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POLICY BRIEF

Rolling back failed socialist policies in New Zealand; lessons for Washington state

Presentation by Nicholas Kerr
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Introduction

On July 27th, we hosted the regular Washington Policy Center breakfast forum for our supporters at the U.S. Seafoods Building on the shores of Lake Union in Seattle.

We heard a presentation from Nicholas Kerr, who grew up in New Zealand and now lives in Seattle. Like Washington Policy Center, Nicholas is devoted to the idea that public policy should be set on an ethical basis that allows people, to the extent possible, to make their own decisions and learn from their own mistakes. As he explains it:

> *"I love being free. Free to say or do what I want. Free to make mistakes and not expect others to pick up the tab. Free to work hard and reap the rewards."*

For that reason we were particularly excited to hear about his experiences in his native New Zealand and what the people of his country learned when a policy of restrictive socialism was imposed on the economy, and what reforms a popularly-elected government adopted to escape from the policy failures of the past. Here are his remarks in full.

Remarks by Nicholas Kerr

Many of you may be familiar with New Zealand's reforms from an economic perspective, so I'm going to spend more of my talk focused on two other areas:

- How policies before and after the reforms impacted individuals;
- How the key players succeeded in implementing the reforms.

As a young New Zealander in the period before 1984 and the following decade of reforms, I'll be speaking from personal experience about their impact. And I'll be discussing their implementation as the son of an economist who was a key figure in making them come about.

My father, Roger Kerr, was a director of the New Zealand Treasury when the snap election was called in 1984. He and a team of economists drafted a detailed document called Economic Management. This was presented to the incoming Labour Government, which won the election amidst a currency crisis.

Speculators had correctly bet in the closing weeks of the campaign on the likelihood, given the clear need for one, of a post-election devaluation. Several of the party's new ministers were already inclined towards some of the Treasury's policy recommendations. This combined with the crisis meant Economic Management was well-received by some senior ministers, and it is widely regarded as having formed the foundation for the reforms that followed. An indication of how well it was received is that it was subsequently published, something no previous government had done.

Two years after the election, Roger was approached by the chief executives of the country's major corporations who had formed a group called the New Zealand Business Roundtable. They wanted to appoint an executive director and formalize its operations.

He felt it was important that the business community support the reforms and turn their back on their past habits of lobbying for favors and corporate welfare. Under my father, it became a think tank, much like the Washington Policy Center, with a formal mission of advancing policies in the interests of all New Zealanders. It favored free markets and limited government.

Before the reforms

Bryce Wilkinson, one of the authors of Economic Management, described the period before the reforms well: "There was an abundance – of limited choice. Blanket foreign exchange controls, high tariffs, tight import quotas. No new cars for ordinary people. No weekend shopping. Queues to get mortgage finance. Too few licensed restaurants to matter. Union strikes a matter of course during school holidays. Monopolies everywhere."

Government owned all manner of things, including but not limited to: one of the largest hotel chains in the country; both television channels (New Zealand only had two until 1989) and many radio stations; major banks; a steel mill and a publishing house; the country's airports and universities; and, the telecommunications, electricity, airline, rail, and ferry companies.

To help you imagine how stifling government became in New Zealand, let me provide a few of the more extreme examples:

- To protect dairy farmers, for a period of time you needed a prescription from your doctor if you wanted margarine;
- To protect the government monopoly on rail, trucks were banned from carrying loads more than 30 miles – that's from here to Tacoma;
- Bars couldn't open past 6pm, resulting in a culture of binge drinking;
- College wasn't just free; the Government paid all students who attended university – as a result it became a lifestyle choice for many;
- During the oil crisis in the 1970s, the government didn't rely on price controls, it simply banned people from driving their own cars, with a policy known as 'carless days'.

Businesses had become part of the problem

Most businesses in industries the government didn't own had their headquarters in Wellington, New Zealand's political capital. Instead of devoting their attention to innovation and productivity, they spent an inordinate amount of time lobbying for favors, protection and the like.

Impact on individuals

When government owns and controls the majority of the productive economy and business is focused on getting handouts, your choices in life become very constrained. Huge numbers of people become dependent on the state. That's always the case for a country with a significant welfare state, but New Zealand took it much further.

Take Kiwis whose passion in life was engineering. If they pursued a career in telecommunications, the generation or transmission of electricity, television or radio, civil engineering and so on, their only option was government employment.

Moreover, given the state had a monopoly over so many industries, employees had close to zero bargaining power, much like public school teachers here. Young and talented people could only get promotions based on tenure or knowing someone in a position of power – for many, a job well done didn't improve one's position. Naturally many of our best and brightest, who had higher aspirations, chose to leave the country.

