

Growing the New Zealand economy: The need for domestic capital

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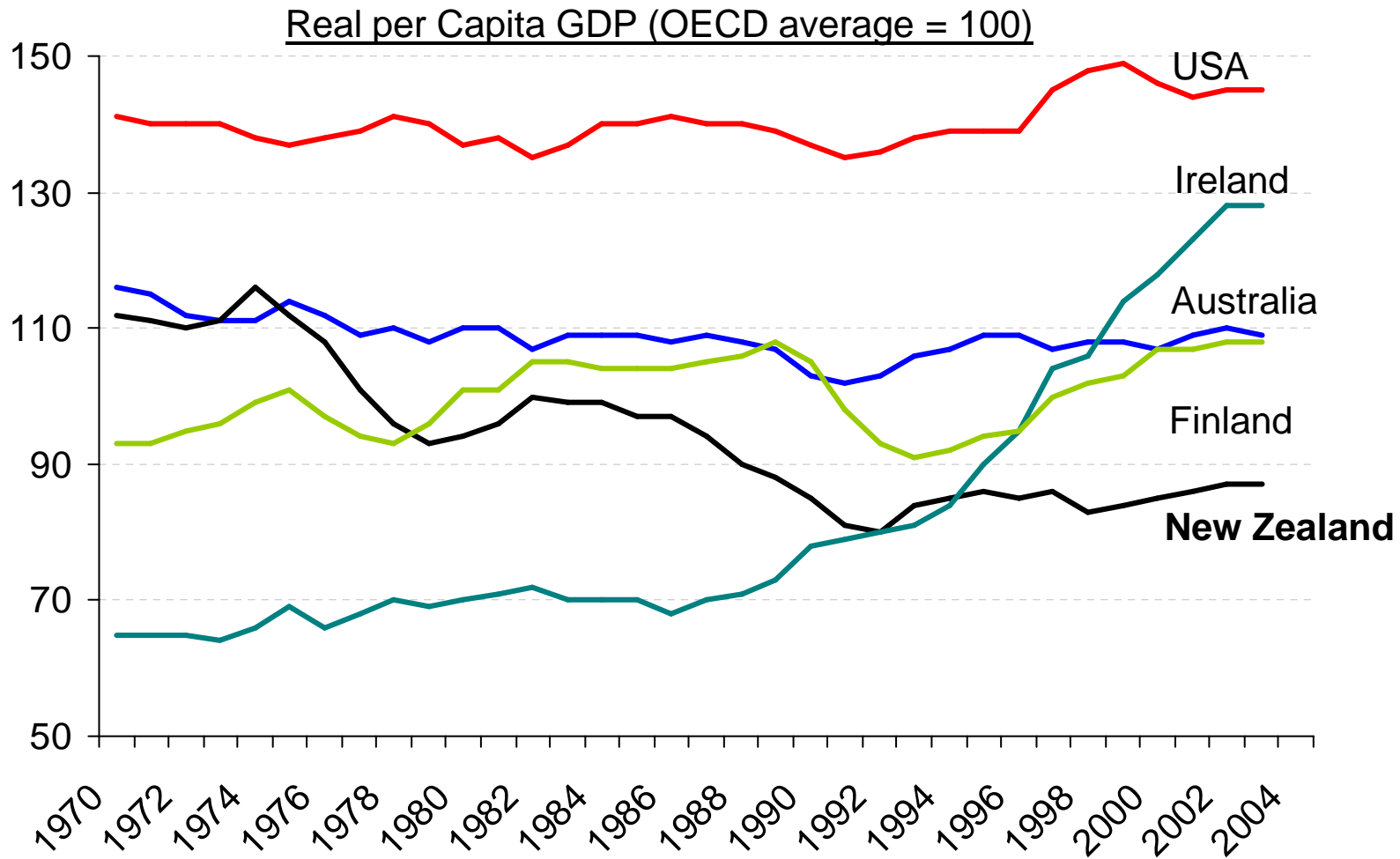
June 2006

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AGENDA

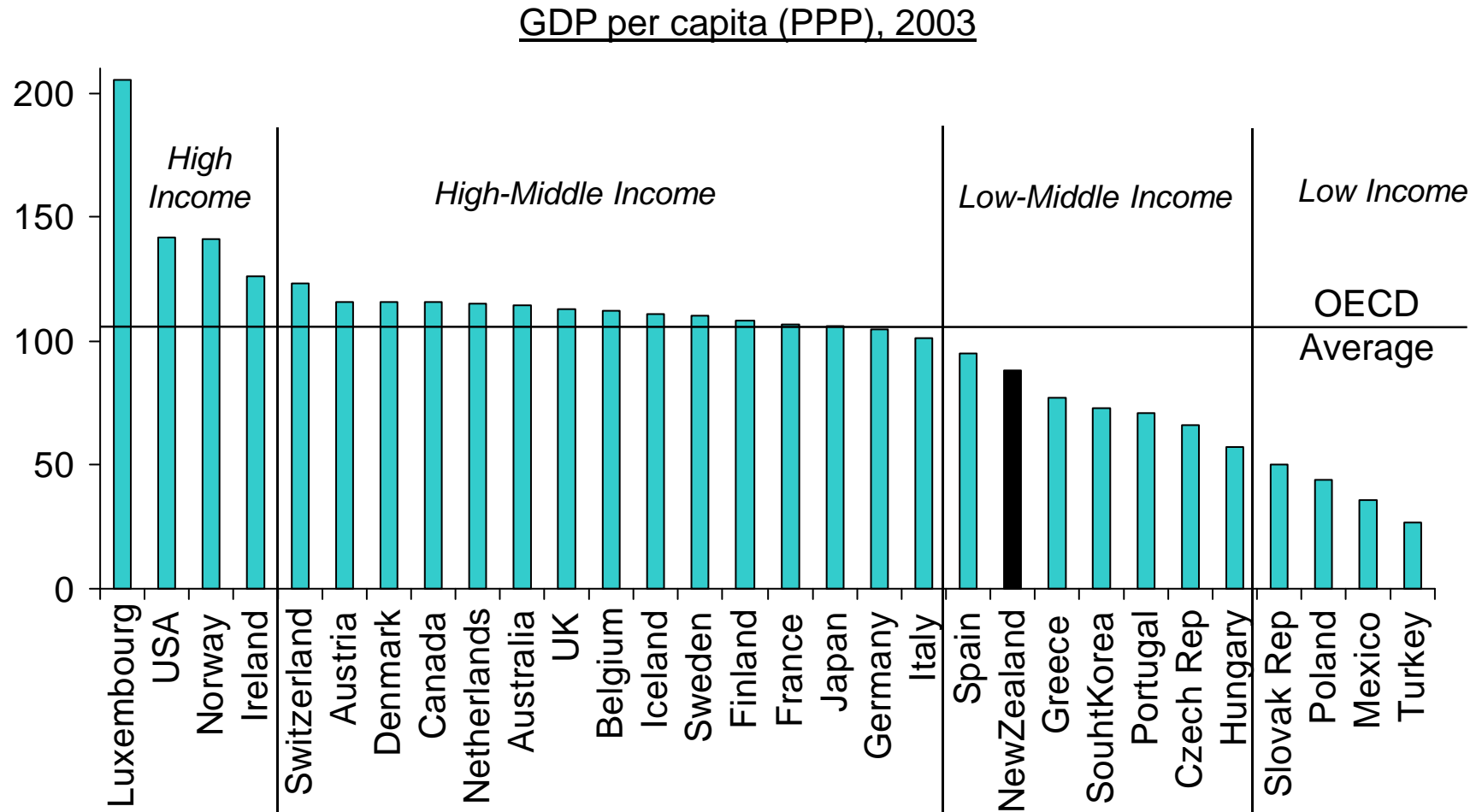
1. New Zealand's economic performance over the past 15 years
2. What this suggests for New Zealand's economic performance over the next 15 years
3. The importance of raising household savings
4. KiwiSaver Plus

NEW ZEALAND'S PROLONGED RELATIVE INCOME DECLINE WAS HALTED DURING THE 1990s



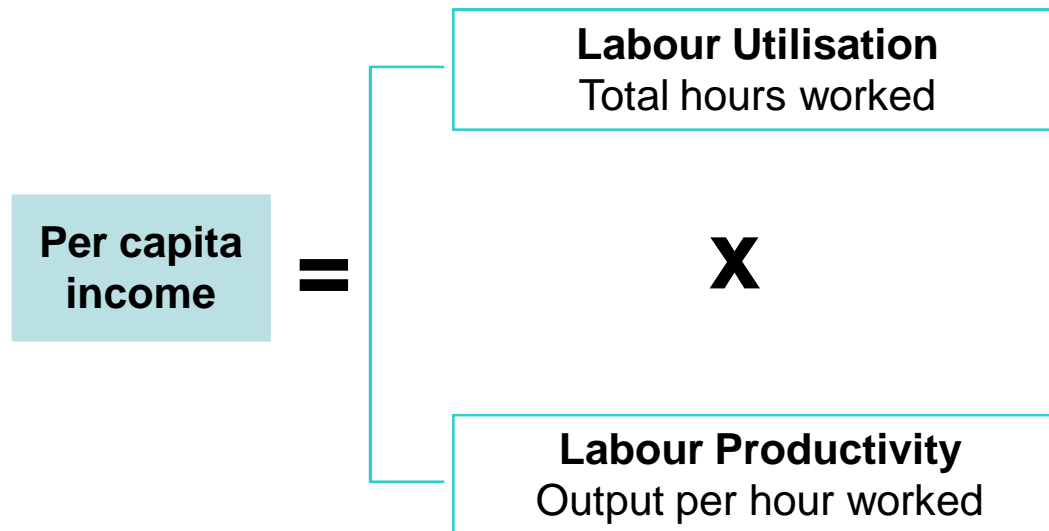
Source: OECD.

