A rowing boat on the open sea, or in a haven from financial and environmental crises?
New Zealand, the GFC, and a union response

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> *Small open economies are like rowing boats on an open sea. One cannot predict when they might capsize; bad steering increases the chances of disaster and a leaky boat makes it inevitable. But their chances of being broadsided by a wave are significant no matter how well they are steered and no matter how seaworthy they are.*[1]

New Zealand, an island nation of 4.4 million people and 268,000 square kilometres in the southern Pacific Ocean, is associated with a history of social progress including being one of the first countries in the world to give women the vote and to build a welfare state. Though the beginnings of the welfare state were in the late 19th and early 20th century, its comprehensive form was put in place during and following the global Depression of the 1930s by the social democratic Labour Party which gained power during the Depression having been formed with strong union involvement. A high level of unionisation was supported by compulsory unionism, and later unqualified union preference, along with varying forms of arbitration and central wage setting. This progressive image did hide the state's origins as a British settler colony built on the confiscation of land from the indigenous Māori people throughout the 19th century. This led to their widespread poverty, demoralisation and threatened loss of culture throughout most of the 20th century. It is only in the last 25 years that these historical grievances have begun to be seriously addressed.

Nonetheless, by the 1950s New Zealand had one of the highest incomes per capita in the world along with consistent and genuinely full employment. This was substantially built on agricultural exports to its former colonial master, the United Kingdom, and a growing, highly protected manufacturing sector. Its economic structure of internationally efficient agriculture, manufacturing protected by import controls and tariffs, foreign exchange and capital controls and a strong welfare state enabled management of domestic demand, prices and wages. However the entry of the U.K. into the then European Economic Community signalled the end of New Zealand's historical dependence on U.K. markets. Coupled with the international oil crisis of the 1970s, the economy contracted and in the face of inadequate responses from a series of governments, a balance of payments crisis was used to justify radical neoliberal reforms by a government that took power in 1984.

[1] "Boats, planes and capital flows", by Joseph Stiglitz, *Financial Times*, London (U.K.), 25 March 1998, p.32.

This paper sketches the actions this and following governments took to embed neoliberalism into the New Zealand economy, public institutions and ideology, and the results in terms of its economy and society. Though the grip of neoliberalism was modified in the first decade of this century, its social and economic failure formed the basis for the development of an Alternative Economic Strategy in the New Zealand union movement through its peak body, the New Zealand Council of Trade Unions (CTU). The paper describes the thinking behind this strategy and outlines its policies.

The coming of neoliberalism to New Zealand[2]

The neoliberal government that came into power in 1984 was paradoxically a Labour Party government. This led to major splits in the party and is an important context for the current situation in the 21st century. The neoliberal reforms were hailed by advocates as perhaps the most pure example of those policies anywhere in the world. They put into place a radical agenda of deregulation of many parts of the economy including the financial sector; the corporatisation and eventual sale of many parts of the state in a society where large portions of industry and commerce had been built up by both central and local government; major changes to the taxation system including reducing personal and company income taxes in favour of a near-comprehensive value-added tax (Goods and Services Tax or GST); the systematic introduction of "new public management" and private sector accounting standards into the remaining public service, decentralising operations and encouraging competition in the public education and health sectors; the removal of subsidies on staple consumer goods and to farmers; and opening the economy by the removal of tariffs, import controls, and currency and capital controls, including a pure float of the currency.

As a result of the extreme deregulation, the international sharemarket crash in 1987 hit New Zealand worse than most countries. Over the next few years, major New Zealand companies including a major bank collapsed and the sharemarket has never recovered fully: it briefly recovered to 1987 levels in 2007 but has fallen again since. Due to both the sharemarket crash and the removal of tariffs and import controls, unemployment rose steeply, reaching 8.8 percent at the end of 1990. Inflation peaked at 18.3 percent before being brought down sharply by the Reserve Bank when in 1989, legislation gave it independence and instructions to focus solely on price stability and a "sound and efficient" financial system.

Public splits in the government and continuing economic turmoil led to a resounding defeat of the Labour government in 1990, by then onto its third leader of the period, later WTO Director General Mike Moore. It was replaced by New Zealand's main conservative party, the National Party, which by then was also dominated by purist neoliberals. The National Party government from 1990-1999 continued the neoliberal programme. It made savage cuts to social benefits and introduced new anti-union labour legislation. The programme of deregulation and increasing use of market mechanisms for public services and infrastructure intensified, along with further widespread privatisations. The deregulation of international trade and investment accelerated, removing most of the remaining tariffs, opening many services to international competition, and removing further controls on overseas investment.

[2] For more detail, see "The New Zealand Experiment: A World Model for Structural Adjustment?", by Jane Kelsey, Auckland University Press, Bridget Williams Books, 1995 (also published as "Economic Fundamentalism: The New Zealand Experiment – A World Model for Structural Adjustment?", Pluto Press); and "Reclaiming the Future: New Zealand and the Global Economy", by Jane Kelsey, Bridget Williams Books, 1999.

The 1984-90 Labour government had already carried out some labour reform which weakened unions, but left in place a form of compulsory unionism and industry-wide awards that covered both union and non-union workers in an industry. The new National Party government labour legislation which came into force in 1991, called the Employment Contracts Act, was largely written by employers' representatives and was an extraordinary attack on the rights of working people and their ability to organise. It outlawed strikes over multi-employer agreements, effectively limiting the formation of collective employment agreements to a single enterprise. The word "union" appeared only once in the Act, in a transitional provision. The process for recognising and registering unions was abolished and unions were regarded simply as incorporated societies. Instead, employees would be represented by so-called "bargaining agents" who could include lawyers, organisations created by the employer, or people setting themselves up in business for the purpose. Industry awards were abandoned. Individual employment contracts were promoted, and all collective employment "contracts" automatically became individual contracts on expiry.

The new structure had the desired effect. In 1990, there were approximately 720,000 workers whose minimum pay and conditions of employment were determined by an award or a collective agreement. By 2000, only 421,400 workers could be identified as being covered by collective agreements. The proportion of casual and fixed term contracts, contracting out and similar insecure employment arrangements grew. Illegal "sweatshops" appeared. They often used illegal immigrants, confiscating passports, and avoiding minimum wage, tax and other liabilities. For the entire March 1991 to December 1999 period the growth in full time employment was less than half that for part time jobs.

