
The Parliament of the Commonwealth of Australia

Report of the 2007 New Zealand Parliamentary Committee Exchange

15—19 July 2007

House of Representatives
Standing Committee on Economics, Finance and Public Administration

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Chair's foreword

Australia and New Zealand share a close and longstanding relationship. The countries, being geographically near, have diverse ties, ranging from defence and trade to sporting and cultural links. Trade between the two countries has exponentially expanded under the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) since it came into effect in 1983. New Zealand is Australia's sixth most prominent trading partner while Australia is New Zealand's largest trading partner.

The similarities of the countries provide a platform to discuss many issues common to both; while their unique features allow the sharing of new ideas. The Australian and New Zealand parliaments tap into this co-operative spirit through an annual trans-Tasman parliamentary committee exchange program.

The House of Representatives Standing Committee on Economics, Finance and Public Administration visited New Zealand between 15-19 July 2007 as part of the program. The visit program, which was organised and hosted by the New Zealand parliament, was thorough and rewarding.

The committee endeavoured to build upon the robust relationships already forged between the two parliaments and to discuss a variety of economic and policy issues with government and non-government organisations. These objectives were fulfilled.

The committee held formal meetings with the Speaker of the New Zealand parliament, the Hon Margaret Wilson MP, the Deputy Leader of the Opposition and Spokesperson on Finance, the Hon Bill English MP, the Opposition Spokesperson on Housing, Mr Phil Heatley MP, and members of both the Finance and Expenditure Committee and the Commerce Committee. The delegation also met with other New Zealand parliamentarians during the visit, including the Minister for Finance, Dr the Hon Michael Cullen MP, the Minister for Commerce, the Hon Lianne Dalziel MP, the Minister for Revenue, the Hon Peter Dunne MP, and the Leader of the Green Party, Ms Jeanette Fitzsimons MP.

Both the New Zealand and the Australian parliamentary committee systems have a role in scrutinising the conduct of monetary policy by their respective central banks. Meetings with the Reserve Bank of New Zealand provided the committee with an overview of the Bank's current monetary policy mechanisms and of the parliamentary scrutiny the Bank is subject to.

From a banking and financial sector perspective the delegation also met with officials from the New Zealand Stock Exchange and from Kiwi Bank, the New Zealand Post Group's subsidiary banking entity. Independent meetings were also held with market economists who gave their views on the New Zealand economy and its economic relationship with Australia.

The delegation contributed to discussions on topics which were the subject of House Economics Committee inquiries in the 41st parliament.

The committee discussed the New Zealand retirement savings system with representatives from the New Zealand Treasury, the Department of Inland Revenue, the Ministry of Economic Development and the Ministry of Social Development. Much of this meeting focused on the KiwiSaver national savings scheme which was introduced on 1 July 2007, only weeks prior to the delegation visit. This issue related to recommendations made by the committee in its 2006 report on *Improving the superannuation savings of people under 40*.

The New Zealand Government's industry policy, in particular its manufacturing strategy, was discussed with officials from the Ministry of Economic Development and New Zealand Trade and Enterprise. These discussions were relevant to both the committee's inquiry into Australia's services industry – the report *Servicing our future* had been tabled in June 2007 – and the inquiry into the current state and future directions of Australia's manufacturing sector – the report of which, *Australian Manufacturing – today and tomorrow*, was tabled soon after the visit.

On behalf of the committee and myself I would like to thank all of the organisations, departments and individuals in New Zealand who participated in the visit meetings and activities. We were made to feel very welcome. People generously gave their time to discuss issues of economic policy relevance and we experienced many cultural aspects of New Zealand including a traditional Maori welcome at the Te Papa Tongarewa museum. The support and enthusiasm of all involved ensured the visit was productive and memorable.