A LARGE INCOME GAP REMAINS BETWEEN NEW ZEALAND AND MOST OTHER OECD COUNTRIES

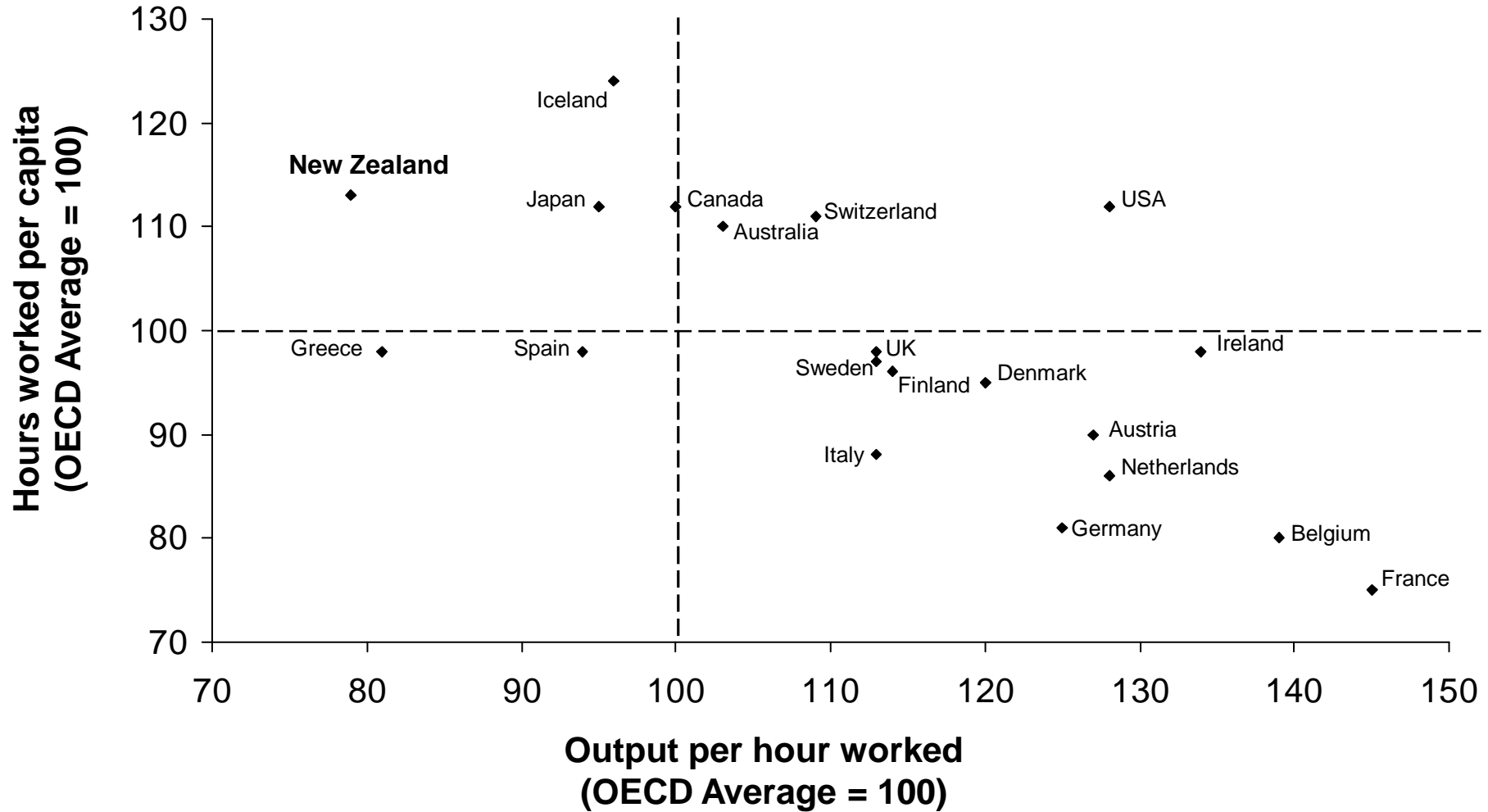


Source: OECD.

TO EXPLAIN THIS, AND TO UNDERSTAND NEW ZEALAND'S PROSPECTS FOR THE NEXT 15 YEARS, WE NEED TO LOOK AT THE ELEMENTS OF PER CAPITA INCOME

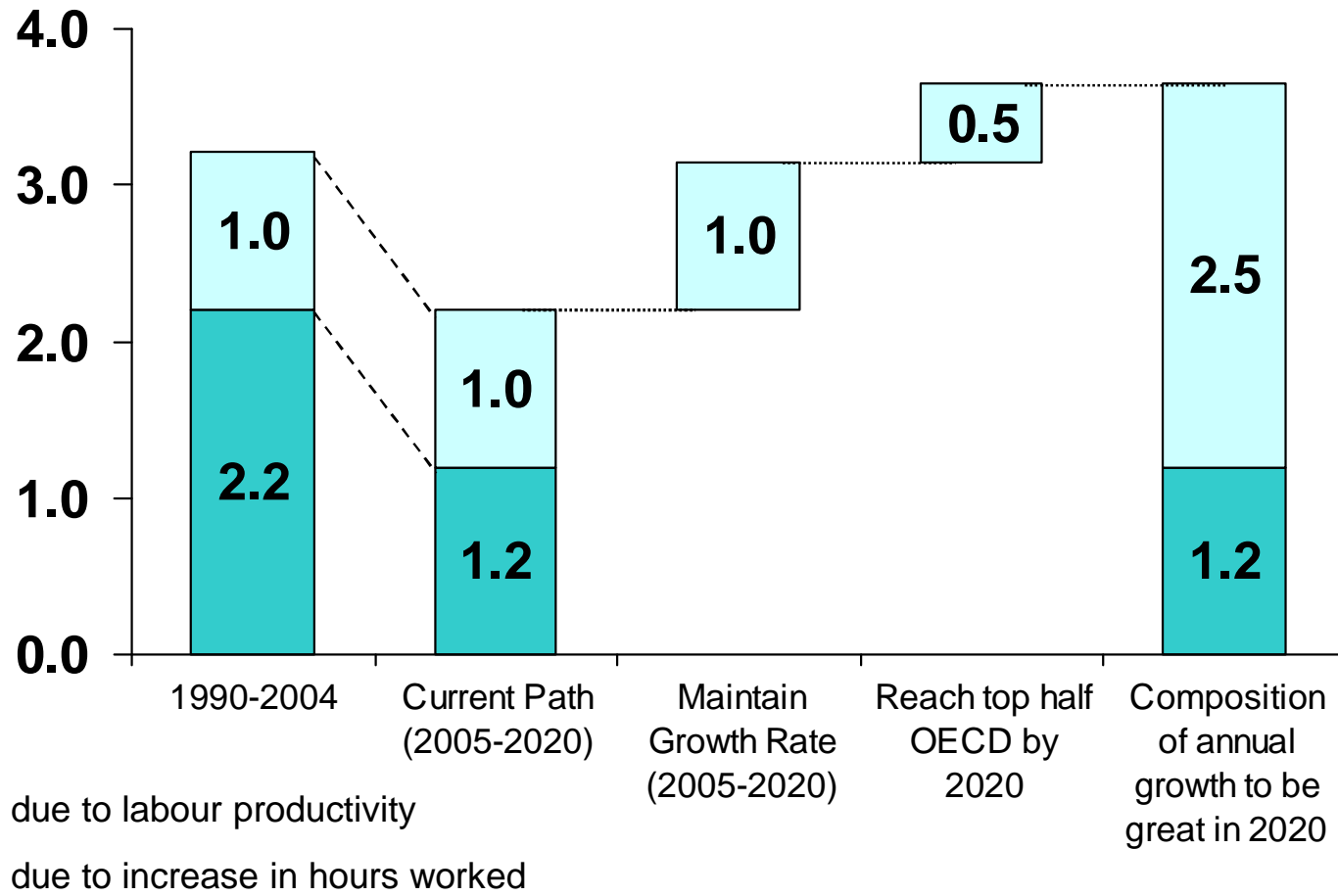


NEW ZEALANDERS ARE HARD WORKING BUT ARE NOT AS PRODUCTIVE AS WORKERS IN OTHER COUNTRIES



Source: Groningen Growth and Development Centre and the Conference Board, Total Economy Database, August 2005. 6

HIGHER LABOUR PRODUCTIVITY IS NEEDED TO MAINTAIN GOOD CURRENT GROWTH RATES, AND THEN TO MOVE TO GREAT



Note: Assumes all OECD countries continue to grow at OECD average per capita rate (1990-2004). Also assumes Medium Labour Force scenario.