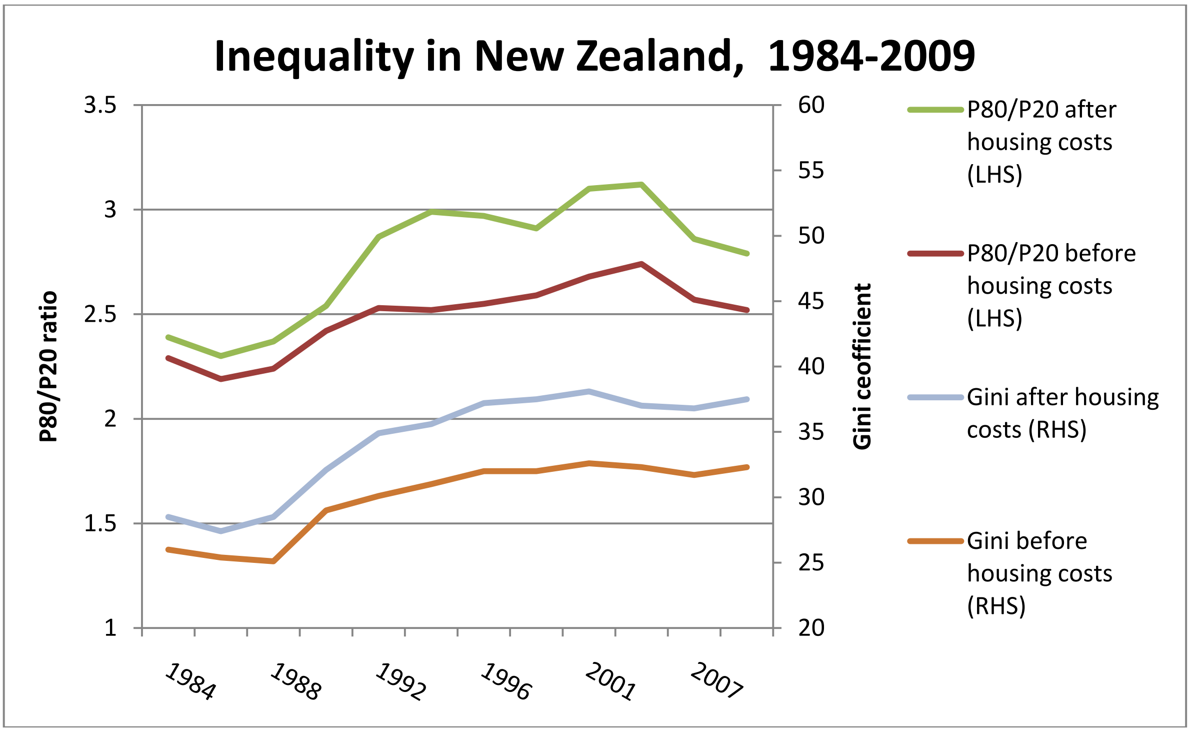

Figure 1: P80/P20 and the Gini coefficient are measures of household income inequality[3]

[3] "Household incomes in New Zealand: trends in indicators of inequality and hardship 1982 to 2009", by Bryan Perry, Ministry of Social Development, Wellington, August 2010, p. 139, ISBN 978-0-478-33500-2 (Print), ISBN 978-0-478-33501-9 (Online), available at http://www.msd.govt.nz/about-msd-and-our-work/publications-resources/monitoring/household-incomes/index.html (accessed 6 September 2010).

It came close to destroying the union movement. The reduction in union membership in New Zealand in the 1990s was the most extensive in the world. It halved as a percentage of the potential membership, falling from 43 percent of wage and salary earners in 1991 when the new legislation came into force, to 22 percent in 2000 when the legislation was replaced.

The effects of the neoliberal programme included many people thrown out of work in manufacturing as firms closed in response to international competition, greatly increased poverty levels, particularly as a result of the high unemployment levels throughout the period and the savage cuts in social benefits, and stagnating or falling real wages as businesses used unemployment and their greatly increased bargaining power to refuse wage increases. Inequality rose at the fastest rate in the OECD over the period (see Figure 1)[4]. The only remaining state wage intervention, the minimum wage was allowed to fall relative to the average wage (Figure 2). Unemployment peaked at 11 percent at the time of the introduction of the Employment Contracts Act. A New Zealand Treasury paper[5] noted that wage levels fell from roughly comparable to Australia in the 1980s to 60 percent of their level by 2002 and that “with labour relatively cheaper in relation to capital than in Australia, it appears that New Zealand firms have opted for a lower level of capital intensity”. Between 1992 and 1996, the relative price of labour to capital fell by 22 percent.

Many of the privatisations were disastrous failures which led to asset stripping or expensive failed overseas adventures rather than improved services. Some such as the national airline, Air New Zealand, and New Zealand Rail were later reversed at considerable cost; others, such as Telecom and the electricity system, present continuing problems of regulation. Reversal is made more difficult by the deep commitments made in international trade agreements.

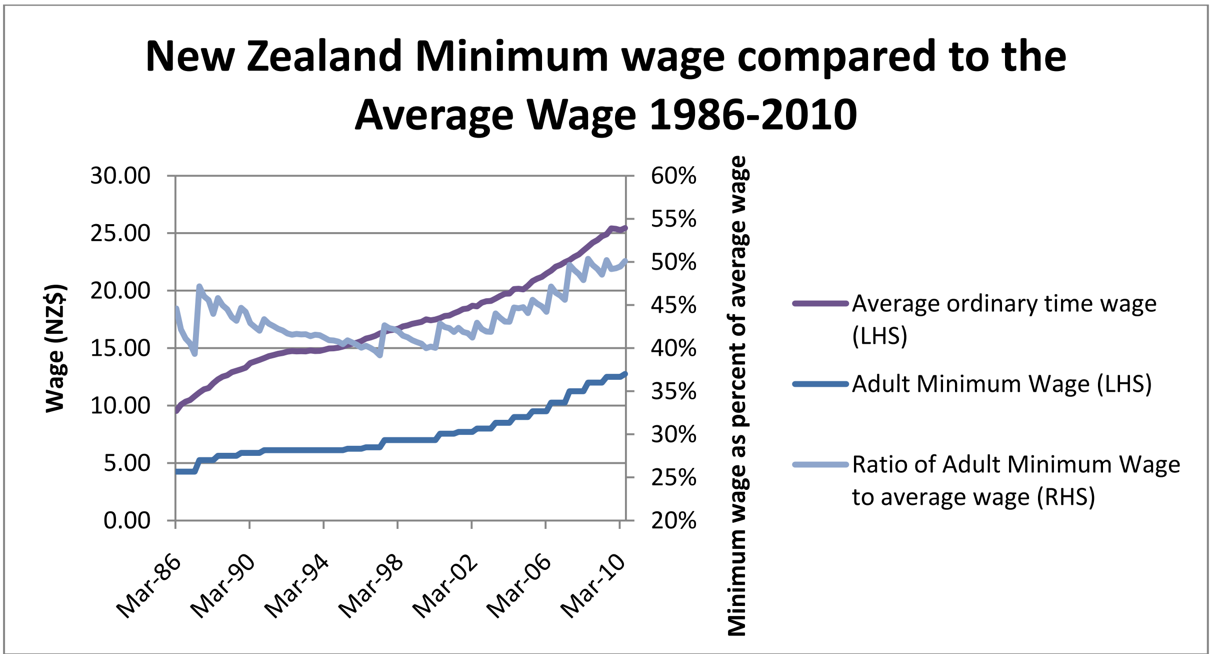

Figure 2: Movements in the Minimum Wage

[4] “Household incomes in New Zealand: trends in indicators of inequality and hardship 1982 to 2009”, by Bryan Perry, Ministry of Social Development.
[5] “Productivity in New Zealand 1988 to 2002", by Melleny Black, Melody Guy and Nathan McLellan, New Zealand Treasury Working Paper 03/06 June 2003.