The Hon Bruce Baird, MP

Chair



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Membership of the Committee

Chair The Hon Bruce Baird MP

Deputy Chair Ms Sharon Bird MP

Members Dr Craig Emerson MP
 Mr Steven Ciobo MP
 Ms Sharon Grierson MP
 Mr Michael Keenan MP
 Mr Stewart McArthur MP
 Mr Patrick Secker MP
 The Hon Alex Somlyay MP
 Mr Lindsay Tanner MP



Membership of the delegation

Leader The Hon Bruce Baird MP

Deputy Leader Ms Sharon Bird MP

Members Ms Sharon Grierson MP
 Mr Stewart McArthur MP
 Mr Patrick Secker MP

Delegation Secretary Ms Sharon Bryant



Visit objectives

The delegation's aims and objectives included:

- Renew dialogue with the New Zealand parliament - including meeting with the Speaker and attendance at question time.
- Review New Zealand's approaches to parliamentary oversight of monetary policy.
- Meet with the Reserve Bank of New Zealand and discuss current economic conditions and extent of regulatory functions.
- Meet with market economists to gain additional perspective on market conditions eg housing affordability and growth in private equity funds.
- Assess the state of and approaches taken to maximise New Zealand's manufacturing and service industry base.
- Review recent developments in relation to retirement savings – 'Kiwi Saver' which commenced on 1 July 2007 – the scheme allows eligible contributors to access their superannuation contributions before preservation age to provide for a first home deposit.
- Meet with the New Zealand parliament's Commerce Committee, and the New Zealand parliament's Finance and Expenditure Committee.



Acknowledgements

During the visit to New Zealand between 15 and 19 July 2007, the delegation was provided with excellent support and service. Ms Lynne Gallie of the New Zealand Department of Internal Affairs and Ms Kate Thornton of the Inter-Parliamentary Branch, Department of the House of Representatives organised a thorough and relevant program of meetings and ensured the delegation was kept well-informed.

The delegation also acknowledges the support provided by His Excellency Mr John Dauth LVO, Australian High Commissioner to New Zealand and his staff, in particular Mr Frank Ingruber, Deputy High Commissioner.

Prior to the Committee's visit to New Zealand the New Zealand High Commissioner to Australia, His Excellency Dr John Larkindale, briefed the delegation. The delegation was grateful for the opportunity to meet with Dr Larkindale and staff of the New Zealand embassy to discuss the delegation's planned program of meetings.

Introduction

- 1.1 The Australia-New Zealand Parliamentary Committee exchange program has been in operation since 1989. It allows the flow of ideas and information between parliamentarians across the Tasman, including on parliamentary procedure and operations of each parliament, and on matters of committee interest.
- 1.2 During the 41st parliament the work of the House of Representatives Standing Committee on Economics, Finance and Public Administration ('the committee') covered many areas of mutual interest to their counterpart committees in New Zealand. It was therefore particularly beneficial that the committee was selected for the 2007 delegation to New Zealand.
- 1.3 This chapter provides background information on the history and objectives of the committee exchange program and on the committee's specific objectives of the 2007 exchange.
- 1.4 The following chapter briefly discusses the trans-Tasman economic and trade relationship and the state of the New Zealand economy.
- 1.5 The monetary policy decisions of the central banks in both Australia and New Zealand are regularly scrutinized by parliamentary committees within their jurisdictions. This is a role of the House Economics Committee and of the New Zealand parliament's Finance and Expenditure Select Committee. Chapter three provides an overview of the role, operations and accountability of the Reserve Bank of New Zealand, with commentary on the Reserve Bank of Australia, where appropriate.
- 1.6 Chapter four discusses the situation in New Zealand in matters which were the subject of committee inquiries in the 41st parliament and also

provides commentary on the Commerce Select Committee's inquiry into housing affordability. The diversification of New Zealand Post Group's activities into banking is also briefly discussed.