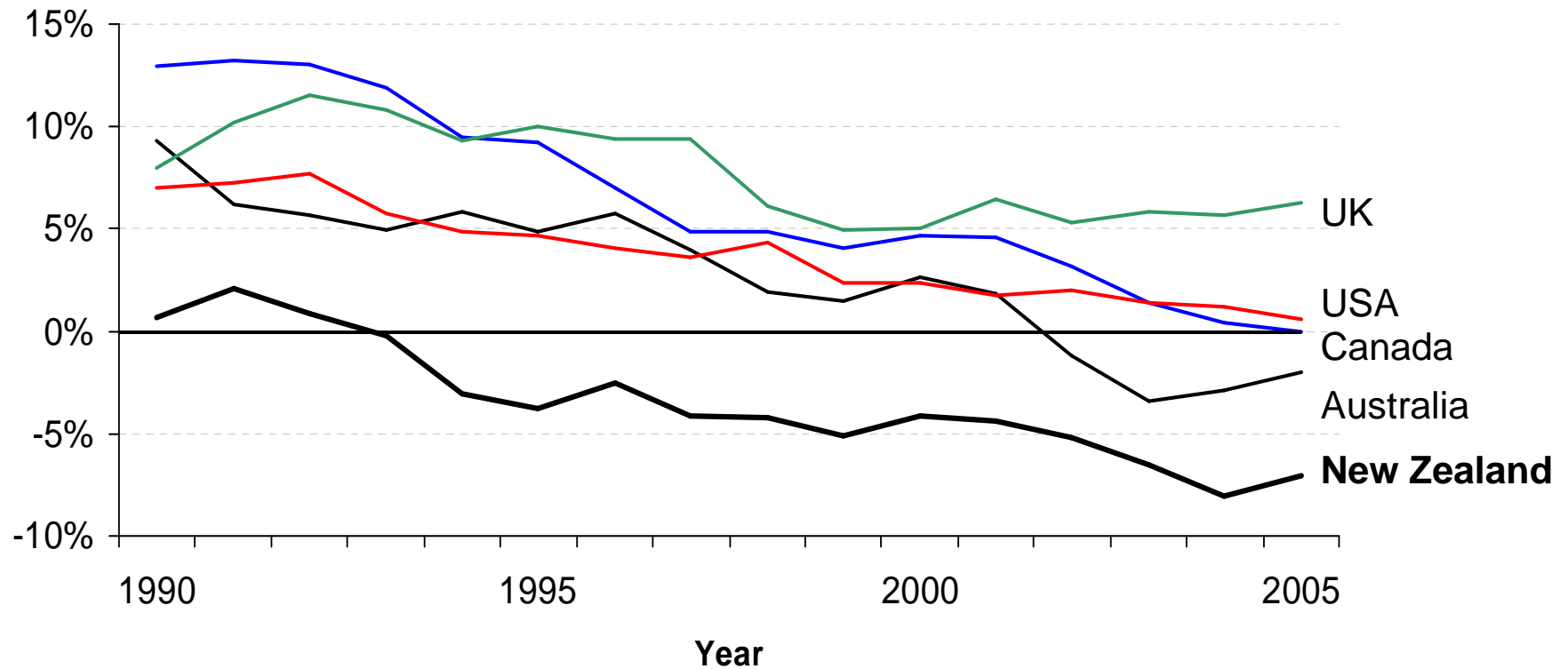
Source: The New Zealand Institute calculations.

PRIORITIES FOR ACTION TO RAISE PRODUCTIVITY

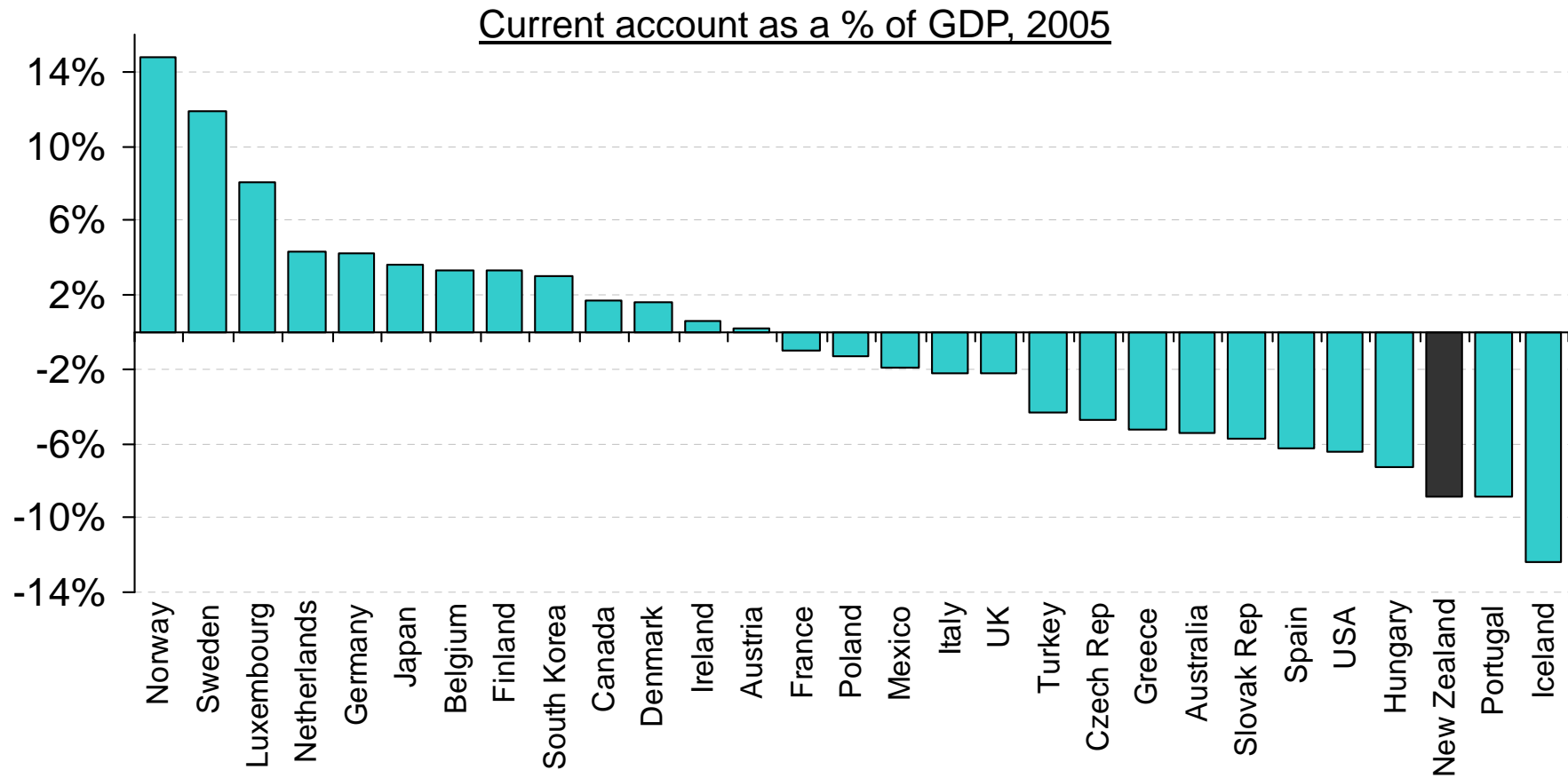
- The challenge is to raise labour productivity growth in a substantial and sustained way
- New Zealand already has, for the most part, many of the policies and institutions that are conducive to strong productivity growth
- Going forward, raising productivity growth is also about focusing on some structural constraints on the New Zealand economy
- One of the key issues in this regard is increasing savings and investment in the productive economy