The National Party was voted out of power in 1999. By then, Labour Party supporters had forced a change in its political programme. It turned to a "Third Way" position similar to the British Labour Party, though with a strong allergy to privatisation. In addition, the electorate had voted in 1993 to change the electoral system to a multi-member proportional representation system similar to that in Germany. In 1999, Labour was easily the largest party but did not gain a majority and formed a coalition with a left party, the Alliance, consisting in part of former Labour supporters alienated by its actions from 1984-1990, but with backing from union, peace movement, Social Credit, and environmental activists. The Alliance split over the government's decision to send troops to Afghanistan and its vote collapsed. In each of the next two elections Labour formed coalitions or support arrangements with minority parties. It was voted out in the last election, in 2008.

Over that period it reversed some of the damage of the 15 years that preceded it. It was initially helped by economic growth which was among the strongest in the OECD. It largely stopped the privatisation programme, renationalised Air New Zealand and the rail system and created a new retail bank, Kiwibank, which proved highly popular. It rebuilt parts of the public service. In 2004 it introduced a system of tax credits ("Working for Families") which favours people who are in work and have families, and made a significant difference in halting the increase in inequality for those in work. However poverty among those relying on welfare benefits, including many children, remains a major problem. Benefit levels have been substantially unchanged in real terms since they were severely cut in 1991. The government emphasised return to work for all beneficiaries capable of it. For example, the income replacement rate provided by the unemployment benefit is well below the minimum wage. Even a couple are entitled to only 36 percent of the average wage and 72 percent of the minimum wage, but single people receive as little as half that.

The government maintained consistent budget surpluses – a policy that put New Zealand in an advantageous position when facing the global crisis – using some of the surplus to build an investment fund to contribute to future payments on the universal pension scheme, New Zealand Superannuation, as the population ages.

The Employment Contracts Act was replaced with the Employment Relations Act 2000 which is a moderate reform and not a restoration of the past systems of awards, arbitration and compulsory or unqualified preference unionism. It recognises union rights, acknowledges that there is unequal bargaining power between employer and employees, encourages collective bargaining, provides for voluntary union membership, is based on the principle of good faith in employer-union relationships, and promotes mediation as the preferred way to resolve problems. Later amendments made multi-employer

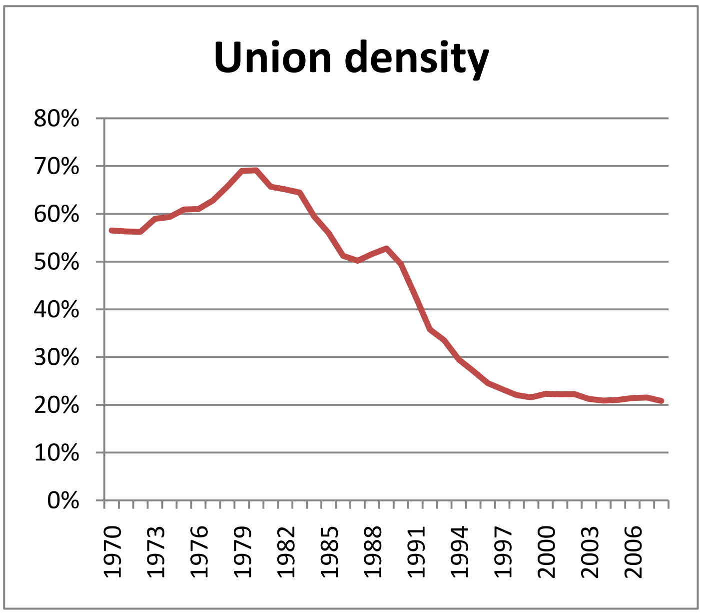

Figure 3: Union density (source: OECD)

collective agreements more feasible, and gave some protection to employees caught up in the sale of businesses.

Annual leave entitlements were increased from 3 weeks to 4 weeks, paid parental leave improved and a process was initiated to eliminate occupational income inequalities due to gender. The government increased the minimum wage each year from 2000 by substantially more than inflation (see Figure 2). Studies have shown no damaging side effects. From 2008, it raised the much lower youth minimum rate to the adult rate. Labour also encouraged concepts of tripartite social partnership, with union and business representatives present in many aspects of policy development and implementation. Nonetheless, while union membership grew, it failed to increase its proportion of the employed workforce and union density levelled (see Figure 3).

However the Labour-led government's fiscal, monetary and international trade policies were in many ways a continuation of those of the previous governments. While it had an enormous task before it in 1999 to repair fifteen years of embedded poverty and damaged public services and community relationships, many were disappointed that it was not more ambitious in carrying that out. It continued previous policies of an independent Reserve Bank focussed on price stability, which contributed strongly to very high interest rates which have weakened productive investment and encouraged speculative investment, particularly in residential property. It continued enthusiastically to pursue preferential trade and investment agreements with strongly deregulatory provisions, signing ones with Singapore, China, Chile and Thailand, and intensifying a longstanding one with Australia. It took no substantive steps to control overseas investment, international capital movements or the exchange rate, and indeed locked in the very liberal existing rules through the international agreements it signed.

New Zealand's international economic relationships are central to its economy due to the country's small size and geographic isolation. Since capital and exchange controls were removed in the 1980s, its international liabilities have ballooned and at March 2010 stood at 185 percent of GDP in gross terms and 89 percent in net terms. The dividend and interest income from this has driven a chronic current account deficit reaching up to 9 percent of GDP in the last decade, a position which has only improved as a result of the recession lowering company profits and imports.

Improving the New Zealand's value-added export performance is therefore crucial. However this has been weak. The Labour-led coalitions took a relatively active role in economic development, with a strategic industry focus including provision of advice and small grants for market development and similar purposes, and tax concessions for research and development. There is very little room to provide assistance to developing firms and exporters within the constraints of political views and official advice that still strongly favour market based solutions and international trade and investment agreements that severely limit options. As a result, New Zealand's exports are still heavily dependent on lightly-processed land-based commodity exports. The economy is becoming increasingly reliant on China and Australia for export markets, now accounting for around a third of New Zealand's trade in both directions. Exports to China are currently buoyed by high international food prices, particularly dairy and logs, with demand driven further by scandals in China's domestic dairy industry. Australia is New Zealand's principle market for manufactured exports, but in turn is very dependent on growth in the Chinese economy.

The National Party was re-elected in 2008, and has led a coalition with a small far-right neoliberal party (ACT – Association of Consumers and Taxpayers) including some former Labour Party architects of the 1984-1990 reforms, and the Māori Party which is based on indigenous rights and values and is showing the tensions of trying to represent both growing Māori corporate influence and a longer standing constituency of low income Māori who are a disproportionate part of the Māori population. The new government has not taken the austerity approach of its 1990s predecessor, but has focussed so far on regressive tax reforms which have increased consumption taxes, flattened personal income tax scales, and lowered corporate taxes, while removing some of the tax system's bias in favour of property investors. Regulatory reform is another significant area of activity. A central plank of its election policy was income parity with Australia by 2025, and it has set up a commission dominated by neoliberal economists and bankers to propose policies and monitor progress towards that end. So far, New Zealand has fallen further behind Australia whether measured by real wages or GDP growth.

The National-led government responded to the recession by bringing forward some infrastructure spending including school buildings, home insulation and roading projects, some targeted labour market programmes, and tax cuts, leading to deficits which are forecast to run until the year ended June 2015, resulting in increasing government debt levels. These are being used to justify severe constraints on government spending, with most departments being told they will not get even nominal increases in funding, although welfare and pension payments are still being indexed. Public services are therefore under severe pressure.