Those who remained experienced declining relative living standards as a result of overall low productivity growth. Many jobs provided little satisfaction and generated massive amounts of waste. Some industries had rules limiting who was permitted to do what, resulting in chronic overstaffing and job dissatisfaction.

Work that could be done by one person was often done by two or more people and there were few incentives to be frugal with resources. New Zealand Rail and the post office best characterized these problems.

One of my favorite stories of the era was told by Richard Prebble, a government minister involved in privatizing many state owned enterprises. He wrote about some rail workers who were shunting wagons in the port of Wellington and inadvertently pushed one into the harbor. They sent one of their colleagues into the water with a hook and cable. A few minutes later he surfaced and asked them which of the many submerged wagons was the one they'd lost.

Reforms

Key reforms included:

- Requiring state-owned enterprises to operate like private businesses, including the post office, railways, ferries, and electricity company;
- Many were subsequently privatized, including the hotels, banks, telecommunications company, airline, airports, and ports;
- The floating of the dollar, removal of foreign exchange controls, the reduction of corporate and individual taxes, and the implementation of a broad-based goods and services tax (similar to a VAT);
- The removal of price and interest rate controls, and the elimination or drastic reduction of tariffs;
- The removal of agricultural subsidies;
- The Reserve Bank Act, which made the bank's primary focus targeting inflation.

A second wave of reform by a new government included further privatizations, as well as welfare, health care, education, and labor market reform. The latter abolished collective bargaining and made it easier for companies and individuals to negotiate their own employment terms.

The effect of these reforms was remarkable on the lives of ordinary New Zealanders. A new generation of entrepreneurs emerged as monopolies faced competition for the first time. Productive and satisfying jobs were created. Employees now had choices and bargaining power and could leave bad employers without having to also exit the industry that they worked in. Other choices became abundant too, from restaurants and clothing, to cars and stereos, or from beer and wine, to furniture and appliances.

One somewhat minor but very tangible impact was that student deaths as a result of motorcycle accidents fell because more could afford cheap imported second-hand Japanese cars that arrived on New Zealand's shores by the thousands.

It's also noteworthy that almost all major companies moved their headquarters from Wellington to Auckland, as they abandoned full-time lobbying and instead shifted their focus to more productive enterprises in the nation's most populous city and natural business capital.

Lessons

What New Zealand now has working in its favor is that is has tried big government and New Zealanders know the dismal results all too well. Because of that, the major parties, reflecting the will of the people, don't want to turn back the clock on any of the key reforms from this period.

That's not to say the parties don't want more government spending, but the areas they want it in are generally ones where there was no reform or where reform wasn't far reaching – for example, policies advocating more government spending usually focus on areas like education, health care, welfare, and housing.

This is the challenge I think Seattle in particular and Washington more generally face – big government on a scale New Zealand experienced has never been tried in our state. People here are more willing to believe that government can solve our problems.

It's also neither easy nor desirable to fabricate a crisis to create an opportunity for a series of reforms. But there are some lessons that I think we can take from New Zealand's experience.

1. Broad support matters for long-lasting policies.

In order to build support, debate is necessary. There was much opposition to many of the reforms, including protests by farmers who wanted to keep their subsidies and unions who opposed privatization, labor market reforms, and more.

But on the other side of the debate were large numbers of politicians, business leaders, and interest groups who spoke in support of the reforms. The public saw this, understood the reforms, and there was broad acceptance when they were implemented, even if for some it was reluctant at first.

Indeed, the Labour government was handsomely reelected after its first three years of reform and fiscal consolidation. When it lost reform momentum during its second term, it was kicked out of office. The National government came in and implemented the labor market and other reforms I've mentioned. Following this, they also won another term.

As a result, no one wants to roll back any of these policies. Contrast this approach to governing with the way President Obama operated and it's easy to understand why his legacy is in a shambles.

2. Order matters

The order in which you implement policies is important. For example, it would have been better if labor market deregulation was one of the first reforms. We suffered high unemployment initially as the labor market could not adjust quickly to the shocks of the other reforms. But politics is, of course, about the possible.

3. Good policy can be good politics

Many individuals or families became rich running businesses that were sheltered by soaring tariffs or other protections. In the case of cars, the few local manufacturers and dealers became wealthy selling vehicles to the privileged at the expense of ordinary New Zealanders who were unable to afford new cars. There was little opposition to the removal of the restrictions that protected them.

4. The simpler the policy, the lower the risk of future politics

New Zealand's GST applies to ALL goods and services with a single flat rate, initially 10% and currently 15%. Australia, on the other hand, picked and chose which goods would be taxed. As a result, it's a political football with parties running on policies to remove or lower the tax on certain items to appeal to sectional interests.