NEW ZEALAND HAS HAD LOW AND DECLINING HOUSEHOLD SAVINGS OVER THE PAST DECADE

Household Savings as a % of Disposable Income

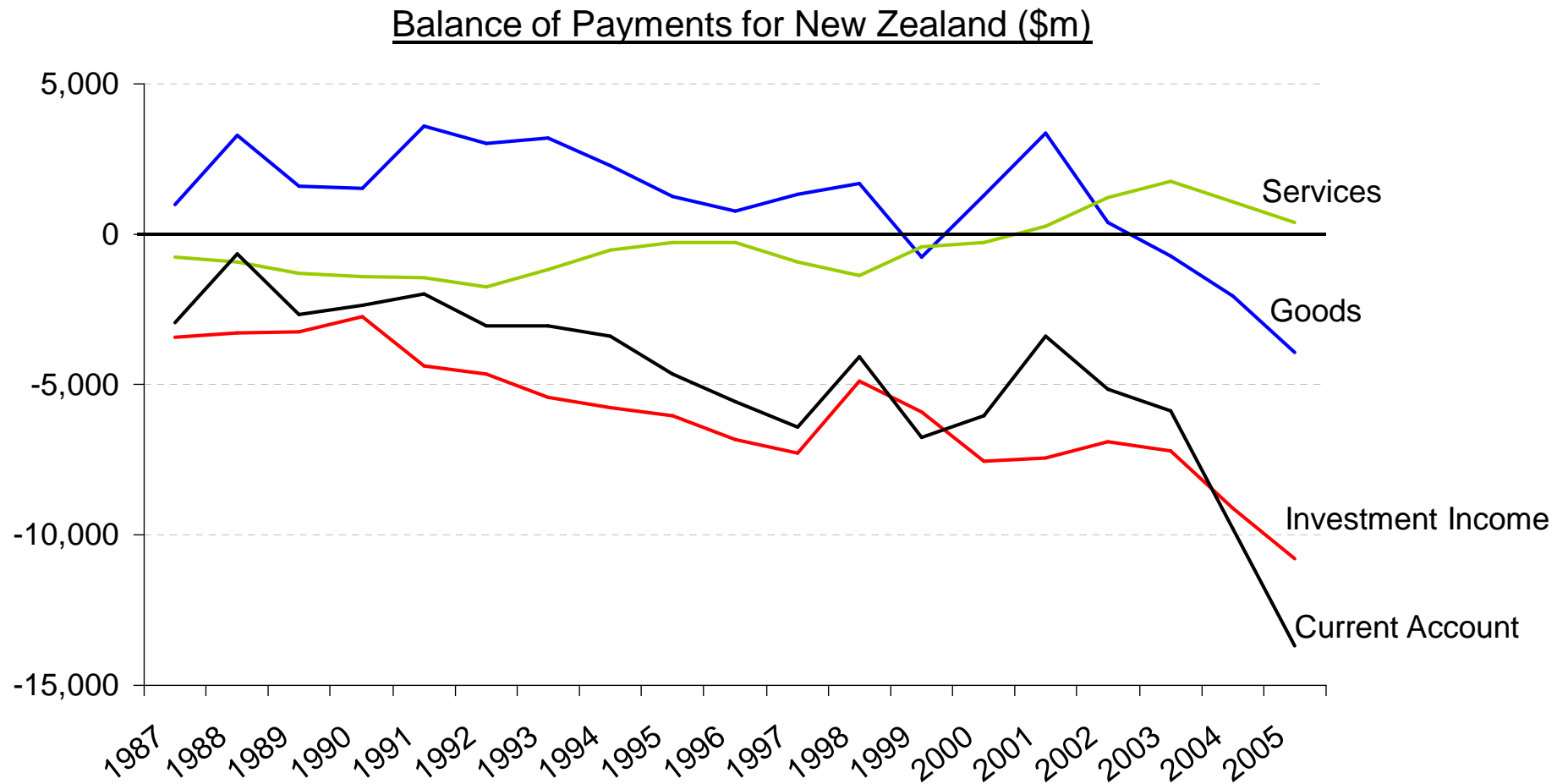


BECAUSE OF LOW DOMESTIC SAVINGS, NEW ZEALAND IS HEAVILY RELIANT ON FOREIGN CAPITAL



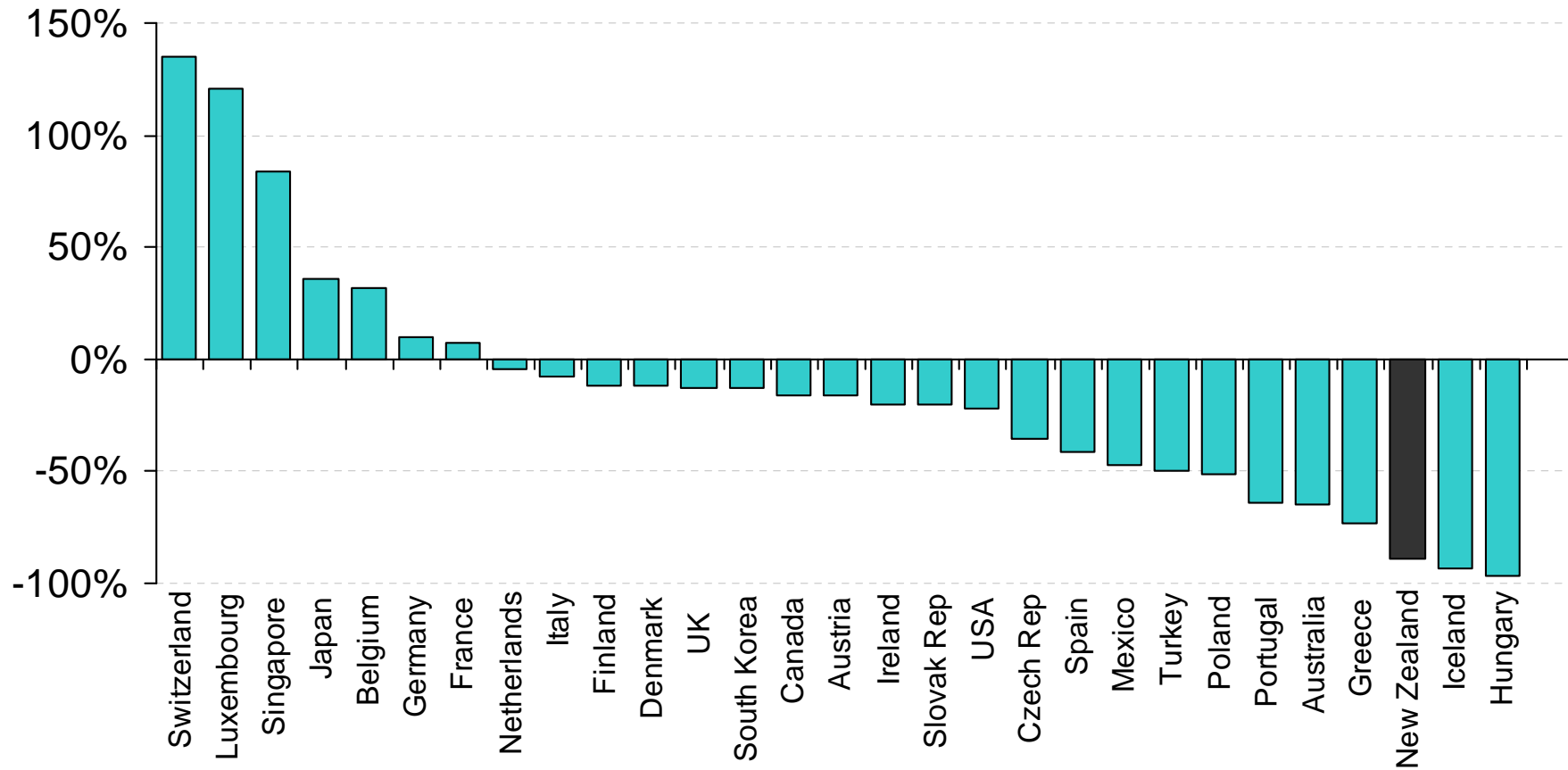
Source: OECD; Statistics New Zealand.