Figure 1.1 Delegation members at the Parliament House Buildings, Wellington



New Zealand parliamentary committee exchange program

History and objectives

- 1.7 The Australia-New Zealand Parliamentary Committee exchange program commenced in 1989 primarily as a means of promoting parliamentary relations between New Zealand and Australia.
- 1.8 In most years since 1989 an Australian parliamentary committee delegation has been hosted by the New Zealand parliament. Similarly, the Australian parliament has hosted a New Zealand committee delegation in those years.
- 1.9 As the Australian parliament has three types of committees— House of Representatives, Senate and Joint committees— the delegations are selected from each committee system on an annual rotating basis.

- 1.10 In 2007 nominations for committee delegations came from the House committees. The Presiding Officers select a committee to participate in the exchange on the basis of their application which sets out reasons why visiting New Zealand would enhance the work of the committee.

Aims of the 2007 visit

- 1.11 The delegation identified a range of policy areas for discussion during the visit including retirement savings, the state and future of the manufacturing and services sectors and financial sector issues. These are also particularly topical areas in New Zealand, both in the private and public sector.
- 1.12 The House Economics Committee has an on-going role in the accountability framework of the Reserve Bank of Australia. Similarly, in New Zealand the New Zealand House of Representatives Finance and Expenditure Select Committee (FEC) scrutinises and holds to account the Reserve Bank of New Zealand. It was particularly useful for members of each committee to meet and discuss the approaches used to examine and scrutinise the central banks. The committee also had discussions with the Reserve Bank of New Zealand about its role, regulatory functions, the state of the economy and monetary policy in general.
- 1.13 Underlying the delegation's subject matter objectives was the aim to foster strong inter-parliamentary relations between Australia and New Zealand.

Meetings with New Zealand parliamentarians

- 1.14 The delegation was honoured to meet with the Speaker of the New Zealand House of Representatives; the Honourable Margaret Wilson MP. They had discussions with the Speaker on a number of economic and policy issues. The committee members also commented on the efficiency of question time, which they observed during the visit.
- 1.15 The Speaker generously hosted a dinner for the delegation which provided an opportunity to meet with Dr the Hon Michael Cullen MP, Minister for Finance; the Hon Lianne Dalziel MP, Minister for Commerce, the Hon Peter Dunne MP, Minister for Revenue and Ms Jeanette Fitzsimons MP, Leader of the Green Party.
- 1.16 The delegation met with opposition members with responsibilities for issues of committee interest including Mr Phil Heatley MP, Opposition

Spokesperson on Housing and the Hon Bill English, Deputy Leader of the Opposition and Spokesperson on Finance.

- 1.17 Over the course of the visit a number of parliamentarians took the time to attend meetings and official engagements with the delegation. In particular, the delegation were grateful for the repeated hospitality shown by Dr the Hon Lockwood Smith MP, the Chair of the Australia-New Zealand Parliamentary Friendship group; Mr Shane Jones MP, Chair of the Finance and Expenditure Select Committee, Mr Wayne Mapp MP, Mr Charles Chauvel MP and Ms Moana Mackey MP.

Figure 1.2 Delegation members meeting with the Chair and members of the Finance and Expenditure Select Committee



New Zealand counterpart committees of the House Economics Committee

- 1.18 New Zealand parliament's select committees comprise members of government and opposition parties, represented in proportion to party membership in the House.
- 1.19 Two New Zealand select committees cover similar functions of the House Economics Committee. With no upper house in the New Zealand

Parliament, committee work covers bills, petitions and policy matters referred for inquiry.

- 1.20 The New Zealand House of Representatives Finance and Expenditure Select Committee (FEC) consider matters relating to the audit of the financial statements of the New Zealand Government and departments, Government finance, revenue, and taxation. Their role includes the scrutiny of the Reserve Bank of New Zealand.
- 1.21 The New Zealand House of Representatives Commerce Select Committee ('the Commerce Committee') considers matters relating to commerce, business development, communications, consumer affairs, energy, information technology, insurance, and superannuation.