While it promised to continue a social partnership relationship, the National-led government currently has legislation before Parliament to reverse significant aspects of Labour's industrial legislation. These would allow all employers, theoretically with the worker's agreement, to remove a new worker's rights to appeal (take a personal grievance) against dismissal in their first 90 days, having introduced this for small employers within weeks of gaining power; significantly tilt personal grievance procedures in favour of the employer; give employers greater power to oppose union access to workplaces; and encourage employers to undermine the union during bargaining by communicating directly with union members. This has put the relationship with unions under severe stress.

New Zealand is now weakly emerging from recession. GDP in the year to March 2010 was 0.4 percent less than the previous year but was positive for the four quarters to March. However unemployment, which peaked at 7.1 percent in December 2009, is still at 6.8 percent and expected to fall only slowly. Other indicators are very mixed, with more robust recovery far from certain.

Unsuccessful in its own terms

Neither the radical programmes of the 1980s and 1990s nor the Third Way model of the 2000s have led to economic success even in neoliberal terms. The OECD has noted (in its economic survey of New Zealand in 2003) that "the mystery is why a country that seems close to best practice in most of the policies that are regarded as the key drivers of growth is nevertheless just an average performer". Real growth in national output (GDP) has been intermittent and despite periods where it exceeded the OECD average, including years during the last decade, has failed to keep up: in terms of national output per person (GDP per capita) New Zealand has steadily fallen further behind in OECD rankings (see Figure 4).

Labour productivity has risen more slowly than Australia and most of the OECD. It has been held back by insufficient investment (low capital intensity: see Figure 5) and low multi-factor productivity, suggesting ongoing problems with quality of management and investment in the skills, experience and production-specific knowledge which workers bring to the job.

International competitiveness has been problematic: New Zealand's international goods and services trade has been in deficit for most of the last decade and the importance of international trade in the economy is above the OECD average but lower than many other small economies. As a result of trade liberalisation, exports have lower value-added than prior to the 1970s according to a recent study[6].

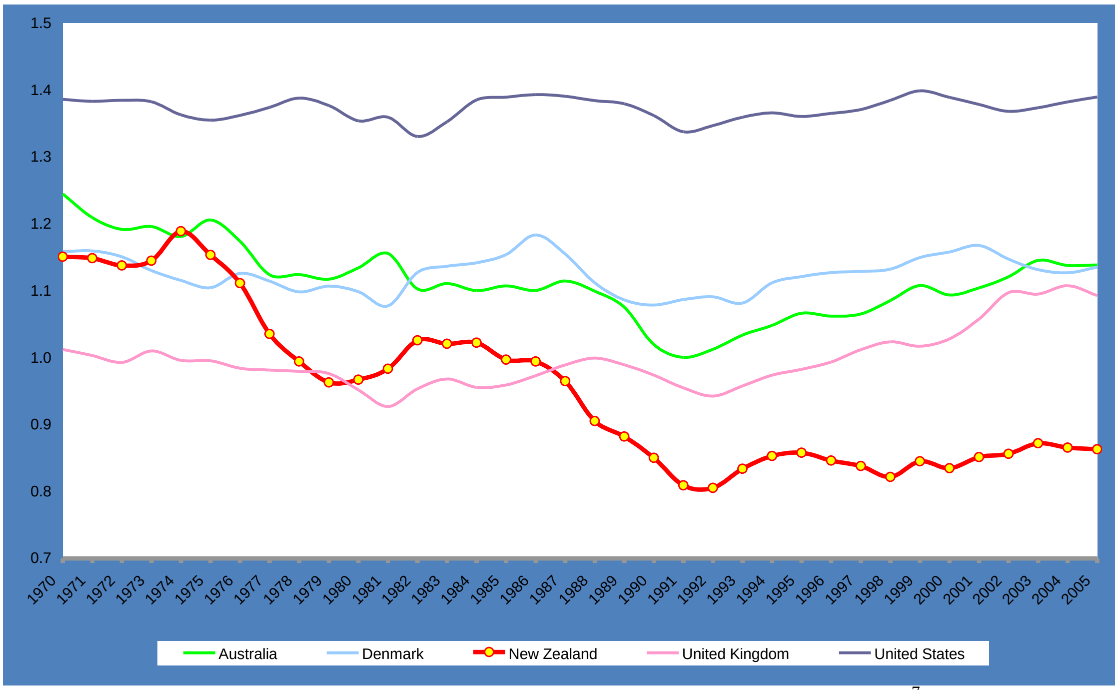

Figure 4: Real GDP per capita as proportion of OECD average[7]

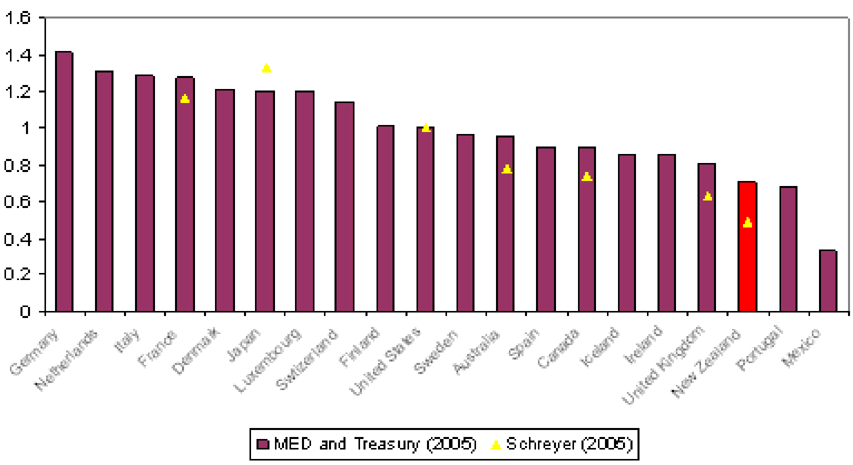

Figure 5: Low Capital Intensity: OECD countries in 2002 (capital per unit of labour)[8]

[6] "Economic progress and puzzles: Long-term structural change in the New Zealand economy, 1953-2006", by Ralph Lattimore, Trinh Le, Iris Claus, and Adolf Stroombergen, NZIER working paper 2009/6, October 2009.
[7] Economic Development Indicators 2007, Ministry of Economic Development, Treasury, Statistics New Zealand , Figure 1.6, p.23.

Overseas investment and the bank system

One of the greatest successes of the neoliberal regime has been in attracting overseas investment. New Zealand has one of the highest concentrations of foreign direct investment in the developed world, equivalent in 2008 to 42 percent of GDP compared to an average of 25 percent in other developed economies and the world as a whole. But the direct investment into New Zealand has been of low quality, usually in the form of takeovers rather than new "greenfield" investment introducing new technology and creating employment. According to the United Nations[9], there were an average of only 24 greenfield foreign investments a year between 2004 and 2008. That compares to an average of 163 a year approved by the official regulator, the Overseas Investment Office, and many more that escape its scrutiny. During the 1980s and 1990s, foreign direct investment was associated with the problematic privatisations already noted: the sale of privatised state assets "accounted for approximately 42% of total inbound investment to New Zealand over the decade [1986 to 1996]"[10]. From the late 1990's, a large part has been private equity and investment company buyouts of many important New Zealand companies, usually quickly resold in highly indebted condition. A 2008 Treasury paper acknowledged that "some analysts argue that New Zealand receives substantial foreign direct investment inflows but has yet to benefit from spillovers [of expertise and new technology into the rest of the economy]"[11]. That is not surprising given the nature of the investment.