THE LARGE CURRENT ACCOUNT DEFICIT IS DRIVEN BY THE INVESTMENT INCOME DEFICIT



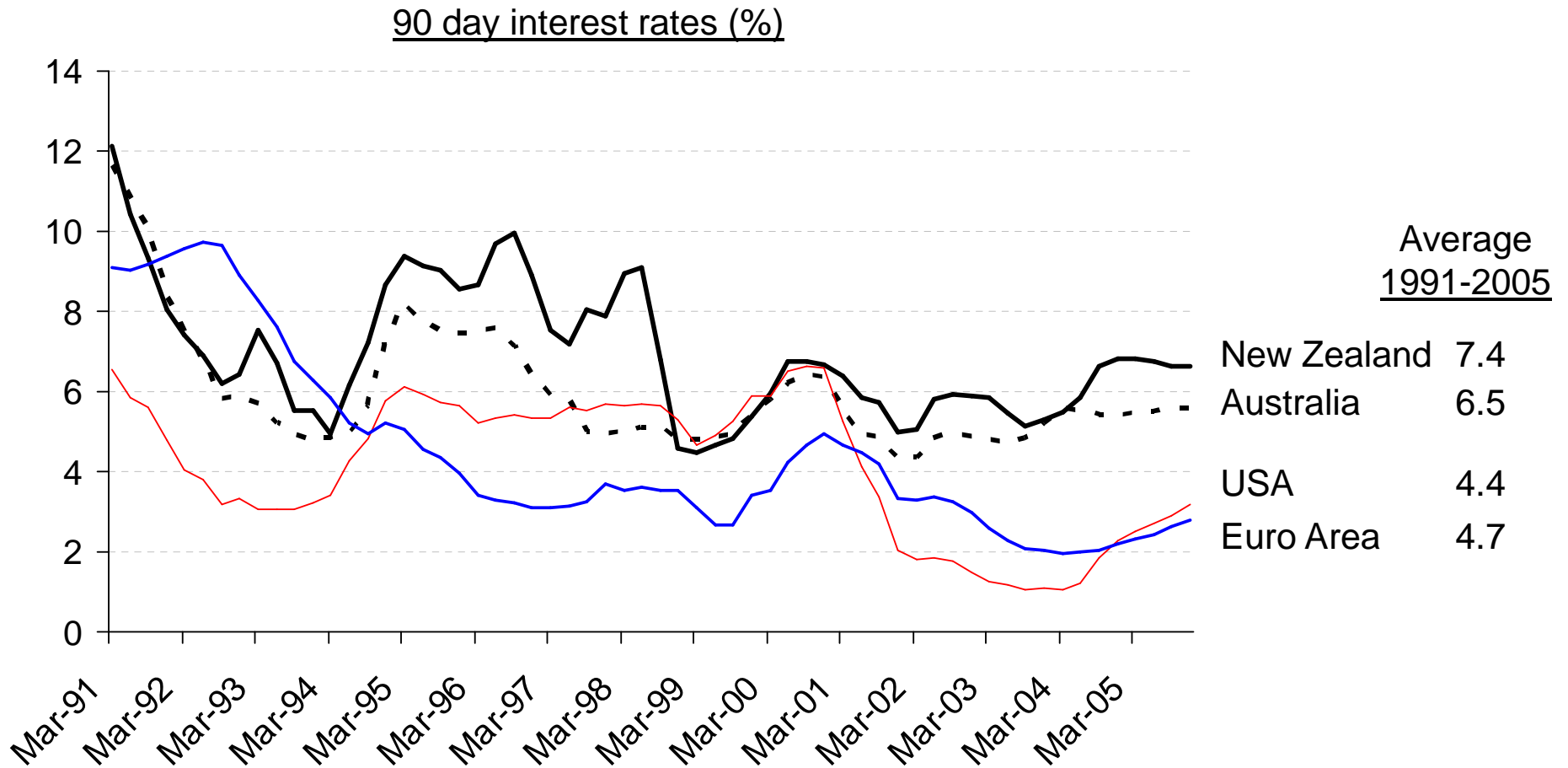
LARGE, PERSISTENT DEFICITS HAVE LED TO NZ HAVING AMONG THE HIGHEST LEVELS OF EXTERNAL LIABILITIES IN THE OECD

Net external liabilities as a % of GDP, 2004



Source: IMF; Statistics New Zealand.

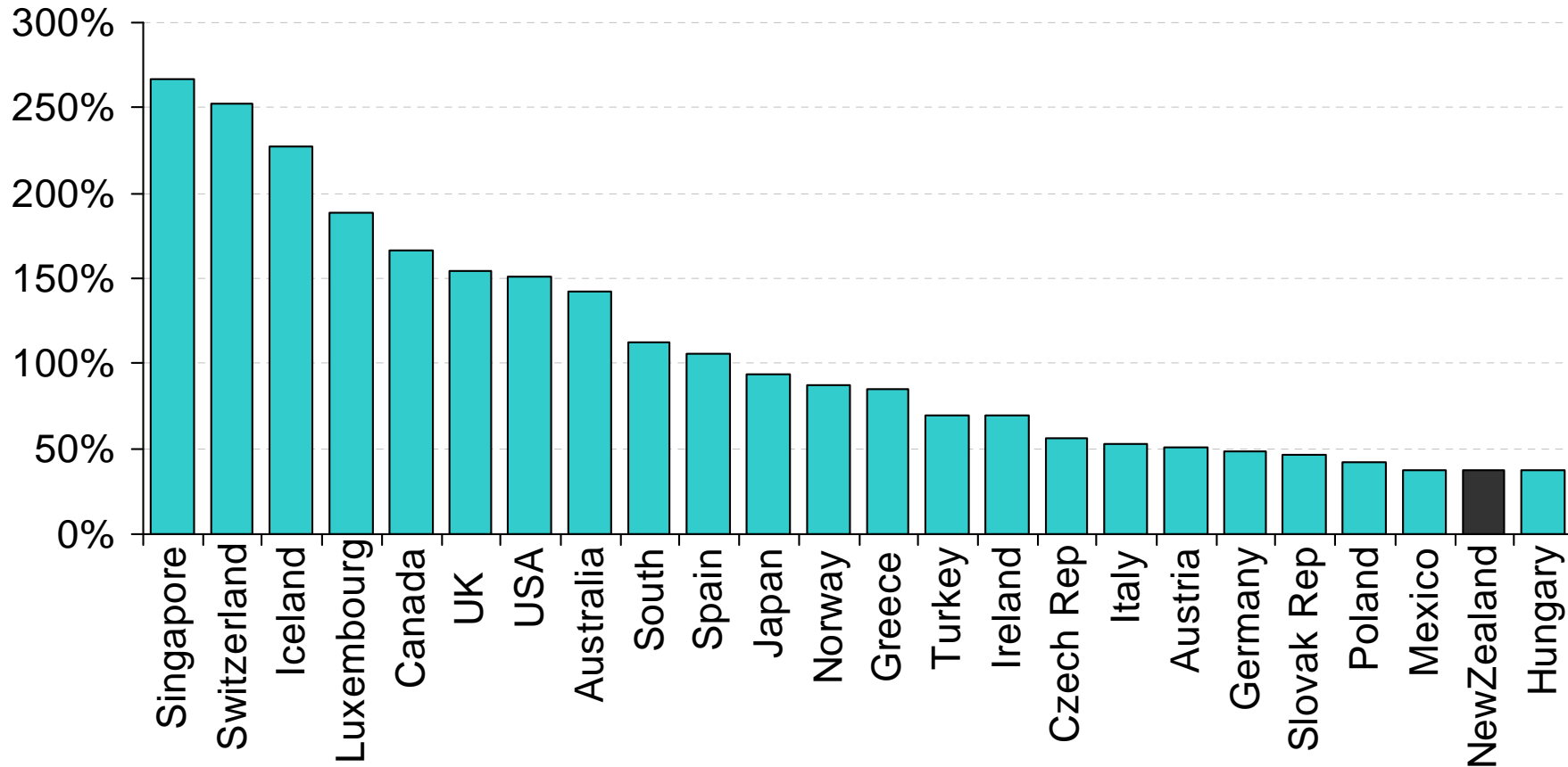
THIS EXTERNAL LIABILITY POSITION MEANS THAT NEW ZEALAND INTEREST RATES ARE RELATIVELY HIGH



Source: Reserve Bank of New Zealand.

