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**NATIONAL FARMERS' FEDERATION CONFERENCE**

**UNDOING RUIN IN AUSTRALIA AND NEW  
ZEALAND**

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## **UNDOING RUIN IN AUSTRALIA AND NEW ZEALAND**

Over 200 years ago, the author of *The Wealth of Nations*, Adam Smith, famously remarked that there is much ruin in a rich nation. I often think that Australia and New Zealand have spent a lot of their history proving Smith's point.

Speaking in New Zealand a few years ago, Geoffrey Blainey, perhaps Australia's leading historian, reminded us that:

In the second half of the nineteenth century Australia and New Zealand were astonishing successes – by the standards of the time. ... [B]y 1890 or 1900 [they] were in the top nations and maybe were the top two.

Explaining the reasons for their success, Blainey said:

... they were not just the lucky countries. They put enormous effort and intelligence and the latest technology into the economic fields where they had natural advantages.

And he noted something which he said is now often overlooked – the importance of sheer hard work:

In 1890 in Australia and New Zealand, my estimate is that well over half the workforce laboured more than 60 hours a week.

To Blainey's reasons for success, I would add the role played by relatively open and competitive economies and limited governments – at the turn of the century the state's share of both economies was no more than about 10 percent.

But as Blainey went on to explain, from 1890 the popular attitudes in both countries slowly underwent a major change in direction. The emphasis swung from self help to government help. Economic incentives and competitiveness were blunted and both economies were increasingly "deprived of invigorating air and sunlight":

It is fair to say that Australia and New Zealand between, say, 1890 and 1970 were, in a subtle way, harbingers of the Soviet Union and its ultimate economic collapse.

Beginning in the 1970s but with greater seriousness from the mid-1980s, governments in both countries have been endeavouring to break some of our more ruinous habits. But the attitudes learned over several generations are not easily discarded. As Blainey pointed out, when Australia won the America's Cup:

... the prime minister urged everyone, in the rather uncompetitive economy he presided over, to take yet another day's holiday.

In the same way, after a few years of solid reform efforts in the 1980s, a New Zealand prime minister called for a break for a cup of tea. Both countries are still struggling to develop the culture of continuous improvement they need in order to compete successfully against strong international fields and achieve their undoubted potential.

The policies both countries have been working to implement might broadly be described as economic liberalisation. Over time, more and more elements have converged. But in both countries there is still a tendency to get things out of focus.

In Australia, one camp has seen New Zealand's reforms as some kind of magic wand, and has had quite unrealistic expectations about the size of the benefits and how long they take to eventuate. Others have seen New Zealand as a model, but overlooked how much remains to be done. Some detractors think New Zealand has done nothing right, and seize on any bad news to argue that reform has failed. Others grudgingly admit its necessity, but tell us it was all too rapid and uncaring.

There are similarly distorted New Zealand views of Australia. A few years ago there were smug attitudes in some quarters towards the gradualistic and half-baked approach to economic reform they saw being followed in Australia compared with New Zealand's bolder measures. That smugness disappeared as New Zealand's reform programme stalled and Australia pressed steadily on. Alternatively, there were people who selectively praised anything anywhere that looked like the 'old' New Zealand. They were very keen on Australia's 'Accord', but these days they are having a hard job finding anything much to praise about Australia.

We ought to throw away these distorting lenses and take a closer look at the realities. More importantly, we should not take as mutual benchmarks two countries with a long

history of mediocrity. We should measure ourselves against the top performers and, more importantly still, against our own true potential.

Let me first remove the distorting lens from New Zealand. Malcolm Fraser recently burst on to the scene as an economic commentator, telling us that the "economic miracle is blowing apart" and that "New Zealand faces a fundamental economic crisis." Australia should beware of "economic rationalism" – maybe he felt it should try economic irrationalism instead?

Perhaps the first point to make is that economic miracles don't exist: there is nothing supernatural about good economic performance. The so-called 'miracle' economies of Germany and Japan in the 1950s and '60s were due to generally sound economic policies (which have long since been eroded) and the industriousness of their people.