5. Good politics can give you room for reform

The Labour government threw a bone to the left wing of its party – a nuclear-free policy which at the time had little in the way of economic consequences. This enabled it to maintain the support of some on the left wing of the party and continue with its economic reform agenda. (Arguably it hurt the country in the long run. For example, New Zealand wasn't part of the Australian free trade agreement with the USA in 2004, something that would have been unthinkable pre-1980.)

6. Play the long game

The Business Roundtable's first major policy paper made the case for labor market reform. It took two elections and a new government before it received the attention it needed. But it's proof of Voltaire's adage that nothing is more powerful than an idea whose time has come. The work that the Washington Policy Center does is important. Even if the policies it advocates for are ignored by those in power today, good ideas win out over time.

7. Business leadership matters

This final lesson is also the one I believe is most important and relevant to Seattle and Washington state. Too often here businesses and their leaders sit on the sidelines or are too late to the debate to make any difference. The most shameful example of this in recent times was the representative of the Seattle Chamber of Commerce on the mayor's $15 minimum wage advisory board abstaining from even voting on it.

Overcoming obstacles to reform

Let me offer a quote from an editorial this year following the death of the second chairman of the New Zealand Business Roundtable, Sir Douglas Myers:

"The Roundtable's leadership was so effective that most New Zealanders came to believe business was always solidly behind the economic reforms. Not so. A protected economy is a very comfortable place for companies with an import license or an established local market closed to foreign suppliers.

"… It is only economists who worry about the cost-plus pricing and wage inflation that protection permits, sending the country and its economy into long-term decline until its creditors will no longer enable it to sustain a high living standard."

The editors are right to acknowledge that the Roundtable was very much alone amongst business organizations in the early days of the reforms. The Manufacturers Federation, along with many other business sector lobbies, were reluctant to face the risks of deregulation and open competition.

It was only over time that they along with the major chambers of commerce slowly came around to supporting the reforms and even began collaborating with the Business Roundtable on policy papers advocating further reforms.

Another obstacle the organization faced was the media. There were a few notable exceptions around individual policies, but generally speaking opinion pages up and down the country were opposed to the economic reforms. One major daily paper went so far as to have an editorial policy opposed to them.

The Roundtable instead used the news pages of the press to advance the cause. That required speeches by the chairman, deputy chairman, and other member chief executives of major corporations. The media could seldom ignore these. Op-eds signed by the same business leaders were also frequently submitted and published. Years of these efforts as well as the education and cultivation of the opinion page editors turned the tide, resulting in more sympathetic editorials.

The Roundtable also had few supporters in academia. Its approach was to debate university professors in the media or on campus. In the long run, the policies that were implemented generated the expected results and these were inevitably contrary to the predictions of academics who opposed them. Some ate humble pie, conceded they were wrong and changed their tunes. Others that were more defiant suffered reputationally and slunk into irrelevancy.

Another key communication strategy was to fly out distinguished and supportive academics from overseas, including Australia, the US and UK. They would deliver speeches, as well as meet with ministers, the press, and others interested in their areas of expertise. These foreign experts were more than able to dispense with the criticism of local academics and helped level the playing field for the policy debates.

Faceless business groups are insufficient – their members and leaders need to tirelessly advocate policies and make the case for reform. As the editorial I quoted from earlier noted:

"Speaking up for further reform was not for the faint-hearted. Myers did so knowing it would not make him popular. He had no personal need to do it… He did it because, as all who knew him can attest, he fiercely loved this country."

New Zealand and New Zealanders are wealthier and freer for his and his fellow business leaders having done so.

Conclusion

Washington's trajectory, if not corrected, has it on a slow but steady course towards less freedom and ever bigger government. The inevitable consequence is the sort of country New Zealand became after decades of similar policies.

In 1900, New Zealand had the highest GDP per capita in the world. It now ranks around 32nd, even after years of improvement following its economic reforms. The unending growth in government and the increasing restrictions on individual liberty here have predictable consequences. New Zealand's experience suggests ways we can reverse this course.

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If you have any comments or questions about this study, please contact us at:

Washington Policy Center
PO Box 3643
Seattle, WA 98124-3643

Online: www.washingtonpolicy.org
E-mail: wpc@washingtonpolicy.org
Phone: (206) 937-9691

About the Author

Nicholas Kerr is a contributor on the Sound Politics blog and writes about public policy on his own blog at nkerr.com. He lives in Seattle with his young family.

He grew up in New Zealand during the economic reforms of the 1980s and early 1990s, which sparked his interest in the power of free markets and the importance of individual liberty.