THE ABSENCE OF A POOL OF DOMESTIC CAPITAL IN NZ HAS CONSTRAINED THE DEVELOPMENT OF NZ'S CAPITAL MARKETS

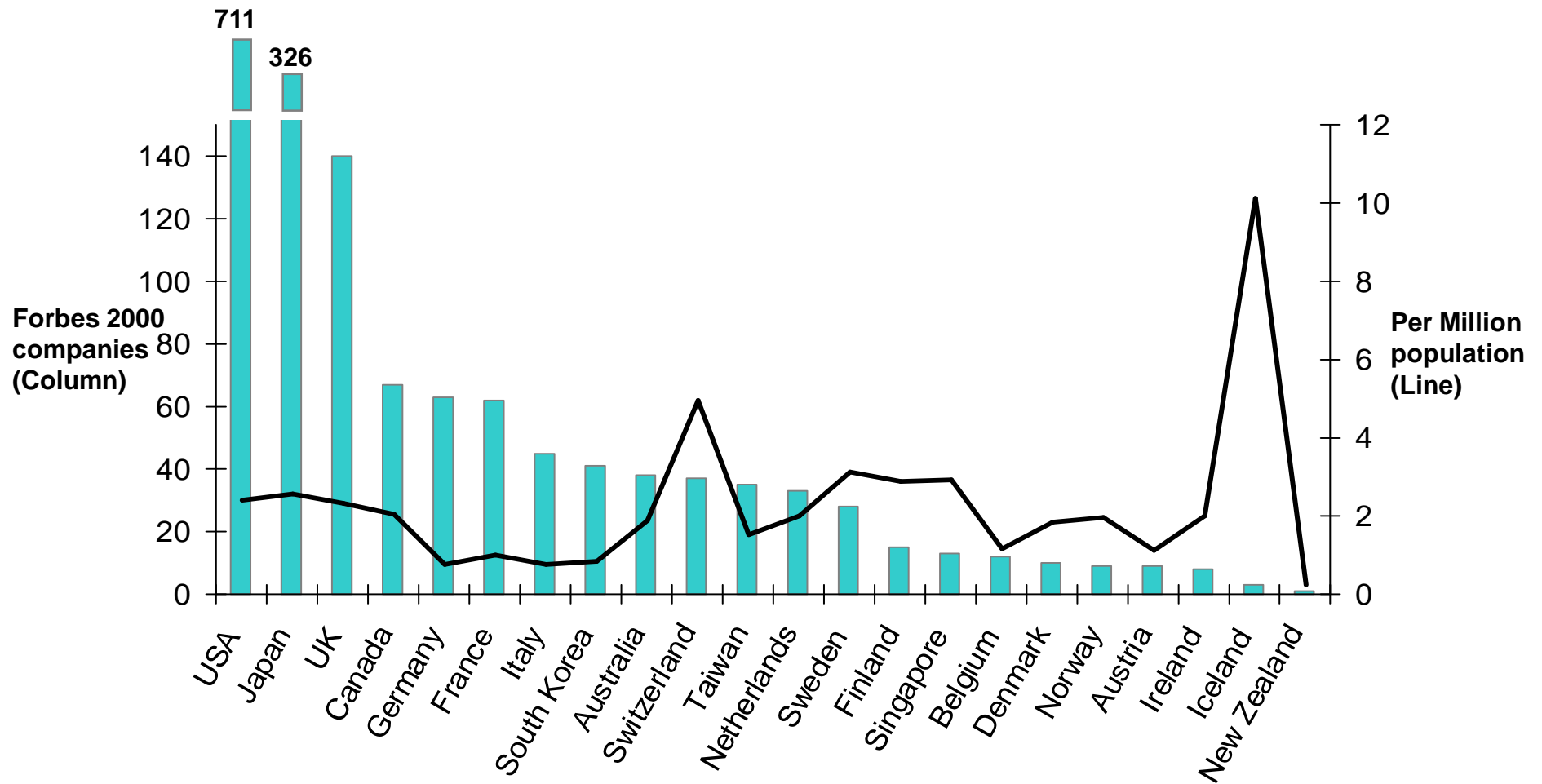
Market capitalisation of national exchange as a % of GDP, 2006



Note: In instances where countries have access to regional or major nearby exchanges only the national exchange was considered. In instances of multiple national exchanges only major, distinct exchanges were included. In all cases we have made conservative assumptions that likely understate market value, particularly for European countries.

Source: IMF; Deutsche Bank; relevant national exchange for Iceland, Canada, Slovak Rep, and Czech Rep.

NEW ZEALAND HAS NOT GROWN LARGE COMPANIES IN THE WAY THAT OTHER COUNTRIES HAVE

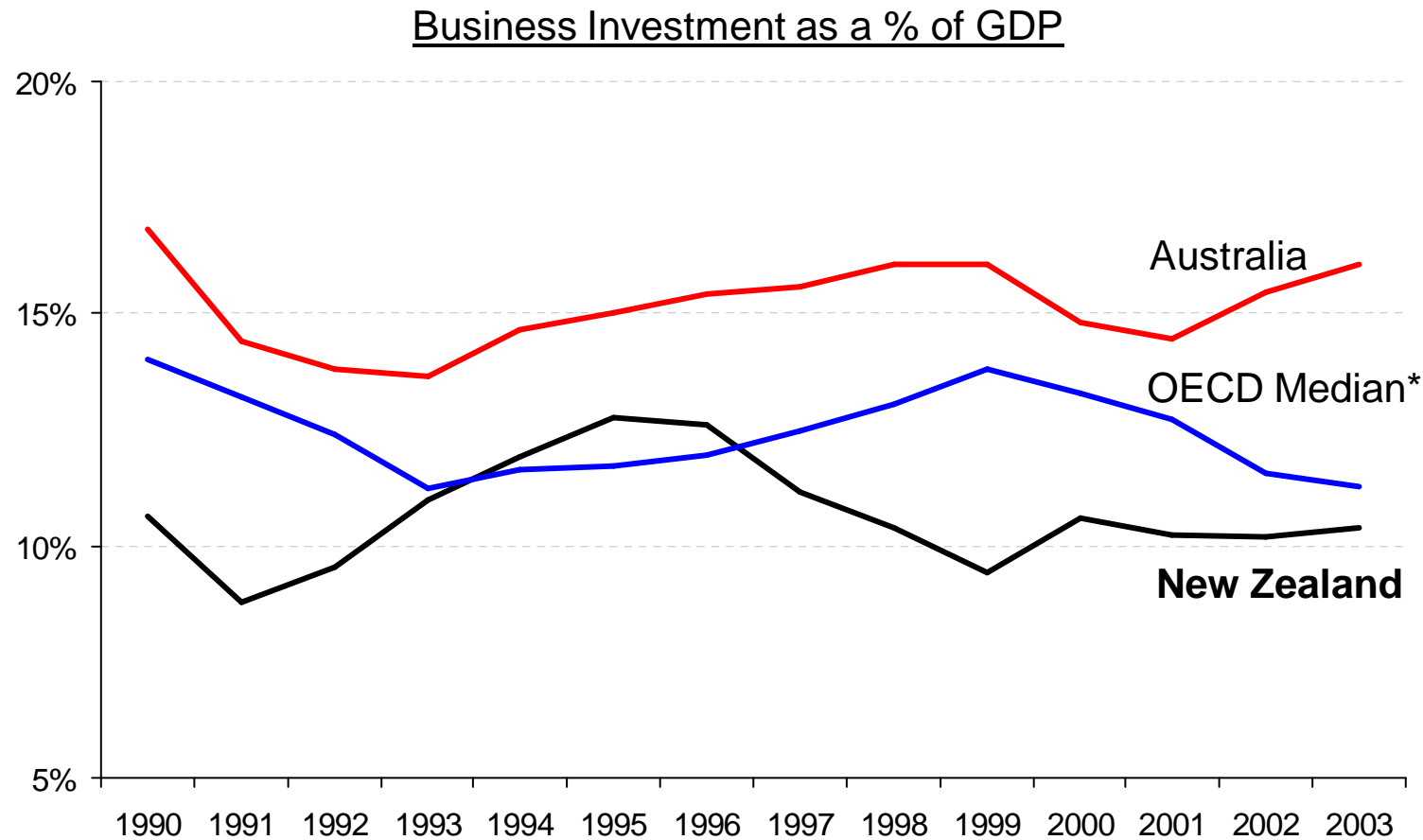


Sources: Forbes Magazine.

MANY OF NEW ZEALAND'S LARGE COMPANIES ARE NO LONGER LARGE NEW ZEALAND COMPANIES

April 7, 2006	December 31, 2001	December 31, 1996
Total of Top 10: 36b, 23% of GDP	Total of Top 10: 26b, 23% of GDP	Total of Top 10: 36b, 36% of GDP
* Telecom: \$11.45 billion.	* Telecom: \$9.3 billion.	* Telecom: \$13.64 billion.
* Contact Energy: \$4.67 billion, majority owned by Origin, could soon be delisted.	* Carter Holt Harvey: \$2.96 billion, delisted.	* Carter Holt Harvey: \$5.5 billion, delisted.
* Fletcher Building: \$4.40 billion.	* Contact Energy: \$2.30 billion, now majority owned by Origin, could soon be delisted.	* Brierley Investments: \$3.9 billion, now primarily Singapore-based UK hotel owner.
* Vector: \$2.75 billion.	* Lion Nathan: \$2.20 billion, Japanese-owned, now listed in Australia.	* Fletcher Challenge Paper: \$2.15 billion, now owned by Norske Skog.
* Sky TV: \$2.54 billion.	* The Warehouse: \$2.01 billion.	* Fletcher Challenge Forestry: \$1.9 billion, now stripped of trees, trades as Tenon.
* Auckland International Airport: \$2.48 billion.	* Fisher & Paykel Healthcare: \$1.75 billion.	* Lion Nathan: \$1.86 billion, now Japanese owned and Australian listed.
* Sky City: \$2.28 billion.	* Independent Newspapers: \$1.54 billion, wholly owned by Fairfax.	* Fletcher Challenge Building: \$1.61 billion.
* Fisher & Paykel Healthcare: \$2.08 billion.	* Sky Network TV: \$1.54 billion, majority owned by News Corp.	* Fletcher Challenge Energy: \$1.52 billion, now owned by Anglo Dutch Shell.
* The Warehouse: \$1.35 billion.	* Auckland International Airport: \$1.52 billion.	* Wilson & Horton: \$1.13 billion, now owned by Australia's APN.
* Fisher & Paykel Appliances: \$1.16 billion.	* Sky City: \$1.29 billion.	* Air New Zealand: \$1.06 billion, bailed out by the taxpayer but still listed.

