Productivity in New Zealand: Some thoughts for the 2025 Taskforce

Arthur Grimes*
Motu Economic and Public Policy Research

September 2009

*Views expressed are exploratory, designed to stimulate debate on productivity issues; and are solely those of the author.
Topics

• Resources
• The process of productive investment
• Constraints on productive investment
• Opportunities for productive investment
• Regional insights
Resources

• A country’s resources include:
  – Climate; given by nature
  – Location; can effectively be modified a little (infrastructure)
  – Land; given by nature, but can be transformed
  – Minerals; utilisation is open to some choice
  – People; quality can be modified, but takes time
  – Ideas/knowledge; can be generated, modified, imported
  – Financial wealth; historically generated, allocation is important

• A country’s living standards depends on its:
  – Stocks of resources; some areas will always be relatively poor
    • Comparative advantage does not imply equalisation of living standards
  – Utilisation of resources; living standards can be modified
Process of Productive Investment
Firms invest when they spot profitable opportunities

Winnowing process - via markets & constraints

Constraints

Successful investments
Productive process: Implications

1. A focus solely on constraints or on productive opportunities misses the bigger picture.

2. Removing constraints does little if productive opportunities are lacking.
Constraints: Planning & Delays

• With **uncertainty**, time is of the essence
  – Restrictions that delay decisions hurt investment
    • Infrastructure development is delayed or prevented
    • Productive investment opportunities are missed
    • Main problem with RMA (rather than Act itself)

• **Trade-offs are required for competing land uses**
  – But not made with explicit reference to costs & benefits
    • E.g. mineral exploration
    • Urban zoning decisions
Constraints: Human Capital

• Long, low tail exists for human capital
  – Poor quality of parts of the workforce
  – Social problems require addressing
  – Requires fiscal resources & policy attention
    • Otherwise the problem gets even worse

• Management & board capability in NZ variable
  – Possibly an historical legacy (sheltered economy)
Constraints: Taxes

• Taxes, subsidies & regulatory constraints are capitalised into immobile factor prices
  – Tax-favoured sectors will have artificially high prices
    • E.g. agricultural land prior to 1984
    • E.g. housing land today priced too high
    • Draws resources away from other (productive) investments

• Otherwise, tax not our largest productive impediment
  – Moderate, stable tax rates
  – Broadly sensible tax structure (except property)
  – Neither a major competitive disadvantage or advantage
Constraints: Infrastructure

• **Connectivity** vital for productive investment success
  – Access to markets & inputs: domestic & foreign
    • Physical
    • Labour – efficient passenger transport
  – Access to ideas: domestic & foreign

• **Connectivity is a network issue**
  – Cannot be addressed just by ranking projects by B:C’s
    • E.g. Auckland – Hamilton road link
    • Location of ports, roads & rail are inter-connected issues
    • Use of broadband relative to other forms of connectivity

→ Centrality of planning land use & infrastructure jointly
Constraints: Policy Time Horizon

Costs and Benefits (2 projects: 1 & 2)
Same cost ($100); different benefit horizons

$100  $80  $60  $40  $20  $0

0  4  8  12  16  20  24  28  32  36  40  44  48

Year

cost

Ben1  Ben2

cost

Ben1  Ben2
Constraints: Prefer project 1
Project 2 doesn’t even meet costs
with 10% real discount rate
Productive Investment Opportunities
Why invest in NZ rather than somewhere else?

- World class universities? X
- World class research institutes? X
- Market scale? X
- Close to other markets X
- Entrepot / trade hub? X
- Deep capital markets? X
- Easy to exploit minerals? X
- Really cheap labour? X
Productive Investment Opportunities
Why invest in Tasmania rather than somewhere else?

- World class universities? X
- World class research institutes? X
- Market scale? X
- Close to other markets X
- Entrepot / trade hub? X
- Deep capital markets? X
- Easy to exploit minerals? X
- Really cheap labour? X
Constraints vs productive opportunities

• Domestically determined constraints are not NZ’s major productivity problem
  – Though of course they should be addressed
  – Adopt pro-production (not pro-consumption) policy approach

• A lack of productive opportunities is the key problem

• Policies designed to make NZ catch up to ‘Australia’ need to be able to be applied to TAS so it can catch up

• What could they be?
Possible underpinnings for productive investment

• Raw materials (oil /other minerals)
  – A gamble but okay if financed privately
  – Can’t count on it

• Science-based utilisation of human capital & natural advantages (eg agricultural base)

• Who will do this (& stay in NZ)?
  – Private sector firms need talent to develop ideas
    • Implies strong science-base in universities & research institutes
  – And need scale to stay in NZ
    • Difficult to address; possible with strong domestic research base?