Another part of the overseas investment has been, as noted above, exceptionally high levels of international debt. All of this is private debt (the government currently has net overseas assets). The dividends and interest on those debt and equity investment liabilities in most years count for virtually the entire current account deficit and have given New Zealand one of the highest current account deficits in the OECD. It exceeds the contribution of primary industries – the backbone of the country's exports – to the output of the economy.

Though the sovereign portion of the international debt will rise as a result of the fiscal deficits run as stabilisers during the recession, New Zealand was left by the outgoing government with strong government accounts including net assets and a history of budget surpluses. There is therefore considerable room for stimulus

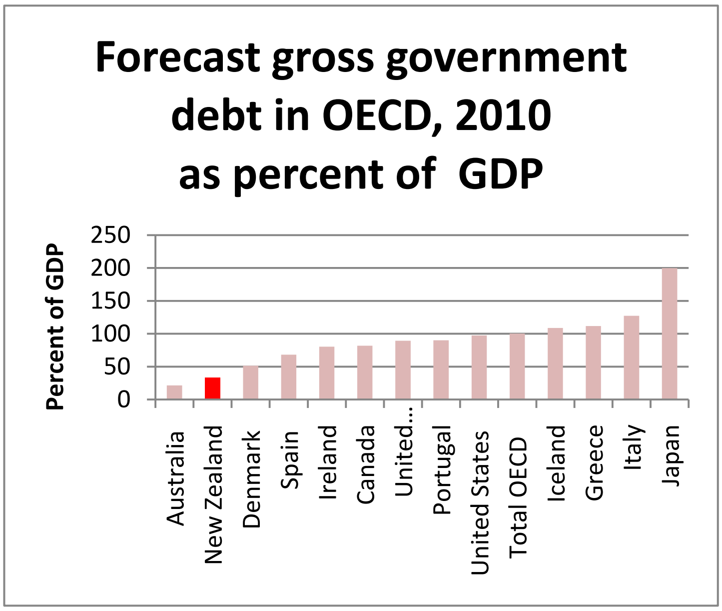

Figure 6: New Zealand government debt compared to OECD, 2010 forecasts (Source: OECD)

[8] "Investment, Productivity and the Cost of Capital: Understanding New Zealand's 'Capital Shallowness'", New Zealand Treasury Productivity paper 08/03, April 2008, p.6.
[9] "World Investment Report 2009", UNCTAD, September 2009, p.212.
[10] "Inbound Investment: Facts and Figures", Foreign Direct Investment Advisory Group, August 1997, p.6.
[11] "Investment, Productivity and the Cost of Capital: Understanding New Zealand's 'Capital Shallowness'", New Zealand Treasury Productivity paper 08/03, April 2008, p.19.

programmes, and the union movement has expressed concern the government is not doing enough given continuing high unemployment (6.8 percent at June 2010), sluggish recovery in output, and the dangers inherent in the international economy.

There is increasing concern expressed that despite the international debt being private, it will lead to credit downgrades or capital flight, though there is some suspicion that this concern is politically driven to justify lower government spending given the considerably lower sovereign debt levels in New Zealand compared to the rest of the OECD (see Figure 6).

The role of the banks in the unhealthy accumulation of international debt is at the heart of understanding New Zealand's response to the Global Financial Crisis (GFC). The banking system is heavily dominated by four Australian owned banks. They hold 92 percent of bank assets in New Zealand. Over the last decade they borrowed heavily on short term (typically 90-day) international money markets in order to finance domestic loans, mainly for mortgages on residential buildings. At 31 March 2010, banks owed 49 percent of New Zealand's gross international liabilities, 74 percent of its net liabilities, 62 percent of its gross international debt and 79 percent of its net debt. This international borrowing severely weakened the Reserve Bank's ability to control New Zealand's money supply. As a result, before the GFC, it raised the official cash rate to a peak of 8.25 percent in July 2007, where it stayed until June 2008. The high interest rates caused the value of the New Zealand dollar to rise well beyond that needed for balance in goods and services trade, and choked off productive investment in favour of speculative investment in property and leveraged buyouts. The New Zealand dollar is the 11th most traded currency in the world in April 2007 according to the Bank for International Settlements[12], despite New Zealand conducting only 0.2 percent of the world's goods and services trade. The annual volume of trading in the New Zealand dollar is 240 times the trade in goods and services. Between 1990 and 2010, house prices rose 122 percent, more than twice as fast as consumer inflation of 56 percent. The fastest price growth was between 2000 and 2010, when house prices rose 59 percent (and 58 percent between 2000 and 2008 alone) compared to 30 percent consumer inflation[13].

The weakened tradable goods and services sector leaves New Zealand's exports dominated by commodities with low levels of added value. Open capital markets and monetary policies targeting only consumer price levels using interest rates have created an unsustainable international position.

The four Australian banks also dominate the Australian financial sector, and that position is protected through a "four pillars" policy in that country which prevents merging or overseas takeover of those banks. The banking system in both countries largely remained stable during the GFC. A threat did arise to New Zealand's banking system however. When international money markets froze, the four Australian banks were unable to refinance their short term debts as they fell due, threatening their liquidity. The Reserve Bank of New Zealand was forced to step in to arrange lines of credit for the banks. There were also concerns about runs on banks in both countries when European governments began to guarantee their banks' deposits. In response, both Australia and New Zealand instituted guarantees on domestically owned deposits in banks and in non-bank financial institutions.

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[12] "Triennial Central Bank Survey", Bank for International Settlements, December 2007, p. 11. http://www.bis.org/publ/rpfxf07t.pdf.

[13] Statistics New Zealand - capital price index for dwellings and outbuildings, and consumer price index, at March.

While the Australian and New Zealand banking systems survived the financial crisis relatively unscathed, it is not clear that was due to the quality of supervision and regulation. For example, one of the banks active in both countries, ANZ, was in fact involved in similar practices to the US banks through its half-owned associate, ING (NZ) Ltd. Two of ING's managed funds led to large losses for 13,000 investors, 2,800 of whom invested in the funds as customers of ANZ. The banks also use off-balance sheet entities[14] and have engaged in huge tax-avoidance strategies in New Zealand, demonstrating their willingness to be ruthless in search of profit. So it was not that high-risk practices were prevented in the two countries' systems, but that there appears not to have been the incentives for the behaviour that led to them becoming widespread elsewhere.

A former Governor of the Reserve Bank of Australia, Ian Macfarlane, has suggested the main reasons may be the lack of competition between the Big Four banks and (paradoxically) the lack of savings in Australia. Low savings in both Australia and New Zealand meant the banks did not have the funds to invest in the high risk US markets. He thought "they would have if they could have". As a result, one commentator described the relative stability of the two banking systems as "dumb luck".[15] Other observers have made similar observations including the chief executive of ANZ's New Zealand subsidiary[16].

