Focusing on Growth

Closing the income gap
with Australia by 2025

Second report of the 2025 Taskforce

2025 TASKFORCE

November 2010

2025 Taskforce

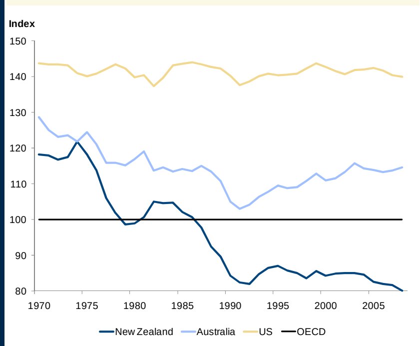
Established in 2009 by the National and ACT Confidence and Supply agreement

"Our vision is to close the gap with Australia by 2025"
– *Hon John Key, Prime Minister*

Role:

- make recommendations
- report annually on progress

GDP per capita relative to the OECD, 1970 – 2008



Source: OECD, OECD = 100, current prices and PPPs

Our first report (2009)

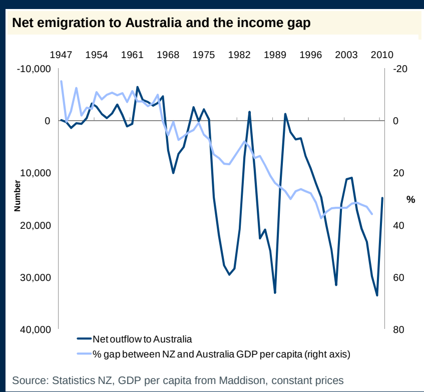
- Closing a 35% gap is possible – but demands far reaching and urgent reforms:
  - Reduce government spending
  - Lower tax rates
  - Rigorous testing of new government spending proposals
  - Get government out of owning trading enterprises
  - Better quality regulation
- We stand by these recommendations
- **Second report: Articulate the underpinnings**

Why does the gap matter?

“She’ll be right”?

- Last year we estimated the gap at 35%. OECD: Gap likely to be 42% by 2025
- **Standard of living**: Better houses, health care, education, infrastructure, etc
- **Opportunities in NZ**: Another 400,000+ NZers could emigrate to Australia by 2025

Challenge: Grow 2% per capita faster than Australia each year for the next 15 years



Net emigration to Australia and the income gap

Source: Statistics NZ, GDP per capita from Maddison, constant prices

Can we do it? Yes we can, but...

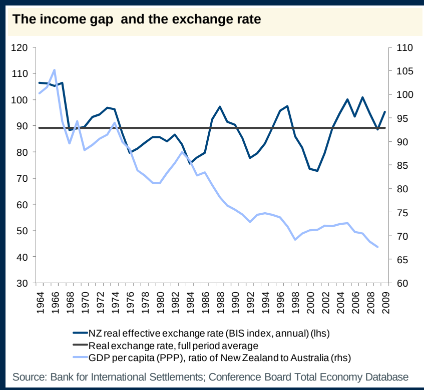
- Some positive steps in the last year, e.g.
  - Cuts to personal tax rates
  - Regulation: RMA, employment law, aquaculture
- But also some negative steps, e.g. higher taxes on some types of business investment
- We don't yet have the policies to achieve the 2025 goal: Governments need to consistently make choices that will increase growth

Response to our critics

- "The global economy is more complex"
  - Fundamental drivers of growth have not changed – we need higher productivity across the economy
- "Our small size and isolation determine our (poor) performance"
  - Evidence does not support this – we can grow much faster if we choose to adopt world-leading policies
- "1980s solution to a 2010 problem"?
  - We've looked at the latest growth literature and stand by our recommendations

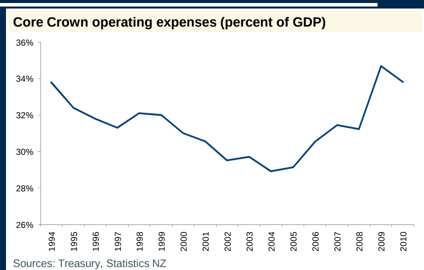
Competitiveness: A long-term problem

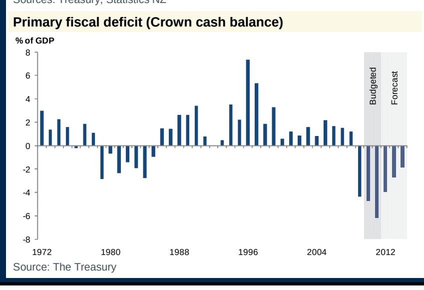
- A high exchange rate is a good thing… in a high-performing economy
- NZ has under-performed for decades – our exchange rate hasn't adjusted as it needed to
- Lifting our growth performance means strengthening the real ability of our firms to compete
- **This report is about putting the economy on a much more competitive footing**



Focusing on growth means...

