

Australia-New Zealand Income Gap 38% and Rising

“Full many a flower is born to blush unseen, And waste its sweetness on the desert air.”

Don Brash and members of the 2025 Taskforce could be forgiven for reflecting on these lines from Thomas Gray’s famous Elegy.

Their second high quality report released earlier this month should have sparked wide public debate, but didn’t.

Strangely, given its mandate to monitor progress towards the government’s goal of catching up to Australian per capita incomes by 2025, the Taskforce did not highlight the most recent estimate of the gap.

However, a table in the report indicates that it has increased from around 35% when the government came into office in 2008 to around 38% today.

This should be no surprise.

First, the government inherited an economy already in recession and Australia came through the global financial crisis better than New Zealand.

Second, turning around the declining performance of the economy in the past decade and starting to close the gap is a medium-term project. Progress could be expected within 3-5 years given outstanding economic management, but not in a single parliamentary term.

The Taskforce’s recipe for success is totally conventional. Stanford University professor Keith Hennessey put it well in a recent article.

“The goals of an ideal economic-growth agenda are simple and well known: a large and thriving private sector and a small government; reduced government spending, which means lower taxes and smaller deficits; open trade and investment; taxes and regulations that don’t distort decisions,

discourage capital formation or work, or provide rents to the politically powerful; deep and flexible labor markets; a reformed financial sector that channels savings to where they can do the most good; a society in which education and innovation flourish; a stable, low-regulation legal environment, in which monetary policy is sound and business decisions issue from customers and competitors rather than regulators and judges.”

Those are the essential messages of the Taskforce report.

The Taskforce should have emphasised that its prescriptions are consistent with advice from the OECD and the submissions of major business organisations. Federated Farmers, for example, stated that it agreed with all but one of the first report’s 35 recommendations.

No credible alternative programme for achieving the goal has been put forward. The report persuasively rejects the ‘economic geography’ arguments of Philip McCann and the ‘smart, active’ government policies promoted by the New Zealand Institute and followed by the previous government.

The Taskforce emphasises the need to shift resources from the domestic sector of the economy to foreign exchange earning and saving activities in order to reduce New Zealand’s external vulnerabilities. This structural change is barely happening, and its urgency is underlined by last week’s credit rating warning.

The report has some excellent material on research and development, foreign investment (where it notes that New Zealand has one of the OECD’s most restrictive regimes), and infrastructure. It questions the government’s planned investment in broadband. There is strong political pressure in Australia for transparent analysis of the case for government involvement in broadband: why isn’t there similar pressure here?

There are still some curious omissions: the report has nothing to say on the case for opening ACC up to competition and for further reforms to local government, which are major issues for business organisations.

However, its most important statement is incontrovertible: “Our reading of the economic literature and the historical evidence suggests that closing an income gap of the sort New Zealand faces ... cannot be done with government spending at more than 40 percent of GDP.” (Total government spending – central plus local – currently stands at 45% on the OECD measure.)

It is extraordinary that the Treasury has never acknowledged this simple point.

A weakness of the report is that it lacks an international perspective. There are profound lessons for New Zealand both in the economic dilemmas of the big welfare states of Europe and the old OECD, on the one hand, and the dynamic economies of the Asia-Pacific region on the other.

Some doubt our ability to catch up with Australia. But the question should be reversed: why wouldn't the gap close if we moved towards the smaller-government, low-tax policies of high-income countries like Hong Kong and Singapore?

Finance minister Bill English responded to the report by saying the government was moving in some of the directions it suggested.

He also said, reasonably, that the government would not break election commitments and that it had to convince people of the benefits of change.

The challenges are indeed political. New Zealand does not have a Tea Party. New Zealanders tend to vote with their feet rather than to agitate for better political decision making.

But therein lies a clear and present danger. The Taskforce warns that the current and projected income gap could result in the emigration of over 400,000 New Zealanders during the next 15 years.

Figures out last week indicated that in the past year, 35,000 people left for Australia and just 15,800 arrived, a net loss of more than 19,000 across the Tasman.

We cannot afford to close our eyes to the challenges posed by the Taskforce. The appropriate literary allusion is, 'Sleepers Awake!'"

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