New Zealand also has a much smaller financial subsector consisting of finance companies which largely made higher risk loans such as to property developers, motor vehicle purchasers or personal loans. A spectacular series of collapses in that sector began well before the GFC, and continued just weeks ago with the failure of one of the largest of these companies, South Canterbury Finance, calling on around NZ$1.6 billion of government guarantees. One estimate is that investors and depositors in these companies have lost over NZ$6 billion in addition to the latest failure, the great majority of them not guaranteed. Causes included fraud, incompetence and excessive risk taking. The subsector was lightly regulated, and there were failures in the regulation and monitoring that did exist. Both these events and the GFC show the failure of the market to behave responsibly in the absence of strong regulation.

The crisis has also shown that any one of the four Australian owned banks and even the larger of finance companies were "too big to fail". As has been seen elsewhere around the world, the New Zealand financial system demonstrably depends on government support.

The Reserve Bank has looked for ways to reduce the probability of a recurrence of the exposure of the financial system to the Australian banks' high reliance on overseas borrowing using innovative liquidity controls which force the banks to increase their use of domestic funding. It is too early to tell how successful it will be.

The effects on people – wages

[14] See for example http://www.converge.org.nz/watchdog/15/06.htm.

[15] "Saved by dumb luck", by Alan Kohler, *Business Spectator*, 2 March 2009, http://www.businessspectator.com.au/bs.nsf/Article/Foundational-fluke-$pd20090302-PR559, accessed 6 March 2009.

[16] "Warning on new bank regulation", by Roland van der Bergh, *Dominion Post*, 21 September 2009; and "Easy money saved the day", by Ian Verrender, *Dominion Post*, 25 June 2009, p.C4, reprinted from the *Sydney Morning Herald*.

Ordinary time hourly wage and salary rates as measured by Statistics New Zealand's Labour Cost Index fell by 1 percent in real terms between 1992 when this index was first recorded and 2009. To go back further the average ordinary time wage must be used. It additionally reflects recognition given to individual workers in their pay and changes in the composition of employment in the economy. It increased only 18 percent in real terms in the 29 years

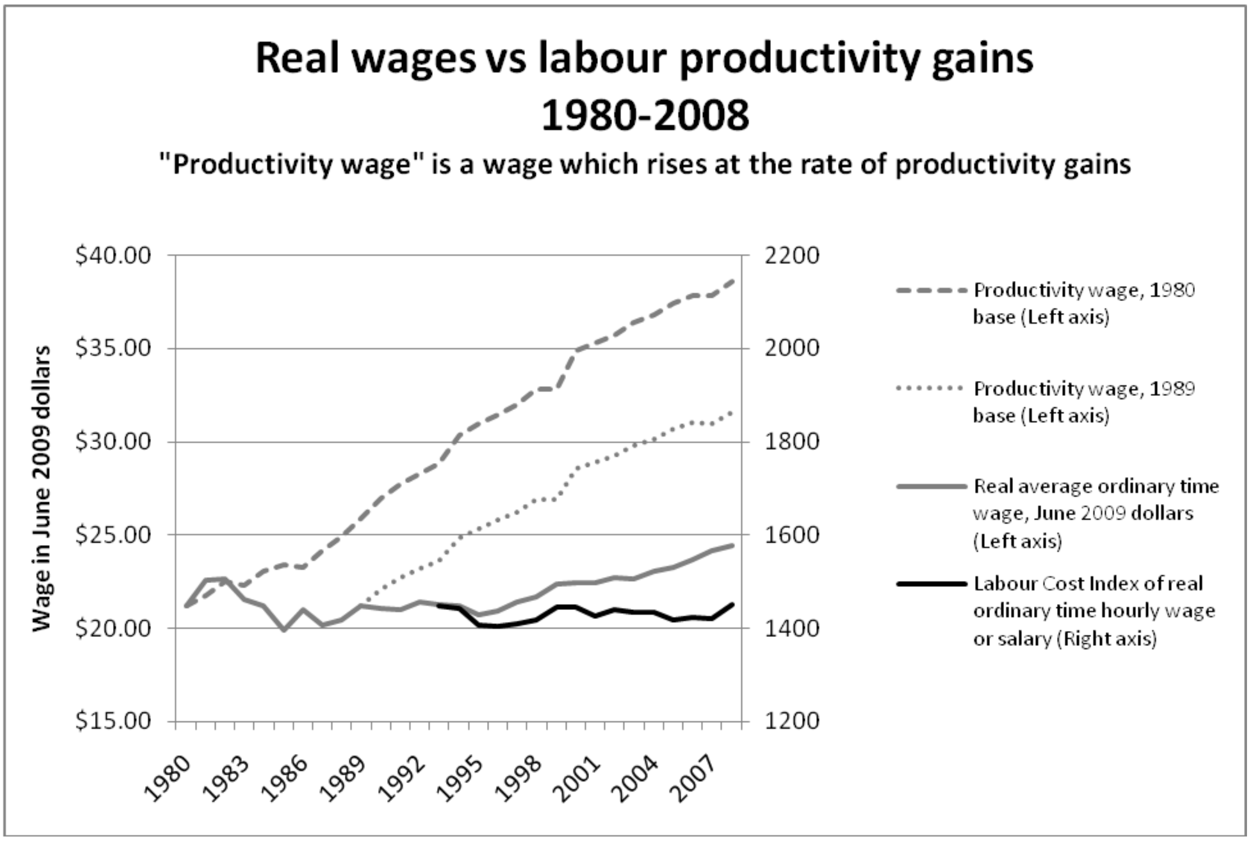

Figure 7: Productivity and wages

from 1980 to 2009. If wages had reflected labour productivity increases however, wages in 2008 could have been around 56 percent higher than they were. Even if we look only at the 20 years from 1989, real wages still rose 18 percent to 2009, and a real wage 28-31 percent higher could have been justified in 2008 by productivity gains (see Figure 7).

In other words, business took almost all the gains of labour productivity. There has been a long term shift in the balance between income to employees and returns to capital ("Gross operating surplus" or profits and interest, in Figure 8). Until 1993, employees received a greater (though rapidly falling) share of the economy's output than capital did. From 1994 until 2006 the position was reversed. Part of that was growth was rising numbers of self-employed due to

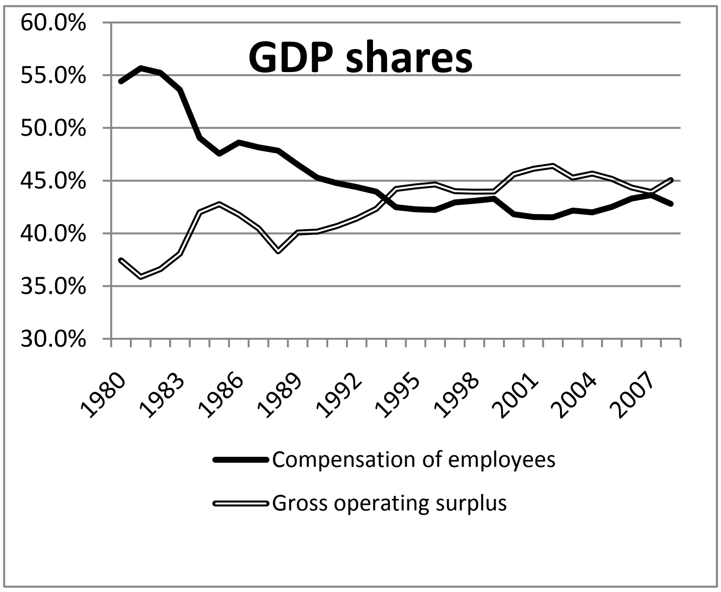

Figure 8: Shares of GDP going to employees and profits

employees being forced into contracting rather than employment relationships, but part was simply the fall in real wage and salary incomes and increased unemployment. The imbalance in how the growing production of the economy is shared (which also shows up in New Zealand's high levels of income inequality) is clearly a systemic issue which got steeply worse until about 2002 when capital received a record 46.4 percent of GDP. After that, the imbalance moderated but has a long way to go to return to historical levels.