Figure 1.3 Delegation members meeting with the Chair and members of the Commerce Select Committee



Official visit program

- 1.22 The program compiled for the visit was of a very high standard. It allowed the delegation to consider a number of areas of committee oversight and inquiry work, and also to gain a solid understanding of the New Zealand economy; Australia's seventh most important two-way trading partner.

- 1.23 The role of the FEC in scrutinizing the Reserve Bank of New Zealand (RBNZ) and the operations of the RBNZ were important aspects of discussions during the visit.
- 1.24 The delegation met with the New Zealand Commerce Committee, currently undertaking an inquiry into housing affordability—an area of mutual policy interest, albeit not an inquiry area covered by the committee in the 41st parliament.
- 1.25 The House Economics Committee inquiries highlighted in discussions during the visit were *Improving the Superannuation Savings of People under 40*, tabled in June 2006, and the inquiry into the state of Australia's manufactured export and import competing base, now and beyond the boom—tabled after the visit in August 2007 as *Australian manufacturing: today and tomorrow*.
- 1.26 Discussions also included the committee's recent inquiry into the state and future directions of Australia's services sector—the report *Servicing our Future* was tabled on 18 June 2007.
- 1.27 The delegation met with parliamentarians, market economists, representatives of the finance and banking industry, and officials from a number of government departments on these policy areas.
- 1.28 The delegation also had the opportunity to discuss technology improvements recently introduced to the New Zealand parliament committee office. This included the "E-Committee" program which was being piloted by the Commerce Committee. E-Committee is a secure networked system which New Zealand members of parliament can access via permanent lap-tops set-up in committee meeting rooms.
- 1.29 The official program is included in Appendix A.

The trans-Tasman relationship

- 2.1 The delegation met with a number of non-government officials who discussed the nature of the Australia-New Zealand economic and cultural relationship.
- 2.2 Australia has a strong relationship with New Zealand. This stems from being antipodeans, having similar historic backgrounds as Commonwealth countries and the strong bonds forged almost a century ago during the ANZAC alliance.

Closer economic relations

- 2.3 The Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) came into effect on 1 January 1983. The agreement is a bi-lateral agreement covering trade; working relationships regarding quarantine; customs; regulatory standards; transport and commercial law matters.
- 2.4 The Closer Economic Relations agreement was discussed at a number of meetings the delegation attended.
- 2.5 Since its inception, trade between the two countries has expanded exponentially.¹ ANZCERTA contains rules of origin (ROO) which allow duty-free access for goods meeting the ROO requirements. Almost all goods meet these requirements now.

1 An average annual growth of nine per cent per annum. Department of Foreign Affairs and Trade, *New Zealand Country Information*, July 2007, p. 6. Website viewed 24 August 2007, <http://www.dfat.gov.au/geo/new_zealand/nz_country_brief.html>.

- 2.6 The growth in trade is reflected in New Zealand being Australia's sixth largest world market, accounting for around six per cent of Australia's exports.² Australia is New Zealand's number one import and export market accounting for around 20.3 per cent of its imports and around 20.4 per cent of its exports.³ The European Union is New Zealand's second biggest export market at 15 per cent of exports, followed by the United States at 13 per cent, Japan at 11 per cent and China at six per cent.
- 2.7 Trans-Tasman merchandise trade was valued at \$15.3 billion in the year to December 2006.⁴
- 2.8 Not only has ANZCERTA contributed to the growth in merchandise and service trade between the two countries but it has also opened the way for considerable two-way investment. Total foreign investment stocks from New Zealand amounted to \$24.3 billion to June 2005. New Zealand is the seventh largest foreign investor in Australia. Similarly, New Zealand rates highly with Australian investors, being the third largest foreign investment destination.
- 2.9 Australia is the largest foreign investor in New Zealand, most of this is foreign direct investment. The total stock of Australian investment in New Zealand was \$58.9 billion as at year ended 2005.⁵ There was a significant increase in Australian foreign direct investment into New Zealand between 2004 and 2005 with stocks increasing by \$19.5 billion. Much of the increase in foreign direct investment since 2003 has been in New Zealand infrastructure and the banking sector.