1. Lower government spending, early return to structural surplus:
   - Faster growth through lower taxes
   - Lower real exchange rate to boost competitiveness of firms
   - Reduce build-up of debt



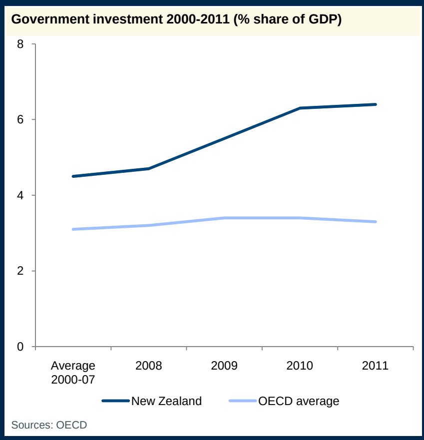


Focusing on growth means...

2. Shift the boundary between public and private sectors:
   - Sell state-owned trading enterprises (in whole or part) to unleash "dynamic efficiency gains"
   - Greater use of public-private partnerships
   - More choice in health and education by increasing scope for private contributions
   - Assist beneficiaries into productive work

Focusing on growth means...

3. Require rigorous and transparent analysis of infrastructure investments
   - Infrastructure programme is large and growing
   - Can assist growth – or can be wasteful
   - Systematic and <u>public</u> disclosure of analysis
   - Only projects where benefits exceed costs should proceed



Focusing on growth means...

4. Create the environment in which firms <u>want</u> to do more R and D

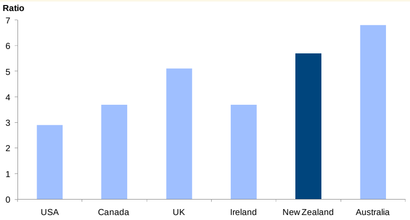
- Improve return from existing investment
- Stop micro-managing research and tertiary education
- Remove special protections; simplify governance; enable productive competition, mergers, takeovers; allow sector to evolve

Focusing on growth means...

5. Reduce regulatory barriers to investment and innovation

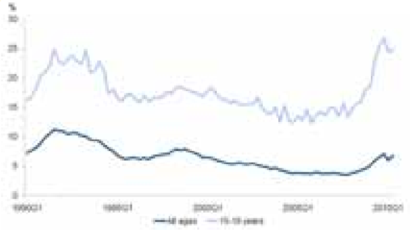
- Need world-beating policies if we aim to attract top talent, ideas, private investment
- Good start but need for much more, notably...
- RMA; cost of housing; labour market / youth minimum wage; agricultural innovation

House price to income ratio, selected countries, 2009



Source: Demographia (ratio of median house price to median household income)

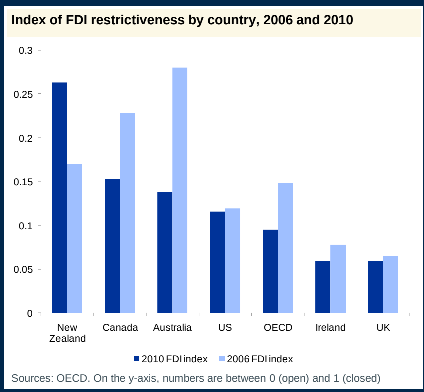
Unemployment rates in New Zealand



Source: Statistics NZ, seasonally adjusted

Focusing on growth means...

6. Welcome foreign investors on same terms as domestic investors
   - OECD: NZ has shifted from being one of the most open to one of the least open countries
   - Remove uncertainty in overseas investment regime
   - Lead public debate – benefits of foreign investment are large but poorly understood



Focusing on growth means...

7. Create world-leading institutions to strengthen the durability of good policy
   - Better long-term management of public spending – reduce the risk of unproductive expenditure during the good times
   - Raise the bar – reduce the risk of ad hoc solutions to perceived problems without full analysis of costs and benefits
   - Create institutions that will assist in
     - Limiting government spending, e.g. independent fiscal council, taxpayers' Bill of Rights
     - Limiting costly regulations, e.g. Regulatory Responsibility Act

Key messages

- Closing the gap is achievable – provided we are serious about doing something about it
- The longer we leave it, the harder it will get – and probably more costly
- Growth drivers haven't changed: people and firms generate wealth – governments need to create the environment and not unnecessarily stand in the way
- Assess all policies and legislation against the objective of significantly lifting growth – and decide accordingly
- **To grow 2% faster than Australia, our policies need to consistently be the best in the world**