The low wage structure led to reliance by business on low wages rather than increases in productivity through investment. For example, Deardorff and Lattimore[17] found in 1999 that

> By 1986, the importable [that is, import substituting] sector supported by trade barriers, was both more capital intensive than the exportable sector and more intensive in all categories of higher labour skills than exportables... This group had nearly halved by 1996 as the tradeable sector shed labour during the early phases of the economic reforms. ... The results suggest that trade liberalisation, trade agreements and improved market access over the decade 1986-96 might have actually improved the distribution in the sense of raising relative returns to employees with lower qualifications and, presumably, lower wages.... The traded goods sector is not intensive in the use of employees, of either sex, with degrees or advanced tertiary training.

Poverty

High levels of poverty have become an unwelcome feature of New Zealand society which had previously prided itself on its absence of beggars and strong social protections to prevent poverty. It showed up in the permanent existence of charity food suppliers ("food banks") and inadequate housing. It was also exposed in the increasing appearance of health problems due to poverty and overcrowded living conditions, including meningococcal disease, rheumatic fever, pneumonia, chronic lung infection, gastroenteritis, ear disease, dental disease and serious skin infections.

Poverty rose steadily through the 1980s but then jumped – on some measures, doubled – in 1992 due to draconian cuts in benefits, high unemployment, and falling real wages following the deunionisation driven by the Employment Contracts Act. Poverty peaked in 1994, when one measure showed 26 percent of the population in poverty. It levelled out or fell (depending on the measure used) slowly until 2001 when it rose again, peaking at 2004 when the Working for Families package brought about a decline. In 2009 up to 18 percent of the population could be described as living in poverty[18]. Working for Families made a difference for people with paid work but not for low income households whose main source of income is from an income-tested benefit or the universal pension, New Zealand Superannuation.

Children have been particularly affected by poverty. At its peak in 1994, over a third of children – 36 percent – were in poverty by one measure. It followed a similar pattern to the whole population during the 1990s, rising again to 2004, and falling or levelling since then. In 2009 up to one in four children – 25 percent – were living in poverty[18].

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[17] "Trade and Factor-Market Effects of New Zealand's Reforms", by Alan Deardorff and Ralph Lattimore, New Zealand Economic Papers, June 1999 v33 i1 p71.

[18] "Household incomes in New Zealand: trends in indicators of inequality and hardship 1982 to 2009", by Bryan Perry, Ministry of Social Development, Wellington, August 2010.

Environment

These are only some of the economic and social effects of neoliberal policies on New Zealand. There are also increasing environmental challenges for New Zealand and the world. Locally, New Zealand faces problems of increasing pollution of its rivers due to intensive farming practices, and problems of waste disposal around its cities. Conservation land and the rare native species which depend upon it are under threat in many places. Globally, there are similar threats but two of the most fundamental are the increasingly apparent limits to potential oil resources, and climate change. Environmental sustainability must therefore be integrated into a economically and socially sustainable world view.

The CTU's Alternative Economic Strategy

Joseph Stiglitz, in the words that opened this paper, wrote that "small open economies are like rowing boats on an open sea." Certainly this metaphor applies to New Zealand, and yet the policies of successive governments appear to have disregarded this self-apparent situation in the interests of the vested interests and powerful forces which benefit from neoliberalism. The events leading up to and following the GFC make this plain. "One cannot predict when they might capsize; bad steering increases the chances of disaster and a leaky boat makes it inevitable," Stiglitz continues, and this paper has documented at least three decades of either bad steering or faulty design. The outcomes that have been documented should be seen as inevitable. Not only must New Zealand reduce its vulnerability to the open sea, but it must be fair to all who rely on her for their livelihoods and dignity.

Affiliates of the CTU asked it to develop an alternative political economy in response to the above developments. Some unions are affiliated to political parties, but all recognised that the policies being followed by the Labour-led government, while better than what had gone before, were not doing much more than putting a halt to further worsening of the situation as this analysis records. In some areas gains were made; but in others there were continuing losses. The GFC and the change of government not only gave greater impetus and relevance to the project, but opened up possibilities that for many years had been effectively closed down as areas for valid policy alternatives.

A draft "Alternative Economic Strategy" (AES) with a substantial background paper covering the causes of the GFC and similar ground to the above was provided to delegates to the CTU's biennial conference in October 2009, along with a briefer discussion paper. Workshops gave delegates an opportunity to discuss and comment on the proposals. It was then sent out for further comment for six months, workshops were held with interested union members and at workplaces. Comments were collected from a number of external groups including a range of experts, environmental groups and political parties. The final version was approved by the CTU's executive body, the National Affiliates Council, in August 2010. At time of writing, it is being prepared for publication.

The AES is based on principles, explained more fully in the document, of Fairness, Participation, Security, Improving Living Standards, Sustainability, and Sovereignty. The policy is structured around three "pillars": Sustainable economic development; Decent work and a good life; and Voice: real participation in decisions in the workplace, economy and community. In this paper only its broad directions can be described.

It begins with a section which addresses the immediate needs flowing from the continuing effects of the GFC. While these have shorter term objectives, they are designed to support longer term development described in the rest of the policy. They include small-scale active labour market policies, strengthened public services, infrastructure development, both through central government and in collaboration with local governments, increased access to tertiary education, support for businesses under certain criteria, publicly owned (state) house building, extended home insulation and clean heating programmes, and encouragement of local manufacturing and services through government procurement and other measures. The section also calls for immediate changes to the financial system to reduce New Zealand's vulnerability to international financial crises and demands of overseas investors, including supporting international calls for clamping down on the shadow financial economy, a Tobin tax, and the recommendations of the Commission of Experts of the President of the UN General Assembly on reforms to the international monetary and financial system. Locally, it proposes management of international capital movements, a managed exchange rate, and an end to further concessions in trade and investment agreements which would further reduce New Zealand's policy space: "financial services, investment, intellectual property, measures that constrain our ability to protect the environment, or services such as health and education which require public regulation or provision or are important for New Zealand's economic, social or cultural development."

