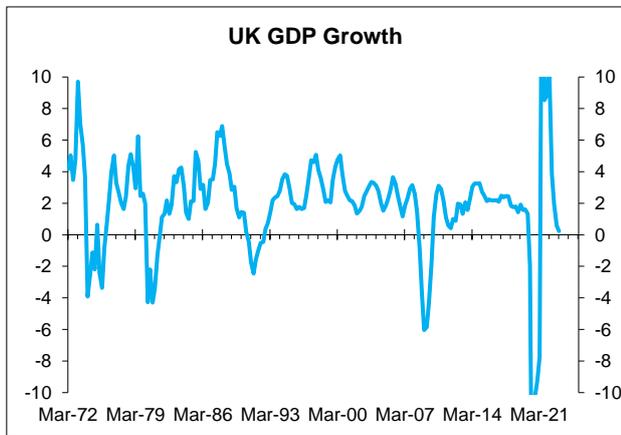
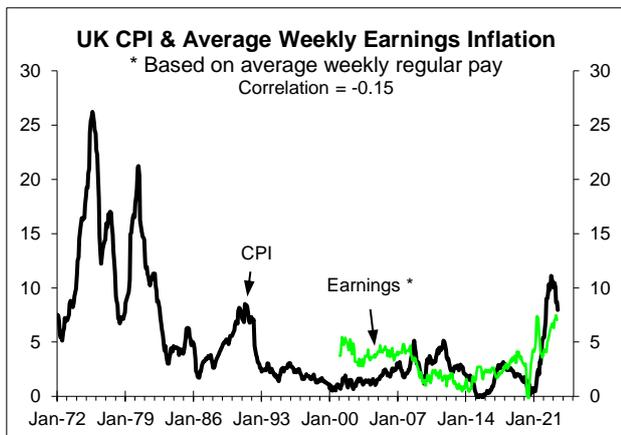
The US wage-price spiral experience

Like NZ, the latest US wage-price spiral is the largest since the 1970s and first half of the 1980s (first chart below) and it took a series of recessions and a huge increase in the unemployment rate to tame (second and third charts below). The battle against this wage-price spiral was protracted and involved a total of three recessions. There was a hint of an inflation problem in the 1980s that was fixed by a recession and a sizeable increase in the unemployment rate as was also the case in the mid-2000s (see the relevant periods in the charts below). Like NZ, recessions and big increases in the unemployment rate have always resulted when the Fed has gone into battle to fight an inflation problem.



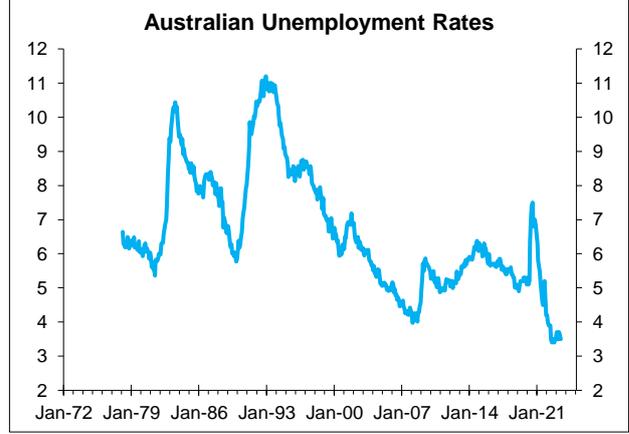
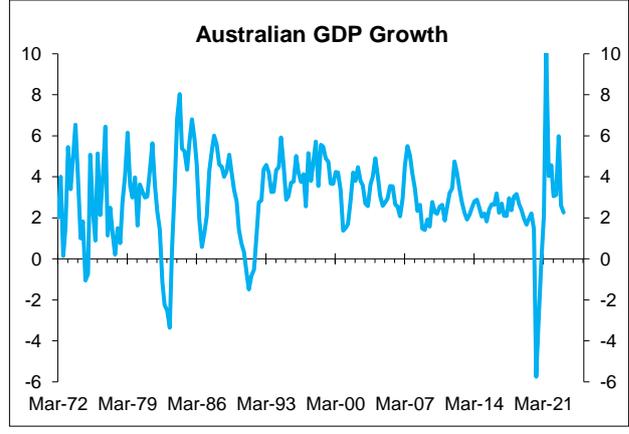
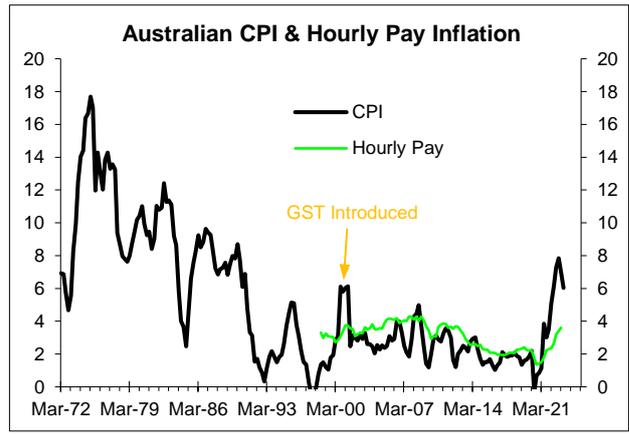
The UK wage-price spiral experience

The wage inflation data only go back to 2000 but the UK had a wage as well as price inflation problem in the 1970s and early-1980s (first chart). And like NZ and the US, it took recessions and major increases in the unemployment rate to tame inflation (second and third charts). There was an inflation problem in the late-1980s and early-1990s that was tamed by a recession and large increase in the unemployment rate and a minor one in the late-2000s to early-2010s that culminated in a recession and large increase in the unemployment rate that the GFC played a major part in causing. Like NZ and the US, no soft landings for the UK once an inflation problem develops.



Australia's wage-price spiral experience

Like the UK, I could only find Australian wage data back part of the way, but it is like the other three with periods of inflation being fixed by recessions and large increases in the unemployment rate. It has the smallest of the current wage-price spirals so has an outside chance of a soft landing. However, the RBA, like the RBNZ, the Fed and Bank of England, makes reactive not proactive decisions, which increasing the likelihood of a recession and large increase in the unemployment rate.



Canada's wage-price spiral experience

The next three charts show that inflation problems in Canada have also always been followed or fixed by

recessions and large increases in the unemployment rate. No soft landings to be seen in NZ of any of the English-speaking countries that are best to consider as providing potential insights for NZ prospects when central banks allow wage-price spirals develop.