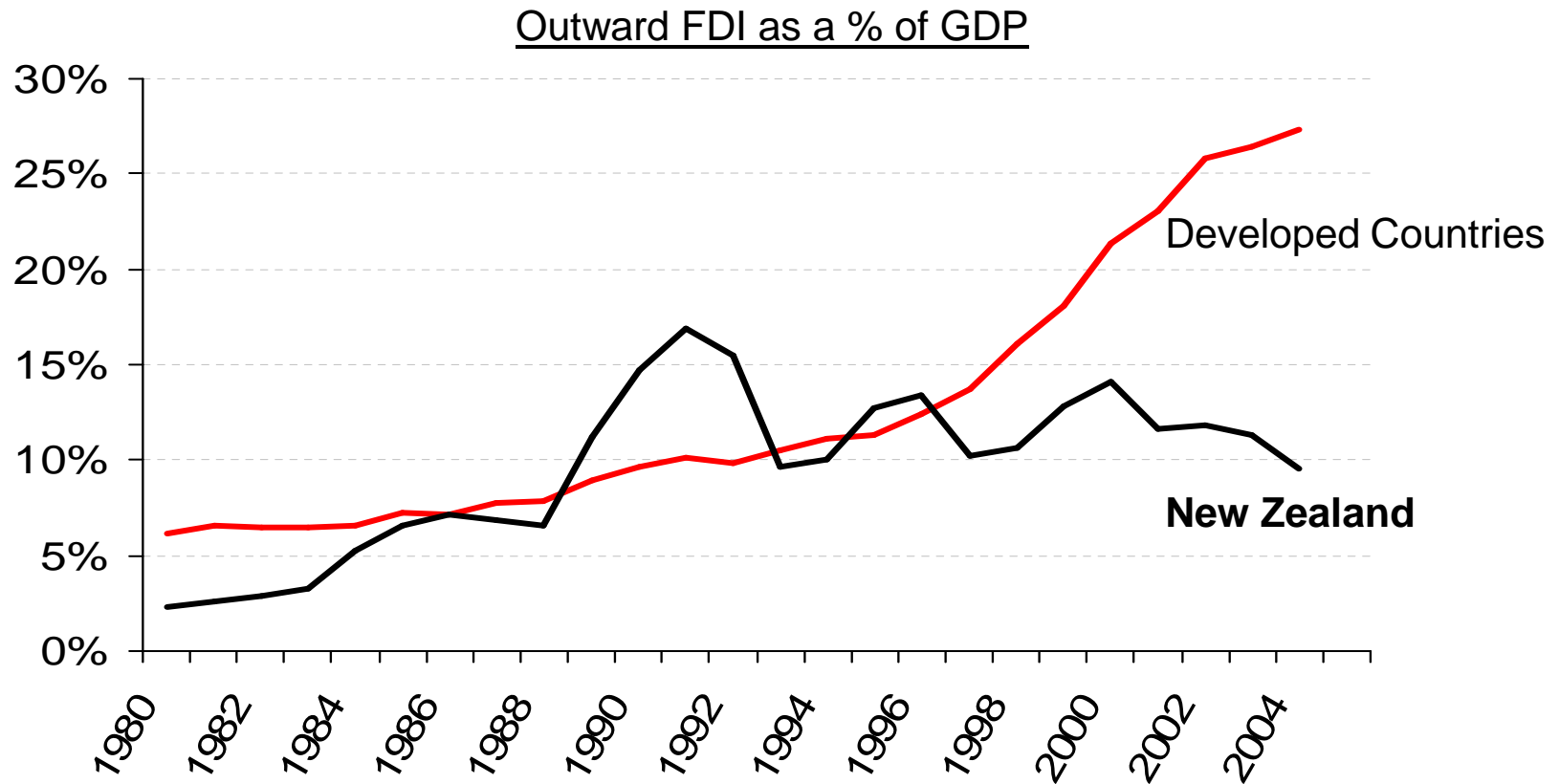
NEW ZEALAND'S BUSINESS INVESTMENT HAS CONSISTENTLY BEEN BELOW THE OECD MEDIAN



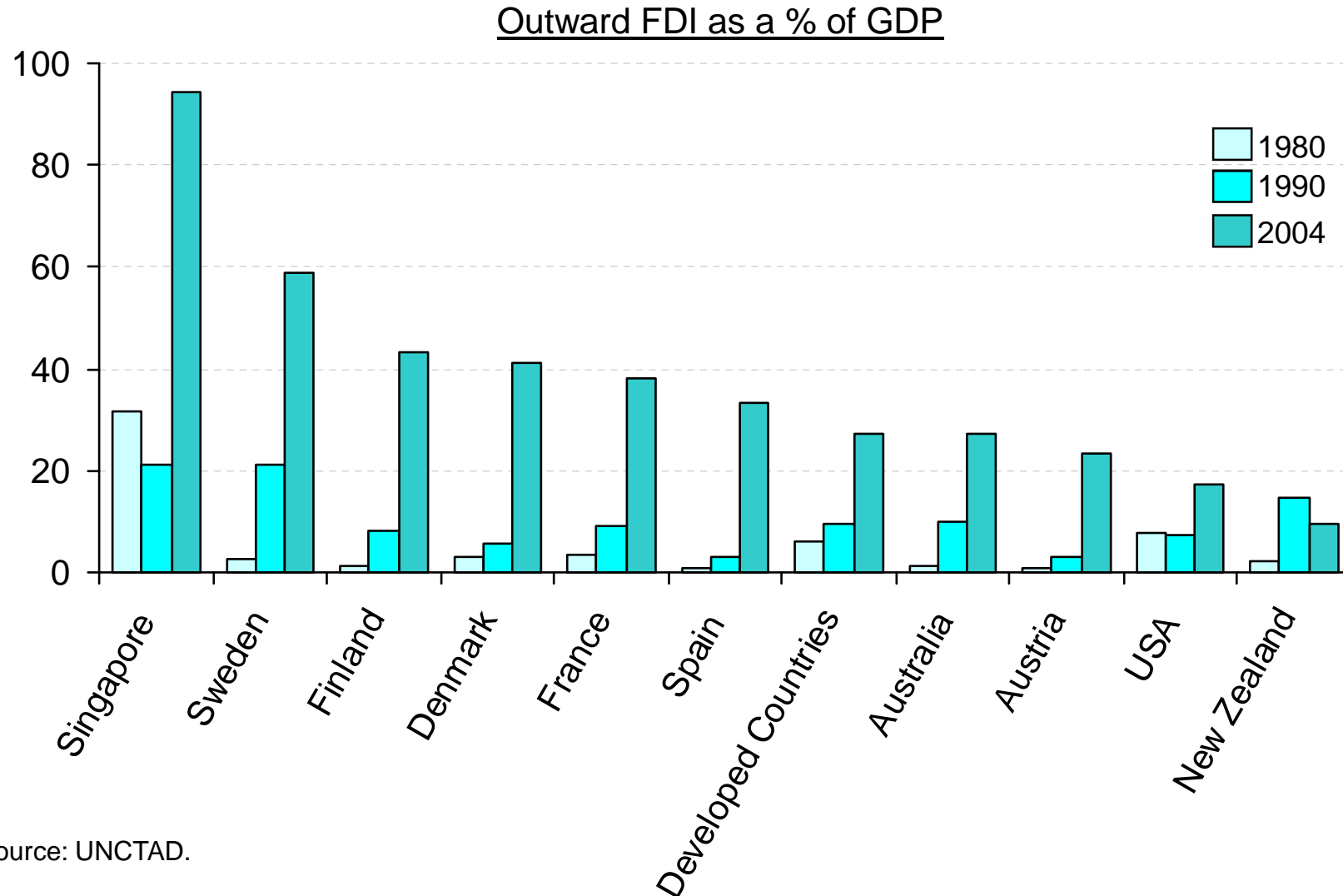
Source: OECD.