The second point is that New Zealand began its reforms as an economic basket case. Then its economic framework was unbalanced for many years after the reforms began in 1984 because the reformist Labour government failed to free up the labour market and impose fiscal discipline. Subsequently it opted for a teabreak. The economic framework only became generally consistent in the early 1990s when these weaknesses were remedied, and by the mid-1990s we were enjoying low inflation, strong economic growth and rapidly falling unemployment.

But the third and most important point to make is that Mr Fraser seems to have been asleep for the past three or four years. It is not as though the true picture has not been well reported in Australia. As *The Australian Financial Review* accurately summed it up in an editorial last November:

There is no doubt the New Zealand experiment has been a success. Reforms driven by Labour's Sir Roger Douglas and National's Ms Ruth Richardson between 1990 and 1994 have led to a complete restructuring of the economy. ... Unfortunately, reform has slowed sharply in the past three years. Ms Richardson's departure in 1994 marked a turning point. Little has been done since, apart from passage of the Fiscal Responsibility Act and some tax cuts. ... a system of proportional representation, introduced at a time when the gains from economic reform were less plain, is hindering leadership ... . Competitors are fast catching up. Many areas demand further deregulation – especially agriculture producer boards and the hugely costly no fault [accident] insurance scheme. Extraordinarily, the Government still owns a coal mining company, not to mention most of

the electricity industry ... . The free labour market has delivered low unemployment but is being disrupted by the courts and needs fixing. And the nation has not yet addressed the problem of its rapidly ageing population.

That assessment is shared by most of the New Zealand business community, most economic commentators, and organisations such as the IMF and the OECD.

While New Zealand has been having another teabreak, Australia has been catching up in those areas where it was behind. It's therefore hardly surprising that New Zealand is not performing any better than Australia; indeed in my judgment Australia now clearly has the edge.

It may be useful to look more closely at how policies in Australia and New Zealand compare under a range of headings. Perhaps the most striking point that comes out is that while New Zealanders, quite rightly, think of Australia as a country that is over-governed at all levels, the reality is that New Zealand stands out as the country that is still most held back by its socialistic legacy.

- ***Inflation***

New Zealand got inflation to low levels earlier than Australia, but now there is little between us. Moreover, most of the major countries now have very low inflation rates. In the mid-1990s New Zealand's long-term interest rates were over 100 basis points lower than Australia's, now that relationship has reversed.

- ***Government spending***

The 1980s Labor government in Australia was more disciplined in its spending than its New Zealand counterpart, and the same goes for the Howard government compared with its post-Ruth Richardson counterparts in New Zealand. Spending by governments at all levels in Australia represented 36 percent of GDP in 1997 whereas the figure was probably between 38 and 41 percent in New Zealand. Australia is set to achieve a budget surplus; New Zealand has had surpluses for six years running.

- ***Privatisation***

New Zealand was well ahead of Australia on privatisation in the early 1990s, but no longer. Most New Zealanders would be staggered to learn that privatisations

in Australia since 1990 total over A\$60 billion, and will top A\$100 billion following the sale of the rest of Telstra. The states, led by Victoria, are moving to privatise all or most of their utilities, and a new wave of government service privatisations is extending into education and health. By contrast, most of the electricity system in New Zealand is still owned by central and local government, and New Zealand is well behind Australia in introducing private sector participation in infrastructure such as water and sewerage, roading and airports.

- ***Taxation***

The New Zealand tax system has the advantage of being more simple and broadly based than Australia's but, after a few false starts, there are signs Australia may be about to embark on some decisive reforms. And whereas in 1989 the OECD estimated that New Zealand had the least distorting tax system among its member countries, this is no longer the case: its latest report on New Zealand out this month states that "as a result of tax reform many other countries' tax systems now match New Zealand's."

- ***Trade liberalisation***

In recent years New Zealand and Australia have been tracking along more or less in parallel in abandoning decades of protectionism, and New Zealand appears to be continuing down the straight and narrow whereas Australia has been wobbling badly. It was painful to see Mr Howard embracing Chesty Bond last year and caving in to the car manufacturers. As of last week, all tariffs on passenger motor vehicles in New Zealand were finally scrapped. New Zealand appears to be on a path to full free trade in the near future, although the developments in Australia have revived protectionist sentiments in the coalition partner, New Zealand First. For example, we are hearing the argument that when you get tariffs down to low levels there's not much additional benefit in going to zero. The real benefit, however, is not the short-term efficiency gains but the fact that a free trade rule is less vulnerable to future special-interest industry pleading. As a former chairman of the Industries Assistance Commission was fond of saying, "There's a lot of difference between not being pregnant and being just a little bit pregnant."