Sustainable economic development

For the longer term, it responds to the central need for the New Zealand economy to develop more value added products and services, and to strengthen the tradable sector as contributions to raising wage levels and restoring balance in external payments. It takes a strategic approach to economic development, giving priority to certain broadly defined sectors of the economy along with cross-sectoral themes such as being environmentally beneficial or high productivity, and supports national and regional infrastructure plans. Economic development would include support for firms subject to strong criteria that reinforce national strategies, skill development, employment relations policies, worker participation and improved wages and working conditions. In New Zealand, size of firms is an ever-present issue when considering exporting, and a review of competition laws is proposed. Specifics in infrastructure development are outlined and include greater state involvement in New Zealand's problematic telecommunications and electricity markets, development of public transport, and a "human infrastructure" fund to provide long term funding certainty to tertiary education and workplace training. Other areas covered include innovation, research and development, gaining from new technology, productivity, education and skill development, the use of government procurement as a sustainable economic development tool, support for Māori economic development, an integrated approach to immigration, regional development, and support for cooperatives.

As mandated by the state of New Zealand's financial system and the GFC, there is considerable space given to changes to the financial system in order to support rather than hinder economic development. This includes closer oversight over all financial institutions in proportion to their use of leverage and systemic significance, recognising the implicit state support that has been revealed by the GFC. Proposals include legislation for separation of commercial and investment banking, control of executive and shareholder remuneration, a Financial Activities Tax, requirements for regulatory approval for high risk financial services, whether from New Zealand or abroad, reduced reliance on overseas funding, and a statutory basis for future bailouts and deposit guarantees. Actions to reduce vulnerability to the four

Australian banks which dominate the New Zealand banking system include scaling up the small but very successful government-owned bank, Kiwibank, ensuring the national payments system is not dependent on any of the big four banks, reviewing Reserve Bank powers, and banning offshore outsourcing of banking infrastructure. Social responsibility is addressed, and proposals are made for funding of firms which currently suffer from lack of suitable finance, including a development finance agency which includes unions in its governance, locally raised long term infrastructure bonds, greater local investment by New Zealand sovereign and superannuation funds, and expansion of savings through changes to voluntary superannuation schemes.

Monetary policy has caused great difficulties for productive investment and exporters, in part because of its effect on the exchange rate. The AES proposes broadening the aims of monetary policy, and giving the Reserve Bank sufficient powers to manage capital flows and the exchange rate, enabling the exchange rate to be pegged (but not fully fixed). It suggests that mechanisms in addition to interest rates should be used to implement monetary policy.

Internationally, the AES advocates working with others to control capital movements and reverse constraints within trade and investment agreements such as those that heighten the risk of further financial crises and constrain our ability to protect the environment, or services such as health and education which require public regulation or provision or are important for New Zealand's economic, social or cultural development. It seeks a "new internationalism" which recognises that many important factors require cooperation rather than a market approach. For New Zealand this would include a new generation of trade and investment agreements with rules founded on the need to regulate and to recognise national economic development strategies and the role of the public sector, rather than founded on concepts of market access and deregulation. It advocates democratisation, transparency and accountability of global institutions currently dominated by US and EU, and a greater role for the UN and UNCTAD in international economic and financial policy making to balance social with commercial imperatives.

Given its social democratic past and the sweeping and often disastrous programmes of privatisation that New Zealand has experienced, the role of the state is a critical one. The AES affirms the role of the state as regulator, stabiliser, redistributor, and owner of parts of the economy. Government procurement and responsible contracting are identified as important tools for spreading good practice and economic development. The role of public service workers, the need for public services to meet the needs of citizens, and the need to recognise the different nature of public organisations from the private sector in governance, management, accountability and financial accounting are raised.

Taxation is addressed particularly in the light of its redistributive role given the big increases in inequality in New Zealand over the last three decades. Proposals include a tax-free band or rebate for low income earners, and restoration of higher rates of income tax at high income levels. It proposes to replace the regressive GST with other forms of tax including asset taxes, a Tobin tax, a Financial Assets Tax and commercial resource use taxes. Pollution taxes, including for greenhouse gases, are advocated, as long there is balance to ensure low income earners do not pay an unfair share of the burden. A review to improve the welfare system; addressing tax avoidance; a variety of proposals on company tax; and a capital gains tax are among other proposals.

There is a range of proposals to combat climate change including a price on emissions, but with credits to ensure the international competitiveness of companies is not compromised unfairly. The AES advocates support for workers and communities displaced or otherwise affected by climate change or policies to combat it, major investment in skills for a low carbon economy, worker participation in the approaches taken to climate change in the workplace, and union involvement at all levels in decision making on the changes required.

The AES also advocates finding alternative measures of progress to use alongside GDP to guide decision making and priorities.

Decent work and a good life

The CTU is working on a parallel strategy of "Union Change" to rebuild the New Zealand union movement. This is acknowledged and its principles integrated into the AES. It includes extending union coverage and collective bargaining beyond those in large and more readily unionised workplaces, a rights-based framework for coverage by collective agreements, participation of unions and workers in their workplace and industry, mechanisms for national and industry level employment standards setting, new forms of worker organisations, and a more structured approach to social partnership.

Under employment, the AES adopts some northern European ideas on flexicurity, including a high level of income replacement if out of work, active labour market policies, and financial and practical support for acquiring new skills. It places full employment as a central objective of government policy.

Given the crucial role of housing not only as an essential for living, but also in investment behaviour in New Zealand, considerable attention is devoted to housing, acknowledging the complexity of the area. It is based on the development of a National Housing Strategy and quality lower cost housing. Retirement, which is important both for individuals and for the economy in terms of the savings accumulated in preparing for it, is also addressed.

Finally this "pillar" addresses equity and the need to reduce inequality (which is also integrated into the rest of the policy). The former includes gender equity in pay and employment, extending paid parental leave, making more flexible working arrangements available, and increasing the minimum wage to 66 percent of the average wage.

Voice: real participation in decisions in the workplace, economy and community

This pillar advocates a fuller view of democracy than a vote once every few years in an election. This includes fuller consultation by central and local government with social partners (unions and business) and other affected groups. It proposes ways for the workplace to be seen as a place for active citizenship, such as providing access to local government and community organisations to hold lunch-time consultation sessions.

It calls for more room for diversity and depth in the media through trust-owned, not-for-profit "public service" newspapers and other media, and funding for investigative journalism.

Finally, the AES proposes structures to increase worker participation, recognising it as part of good management practice, but also as a way to make full use of the skills and experience of employees. It proposes participative representative structures at the workplace level; industry sector councils to share good practice around productivity, skill development, industry development initiatives, and networking of firms; and a National Tripartite Social/Economic Council.

Conclusion

The AES can be seen as a development of a variety of social democratic policy strands, borrowing much from successful northern European countries, but also integrating a level of environmental sustainability and, most topically, addressing the challenges of the GFC. It is specifically designed around the situation in which New Zealand finds itself: one of dual failures. There is the failure of neoliberalism both domestically and internationally. There is a failure of the dominant political parties and economic orthodoxies (strengthened by powerful vested interest) to consider substantive alternatives. Many parts of the Strategy require long term effort and resources, but it is hoped that it provides a coherent alternative that addresses many of the needs of working people and the problems of the crisis-ridden economic environment in which we find ourselves.

It would be unrealistic in the face of these powerful forces to expect that New Zealand could be in a haven entirely protected from financial and environmental crises, but it certainly could be made less vulnerable to them. The rowing boat that is New Zealand would then be more secure and provide a better life for those who rely on her.