*Czech Rep, Luxembourg, Poland, Hungary, Portugal, Slovak Rep, and Turkey not included.

NEW ZEALAND'S OUTWARD FDI REDUCED THROUGH THE 1990s, PARTICULARLY RELATIVE TO OTHER DEVELOPED COUNTRIES



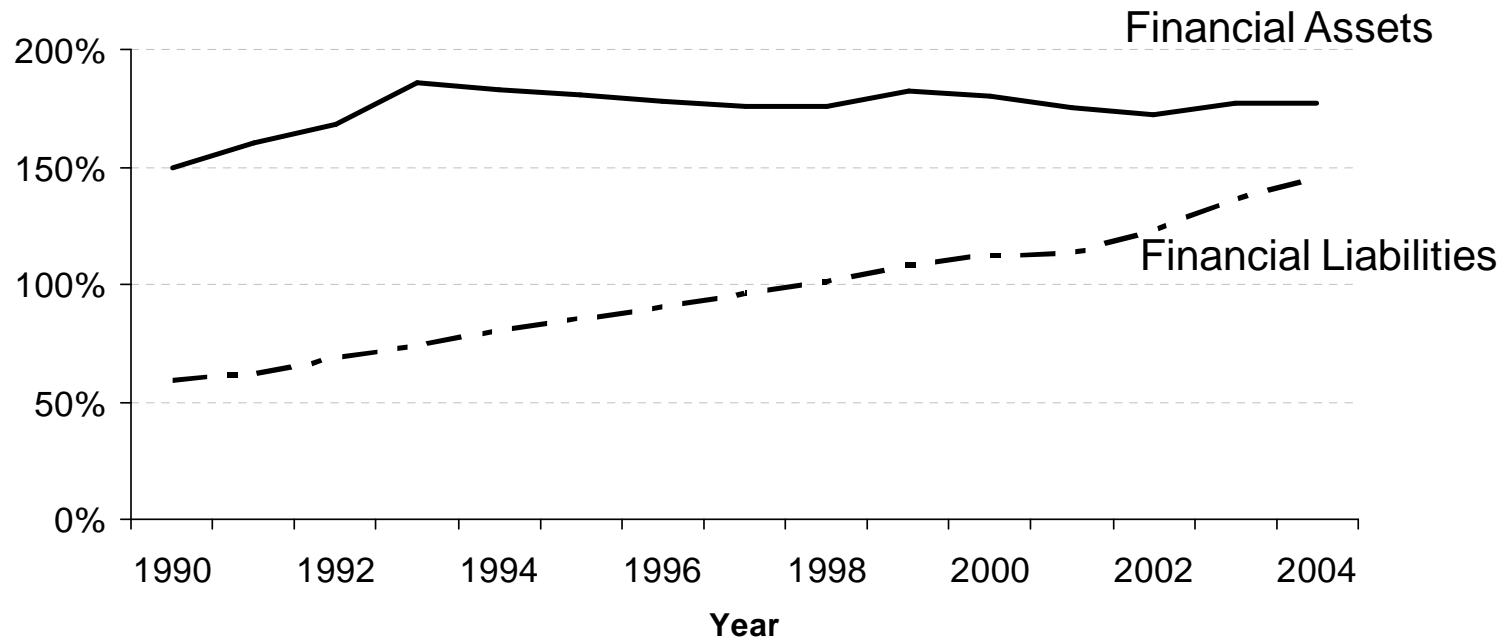
NEW ZEALAND IS DISTINCTIVE IN HAVING A LOW AND REDUCING OUTWARD FDI STOCK



Source: UNCTAD.

HOUSEHOLD FINANCIAL ASSETS CONSTANT, HOUSEHOLD DEBT INCREASING RAPIDLY

Household Financial Assets and Liabilities as a % of Disposable Income



CREATING AN OWNERSHIP SOCIETY IN NEW ZEALAND

- Asset ownership provides people with a stake in New Zealand's economic success
 - Because of this, widespread asset ownership changes public attitudes towards business and economic success
- This has been an important benefit from the compulsory savings scheme in Australia
 - The Australian Treasury estimate that increases in the value of housing contributed \$4000 to the average person's balance sheet in 2005 while shares in superannuation and other funds contributed \$23,000
 - The financial position of the average Australian is linked closely to the performance of Australian companies
- This is not the case in New Zealand
 - Only around 20% of New Zealand households, mainly those on higher incomes, own financial assets

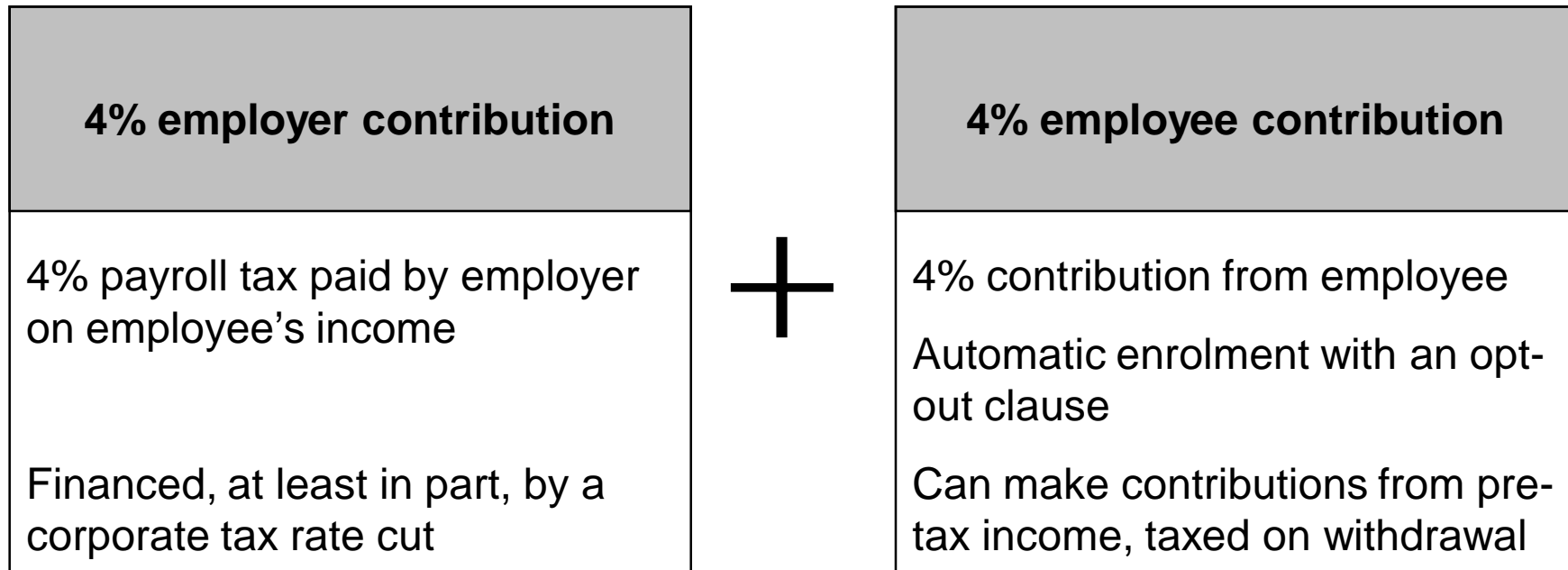
IMPLICATIONS FOR POLICY ACTION

- These national-level economic and social issues generate a compelling need to focus on increasing savings in New Zealand
- Policies that increase the level and broaden the distribution of household savings are important for two types of reasons
- First, increased savings will address some significant macroeconomic risks and costs, around the current account deficit and the hollowing out of New Zealand's capital markets
- Second, increased levels of saving is an important part of strengthening the New Zealand economy, and New Zealand society, to better position New Zealand to prosper into the future
 - This is a vitally important part of an economic growth agenda for New Zealand

EVALUATION OF KIWISAVER

- KiwiSaver is a welcome step in the right direction, but it is unlikely to be have a material effect on household savings
- The commentary accompanying the Bill states that 25% of the population to be participating by 2014
 - 25% participation x 4% contribution = 1% of wage income
- I suspect that participation rates may be lower because of the absence of financial incentives, even with the automatic enrolment
- The increase in savings due to KiwiSaver will not make much of an impact on the current account deficit, the capital markets, or on creating an ownership society
- So although KiwiSaver is a good start, the priority now must be to establish a more ambitious version of the KiwiSaver scheme

PROPOSED KIWISAVER PLUS SCHEME



SUMMARY

- New Zealand's economic performance has been substantially better over the past 15 years, but a substantial challenge lies ahead
- This will require deliberate, aggressive, and sustained action from both government and business
- We need to start taking some risks
- Increasing household savings significantly is a vitally important part of the economic transformation agenda