- ***Industry policy***

The seemingly interminable and dubious exercises in 'industry' policy in Australia – like the Mortimer and Goldsworthy inquiries, ideas of foreign free trade zones, shipbuilding handouts and other initiatives from Mr Moore and his department – have few counterparts in New Zealand. There was a proposal for \$100 million of business assistance in the coalition agreement but all the New Zealand business organisations said they didn't want it – they wanted lower taxes instead. It hasn't been heard of since.

- ***Agricultural marketing regulation***

Australia has been more successful than New Zealand in removing statutory monopolies and reducing other marketing regulations. A large slab of New Zealand agriculture is still stuck in a defensive posture, reciting the old 'farmer control' mantra, without recognising the benefits of competition and external investment in processing and marketing. However, the pressure is mounting to end these anachronistic arrangements: in last week's budget the government gave our boards until 15 November to come up with plans to operate without statutory backing.

- ***Labour market regulation***

The Employment Contracts Act of 1991 was a substantial achievement; it was a major factor in bringing down the unemployment rate from around 11 percent to around 6 percent by the end of 1996. Regrettably, the new legislation left too much of the old regime on the statute books and instead of giving responsibility for labour law to real courts, the government left in place a specialist labour court which has defied parliament's intention of treating contracts of employment like other contracts. By a series of rulings in areas like dismissals, it has proceeded partially to re-regulate the labour market, and must bear much of the responsibility for the fact that unemployment is once again over 7 percent and trending upwards.

Australia is catching up on labour market reform. Despite the noisy minority pleading for 'solidarity', which is just another way of saying 'we want a labour market monopoly', it seems obvious that the vast majority of Australians are thoroughly sick of labour market regulations that shield indolent and unreliable employees from competition from people who are prepared to work for a living. There are also signs that a more vigorous work ethic is re-emerging: I was interested to see a recent survey which found that the percentage of Australian

employees who confessed to taking 'sickies' (time off work due to a bogus illness) had declined to 4 percent, down from 10 percent in 1995.

- ***Social policy***

Although far from a world leader, Australia is arguably ahead of New Zealand in most social policy areas. Both countries retain state-dominated education and health systems, but spending on these items and superannuation accounts for 17 percent of GDP in New Zealand compared with 13 percent in Australia. There is no evidence that New Zealanders enjoy higher standards of education, health, or prosperity among the aged as a result of this higher spending. To the contrary: in education, for example, international surveys of education performance consistently place Australia ahead of New Zealand. A likely factor in Australia's better performance is the much larger role of the private sector: some 30 percent of Australian children attend private schools compared with under 4 percent in New Zealand (or around 13 percent if integrated schools are counted).

In New Zealand, 24 percent of spending on health is privately financed compared with 33 percent in Australia. New Zealand spends a higher proportion of GDP on welfare benefits than Australia, and has a higher proportion of sole parent families. And Australia has income and assets tested pensions whereas New Zealand has just reverted to universal superannuation: our notion of equity is apparently that millionaires deserve to be supported in their old age by lower income taxpayers.

Looking at this scorecard, my assessment is that in few areas of reform is New Zealand now ahead of Australia, even though some of its policies are of higher quality. Australia has caught up and is ahead in crucial areas. New Zealand's failure to move consistently to reduce the state's domination of the economy is holding back growth of the private sector. When allowance is made for Australia's resource endowments, the quality and depth of its business sector, and its more pro-business and anti-welfare culture, I have little doubt that it will outperform New Zealand in the period ahead unless New Zealand raises its game.

Last week the governments in both countries brought down their annual budgets.

In New Zealand the government finally recognised that its lack of spending discipline since the mid-1990s has done enormous damage to the private sector and the labour market and has curbed its spending plans, but they remain excessive. It has also moved ahead with some microeconomic reform initiatives including accident compensation, statutory marketing boards, roading and education. However, much more needs to be done to make up for the time lost in recent years.

