Closing the Gaps – Between Current Economic Policy and the Needs of Producers

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- Several recent years of fortuitous circumstances have allowed New Zealanders a mirage of economic robustness and prosperity, when the reality is an economy with low incomes, low productivity and major structural weaknesses.

- New Zealand's economic problems are serious and need to be resolved if New Zealand is to have a prosperous future.

- Resolution requires a fundamental shift in policy, towards building international competitiveness and economic capability and efficiency, with less debilitating regulation and intervention.

- Productivity, competitiveness, exports and savings must be top priorities. Serious, complementary tax reform is also needed.

- The “big picture” is that since 1960 New Zealand has steadily gone backwards, compared to Australia and the rest of the OECD. There have been some years of good growth but these have tended to highlight New Zealand’s fundamental economic weaknesses.

- Unfortunately, New Zealand’s long term performance in both has been poor, well behind Australia’s and the OECD average:

	Australia	USA	New Zealand	OECD
Increase 1960-1999:				
Real GDP/employee % (productivity)	97	83	39	158
Exports/ capita %	490	550	220	540

Source: OECD

- Since 2000, New Zealand has enjoyed an unusual period of high economic growth, of the order of 4% per annum. This reflected an unusual coincidence of external factors:

  - the terms of trade have averaged 1035 since 2000; only one single year has been higher since 1998.

  - net inward migration has been very high since 2000, peaking at over 40,000pa; since 1970 the previous highest year was 28,500.

- These strong growth stimuli were reinforced by strong growth in household debt, the household debt income ratio rising to 143%, from 100% in 2000 – it was less than 60% in 1990.

- This period of high growth had a number of consequences that highlighted its unsustainability and the economy's basic weaknesses:

  - the Current Account deficit is now 8% of GDP, which is very high and clearly unsustainable. 5% is considered to be high.

  - national and household savings rates continue to decline and are now negative – Households at negative 12%, one of the lowest rates in the OECD.

  - New Zealand's external obligations continue to rise and are now $164 billion and 110% of GDP – amongst the highest (worst) in the OECD. The cost of servicing these obligations is now an important issue.

- There are other areas of concern, including:
  - in the last 2 years labour productivity growth (RBNZ) average a low 1% per annum.
  - changes in employment-related legislation have reinforced the role of unions, at the expense of employers and the development of performance and productivity based labour arrangements.
- New Zealand’s inability to grow its exports on a competitive basis and at a sufficient rate is a critical weakness. In spite of its high export dependence, New Zealand’s exports per capita are now below the OECD average.

- It is a serious question, whether there is a political constituency now for addressing these difficult issues or, if not, the likelihood of decisive leadership in the needed direction?

- New Zealand is a low income country, according to the OECD. Reflecting this most people don’t pay much tax, are net beneficiaries of government expenditure and the Household sector, currently, doesn’t save.

- The 3% of individual tax payers with the highest incomes pay about 25% of all personal income tax. The top 10% pay about 45%. At the other end of the scale, 56% of tax payers pay only 14% of personal income tax.

- Average central government expenditure per taxpayer is about $13,000pa. A personal income of $38,500 generates direct and indirect (specifically GST) taxes of about $13,000.

- About 670,000 tax payers had incomes above this level; but 2.4 million had incomes below this level. These numbers are approximate.

- So, there are a lot of voters in the community that are likely to be more interested in increased government expenditure than lower taxes and who are unlikely to have any incentive to support policies that reduce the burden and disincentive of taxation and increase the competitiveness of producers generally and exporters in particular.

- Meanwhile, we seek more open trading arrangements with China and others, which is good, but without putting in place the policies that will allow New Zealand businesses, and tradable goods producers in particular, to compete.

- The following quote from Bill Buckley (Buckley Systems, in Management, Nov 2005) on competing with China is relevant:

  > "Its doomsday for New Zealand engineering. This is something I've got to compete against when I've got to employ people here with more rights in this Company than I do. The whole outlook of our Government makes it impossible for us to make a living anymore."

- Many businesses in New Zealand today will empathise with this view.

- Without an effective policy response the implications for New Zealand could be very sobering. On the other hand, with a more astute policy response there is a better outlook.

Now, more specifically on the mining and mineral processing sector.

- Australia is New Zealand's largest export market, by a substantial margin and, in 2004/5, gold was New Zealand's second largest export to Australia, 17% ahead of next-ranked timber, 60% ahead of cheese, more than twice refrigerators and freezers, and some three times wine and carpets.
- Producers are exposed to a whole range of risks and policy has a substantial influence on the nature and extent of those risks.
- Positive tax changes look problematic and expenditure growth is oriented to consumers, not producers. The example of forestry is sobering.
- The Resource Management Act continues to be an unduly expensive impediment to investment and development, with little prospect of real improvement.

- Energy is important for most new investments but is now problematic. It is difficult / impossible to get satisfactory long term supply arrangements to support major projects, in the face of the likely gas and electricity shortages.

- Lines companies, an essential element, are cost plus prices setters, risk averse and not exposed to competition.

- Telecommunications policies seem more designed to protect the incumbent than to facilitate the development of a competitive, world class infrastructure.

- Kyoto Protocol policy was poorly designed and implementation has been difficult – OceanaGold was the first company to sign an agreement through the full process. How should we regard that agreement now?

- The sector has an excellent export growth potential but the administration of the RMA is a major issue, as is the impact of central and local government generally, which often increases risk for the developer, but then requires full indemnity for its own risk, in spite of the benefits it will gain.

In Conclusion:

- New Zealand faces serious economic problems, that are unlikely to be remedied without decisive Government action to create a more competitive economy and a sustained improvement in exports per capita and productivity.

- Effective leadership is needed as politics favour more of the same – increasing tax revenue – on the present basis, and other revenues, expenditure oriented to Households not producers and an orientation to achieving social objectives, even where they reduce competitiveness, rather than driving economic performance.

- The serious distortions in the economy, particularly the external deficit, high level of external obligations and low saving rate, as well as the increasing burden of taxation on a shrinking proportion of workers and personal tax payers, justifies urgency.

- The gold mining industry has the potential for substantial expansion and greater contribution to the economy and exports.
  Material improvements in the policy environment are likely to give a good payback, in national net benefit terms.