

Black or White: Good Cat is Mouse-Catching

Some months ago the *Sunday Star-Times* organised a series of questions to put to the prime minister, John Key, and printed them along with his replies.

This was a worthwhile exercise in open democracy.

My question was along the following lines: “Your predecessor Helen Clark famously declared that the role of government is whatever the government defined it to be. What is your idea of the proper role of government?”

Mr Key replied that his view was a pragmatic one: the government should do whatever works.

This was a good answer. It reminded me of the Sichuan proverb: “black or white – good cat is mouse-catching”. Deng Xiaoping, the Chinese leader who initiated China’s moves away from a socialist system in the 1970s, adapted it to say that it didn’t matter whether the cat was black or white “as long as it can catch mice”.

Deng’s reforms certainly worked: in a generation they lifted more people out of poverty than ever before in human history.

I agree that public policy should be based on what works for prosperity, liberty and equity. No one would argue that governments should adopt what doesn’t work. Hence the need for evidence and analysis to inform policy: for so-called “evidence-based policy making”.

Economics is a discipline that can help inform policy choices. It is fundamentally an empirical science. There is no sense in which a policy can be correct in theory but wrong in practice: if the practice goes wrong, the theory is defective (as socialism demonstrated).

Free trade is an example of a policy that is ultimately justified more on practical than theoretical grounds. To be sure, it rests on the fundamental

economic principle of comparative advantage, but there are a number of theoretical arguments for departing from that principle: optimum tariff notions, strategic trade theory, infant industry arguments and the like.

As a matter of policy, however, the vast majority of professional economists put aside these theories as unworkable in practice and come down on the side of free trade.

A similar comment applies to business ownership. The evidence is now compelling that – not always, but on average and over time – privately owned enterprises out-perform state-owned enterprises (and it is the general outcome that should inform sound public policy). The reasons for better private sector performance have become well understood but the fundamental argument for privatisation is pragmatic: it generally works.

Likewise, there is a high level of agreement among economists about the potentially harmful effects of minimum wages. In a paper last year on evidence-based policy-making, the chairman of the Australian Productivity Commission, Gary Banks, cited indigenous leader Noel Pearson (who is giving the Business Roundtable's annual Sir Ronald Trotter Lecture in Auckland next month).

“[As Pearson affirmed], perhaps the most calamitous and tragic example of all was the extension of ‘equal wages’ to Aboriginal stockmen in the late 1960s. Despite warnings by some at the time, this apparently well-motivated action led to the majority losing their jobs, driving them and their extended families into townships – ultimately subjecting them to the ravages of passive welfare.”

Of course, facts seldom speak for themselves – they have to be interpreted. Everyone involved in the debate about public policy argues on the basis of some set of principles or ideas, whether or not they are conscious of them or make them explicit.

This is obviously true of the current government. For example, the Confidence and Supply Agreement between the National and ACT parties recognises that a commitment “to limited government – government limited

to its proper role” will need to be consistently adhered to if the 2025 goal of bridging the income gap with Australia is to be achieved.

‘Limited’ does not mean minimalist – or even necessarily small – government. It means government focused on roles that economics teaches us governments need to undertake, such as the provision of genuine public goods and a social safety net.

Thus in some circumstances, high levels of spending on, say, national security (a public good) may well be justified. But if governments go beyond such roles, economic growth and the well-being of the community is jeopardised.

A study for the Treasury suggested that a limited government criterion for public expenditure would normally point to a spending ratio of around 15% of GDP. Even John Maynard Keynes thought government spending should be no more than 25% of a country’s GDP. By comparison, government spending at all levels is currently running at around 45% of GDP in New Zealand.

Just as fat and lazy cats are not good mouse-catchers, over-extended and bloated governments are not good for economic growth and prosperity.

The 2025 Taskforce, which derives from the Confidence and Supply Agreement – with its emphasis on the importance of limited government – will no doubt be making that point when it reports later this month.

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