In Australia the government appears to have maintained a firm grip on spending and a budget surplus is in prospect. After a long period of drift last year, it appears to be returning to a reformist agenda, including major tax reforms.

The tax reform agenda is certainly a positive initiative. To a New Zealand observer, perhaps the only surprising thing about the tax debate in Australia is that there is one. As far as the Business Roundtable and many others in the business sector in New Zealand are concerned, the main steps in thinking about tax are pretty straightforward.

- First, the true tax burden is government spending. We have argued that there is a strong case to get government spending down to 20 percent of GDP or below, in order to reduce the economic (deadweight) costs of taxation and eliminate poor quality spending programmes.
- Second, even with a lower government spending ratio at least two tax bases will be needed for the foreseeable future. Therefore a sound consumption tax base is imperative.
- Third, the best consumption tax is a broad goods and services tax (GST). It should have no avoidable exemptions and be at a flat rate. Contrary to many claims, GST is not a particularly regressive tax; rather it is broadly proportional as most people spend what they earn over their lifetimes. The New Zealand GST is a good model, and it is years since it has been the subject of any controversy.
- Fourth, the income tax is becoming increasingly problematical in today's world of open borders. The deadweight losses from the taxation of capital income in particular are very high. I would argue that a major priority for New Zealand and Australia should be to get their top personal and business income tax rates

down, and in the process flatten and simplify the income tax scale. Equity objectives are better pursued through targeted government spending and taxation policies than by universal progressive taxation.

I appreciate that in an Australian context there are also other important tax issues such as federal/state revenue requirements and vertical fiscal imbalance.

Another area where Australia obviously must make progress is waterfront reform. To a New Zealander – and no doubt to a Japanese or any other foreigner – nothing symbolises Australia's economic inefficiencies and the ugly face of Australian unionism so much as the rorts on the wharves. I gather just about every Australian has received the e-mail message that came my way pointing out that thousands of stevedores living at or just below the six-figure salary line might be out of work, and urging recipients to "show they cared" by "sponsoring" a Patrick stevedore. The bit I liked best was the suggestion that you could watch the stevedore of your choice working by visiting your local wharf during normal working hours (between 11.00 a.m. and 11.15 a.m.).

Joking aside, a serious point worth making is that it is years since I have heard anyone in New Zealand referring disparagingly to 'wharfies'. New Zealanders are proud of our port reforms and the huge productivity gains made by port employees. Do Australian wharfies forever want to be social pariahs?

I don't pretend to understand all the complexities of the waterfront dispute, but one thing that seems to stand out is the penalty you pay for going in for half-hearted reforms. The 1980s Labour government in New Zealand knew it should reform the labour market and attempted some legislative changes, but they amounted to no more than tinkering. As a result, few firms were able to make the necessary changes to their operations, and unemployment continued to climb.

By contrast, the Employment Contracts Act resulted from deep reflection about the principles that should govern the operation of the labour market. It is a relatively short and simple statute – the parts of it that matter probably run to no more than 20 pages. Australia's Workplace Relations Act, on the other hand, is a complex and unwieldy statute that runs to 555 pages. Even so, the mistake we made was to leave too much to judicial interpretation. Richard Epstein of the University of Chicago Law School sagely advised us to go for a statute of no more than 2000 words which would have the sole

purpose of instructing courts that their job was simply to apply the common law of contract in the employment context. If we had followed that advice, I believe the unemployment rate in New Zealand would by now have been 5 percent or below – close to the US rate of 4.3 percent. Until Australia implements a much less complex regime I fear it will continue to suffer from dysfunctional workplaces, waterfront-style disputes and high unemployment.

I mentioned earlier that while Australia - New Zealand comparisons are interesting, two countries with the history of ruination chronicled by Geoffrey Blainey are hardly the best benchmarks for each other. The current World Competitiveness Index rankings of New Zealand and Australia by the Institute for Management Development (IMD) are nothing for us to cheer about, unless we are content with mediocrity. New Zealand and Australia are now ranked 13th and 15th respectively out of the 46 countries covered, and New Zealand has lost ground in recent years. Being ranked ahead of Sweden (17th) and Japan (18th) is more a condemnation of their recent performance than an endorsement of ours. Both of us are a long way behind the United States, which is in first position.

In New Zealand, the Business Roundtable has continued to highlight the gap between New Zealand's current performance and its potential, and to press for neutral, economy-wide policies which would help close the gap. I am aware that the National Farmers' Federation has played a similar role in Australia. In his history of the NFF, journalist Tom Connors wrote that in the early 1980s:

... the NFF, as the national voice of farmers saw its mission as influencing the factors ... impinging most on farmer welfare. They were the inflation rate, interest rates, levels of protection for secondary industry, the restructuring of transport and waterfront services, freer world trade, financial deregulation and smaller government outlays to take pressure off interest rates and allow for lower taxation.

The remarkable thing about this list, which the Business Roundtable could subscribe to without altering a word, is that the factors identified as most affecting farmer welfare are factors affecting the Australian economy as a whole. There is nothing here about maintaining subsidies for agricultural industries, marketing boards, drought relief, freight or fuel subsidies or special tax concessions for farmers. There is no special

pleading for public monopolies to be maintained in transport and communications in order to provide subsidies to those living in rural areas.

I have the impression that the NFF has generally been able to maintain an approach that promotes the prosperity of the Australian economy in general rather than seeking to get something for farmers at the expense of others. I know that sometimes you can be let down: I was appalled a couple of weeks ago to see a placard in a photo of New South Wales farmers protesting the native title legislation which read 'Don't deregulate milk!' Your organisation's New Zealand counterpart, Federated Farmers has had occasional bouts of schizophrenia – it set back the cause of postal services deregulation by several years, for example – but generally it has been a solid supporter of economic reform. It is vital for organisations to keep their eyes on the big picture: the benefits to farmers of more efficient infrastructure services like postal services, telecommunications, electricity and roading, which are inputs into everything produced in the economy, vastly outweigh any additional direct costs of services to those in 'the bush'.

Many parts of the rural sector in New Zealand are currently in poor shape. Farm profitability is low, the average age of the farm workforce is going up, and rural services are under threat. Mainly this is the result of the policy failures of recent years, especially the loss of international competitiveness. Partly it is due to self-inflicted injuries, particularly the attachment to producer-owned marketing boards: I sometimes think the barons that run them are determined to hang on until all farmers are turned into peasants. Federated Farmers is very well led, but it has been preoccupied with its internal affairs in recent years. The Business Roundtable has been willing to maintain the often unpopular role of championing economic reform in New Zealand, but we would value more continuous, forceful and well-researched support from representatives of the farming community.

From our side of the ditch, some of us have noticed the outstanding role that Don McGauchie has played in leading the NFF over the past four years. I hope the NFF will continue to be a champion of broad, economy-wide policies that benefit all Australians. Despite the curious views of former prime ministers and academics like John Quiggin, the cause of economic reform in a liberalising direction is now established beyond reasonable doubt. Every OECD country without exception, and many non-OECD countries as well, have moved to free up their economies over the past 20 years. In none of them has the direction of change been deliberately or consciously reversed. The

New Zealand electorate has now voted to maintain the direction of reform in four successive elections, one under a new electoral system. I sometimes wonder whether Australia's economic irrationalists – and we have some counterparts in our universities too – think that all the world is out of step except them.

Undoing decades of ruin in Australia and New Zealand is a massive undertaking, and we can take only limited satisfaction from what has been achieved to date. Both countries are, however, within sight of ridding ourselves of the twin yokes of protection and labour market regulation that did so much to drag them down the per capita income tables. But the most positive statement that can be made about areas such as education, health and the welfare state in both countries is that the potential for improving them is vast. Taking the next steps in reform will require as great a commitment from our governments and as much leadership from business and other organisations as the changes of the past 15 years – and the rest of the world will not stand still while we think about whether to take them.

Lamenting New Zealand's fitful progress in recent years, Richard Epstein wrote in a recent letter:

It is amazing how people think that once you have turned the corner you can then revert to the older, more casual ways, and still avoid a relapse. The clear point is that political institutions have to renew themselves every day. Their rate of depreciation is quite extraordinary.

Those of us who do not want to see Australia and New Zealand revert to their old ways, and who know there is no excuse for not achieving one of the highest living standards in the world again, must keep making this point.