Single trans-Tasman economic market

- 2.10 Since the inception of ANZCERTA both the New Zealand and the Australian Governments have been committed to working towards a single economic market between the two countries. The Australian Treasurer, Mr Peter Costello MP and the New Zealand Minister of Finance,

2 Department of Foreign Affairs and Trade, *Trade at a Glance 2007*, Canberra, p. 12.

3 Department of Foreign Affairs and Trade, *New Zealand Fact Sheet*, May 2007. Website viewed 24 August 2007, <<http://www.dfat.gov.au/geof/fs/nz.pdf>>.

4 Department of Foreign Affairs and Trade, *New Zealand Country Information*, July 2007, p. 7. Website viewed 24 August 2007, <http://www.dfat.gov.au/geo/new_zealand/nz_country_brief.html>.

5 Department of Foreign Affairs and Trade, *New Zealand Country Information*, July 2007, p. 7. Website viewed 24 August 2007, <http://www.dfat.gov.au/geo/new_zealand/nz_country_brief.html>.

Dr Michael Cullen MP have meet on four occasions between January 2004 and January 2007 to progress this agenda.

- 2.11 In these meetings the Ministers have agreed to work towards a single market regulatory framework. As a result of these meetings there has already been a reduction in the regulatory barriers involved in doing trans-Tasman business including in the areas of business law and business and financial services.
- 2.12 There is already legislation facilitating joint co-operation between the countries' banking and prudential supervisory bodies and the central banks. There has also been a memorandum of understanding signed on Business Law Coordination which has included the recognition of certain cross-border business law issues and a protocol of information sharing about mergers between the Australian Consumer and Competition Commission and the New Zealand Commerce Commission.
- 2.13 The January 2007 meeting sought to progress single market patent application processes, double taxation legislation, retirement savings portability and cross-border court proceedings and judgement recognition.
- 2.14 The suggestion of a currency union is often debated within the countries. The Reserve Bank of New Zealand (RBNZ) included a chapter on the economic merits of a single currency with Australia in their December 2005 Reserve Bank Bulletin.⁶ The delegation did not have any in-depth discussions on this issue during meetings.

New Zealand economy

General

- 2.15 The New Zealand economy has undergone significant structural reforms since the mid 1980s which freed-up a highly regulatory regime and a rigid macro-economic framework. The program of reforms was extensive.⁷ As a result of these reforms New Zealand now has a largely deregulated market and one of the most liberalised market economies in the developed world. New Zealand currently enjoys the enviable second position in the World

6 Reserve Bank of New Zealand, *Reserve Bank of New Zealand Bulletin Volume 68 No. 4*, December 2005, p. 16. Website viewed 24 August 2007, <http://www.rbnz.govt.nz/research/bulletin/2002_2006/2005dec68_4.pdf>

7 Organisation of Economic Cooperation and Development, *The OECD Observer*, No. 212, June-July 1998, 'New Zealand Reform of the Financial Sector', Hans Suppanz.

Bank's 'Ease of doing business' study.⁸ The study assesses business friendly regulations.

- 2.16 With the spread of internet usage and the buoyancy of the Asian market, some of New Zealand's traditional impediments to global trade have been removed. The growing markets are now more accessible and closer than Europe.
- 2.17 Real Gross Domestic Product (GDP) to March 2007 was NZ\$128 billion⁹, with the services sector being the primary contributor to GDP, accounting for approximately two thirds.¹⁰ The primary sector accounts for around seven per cent and the manufacturing sector around 14 per cent.¹¹
- 2.18 The country's principle exports are dairy products; meat; forestry products; machinery; metals; fish; and fruit. Total merchandise exports amounted to NZ\$32.4 billion in 2006.¹² Services exports sit at around NZ\$11.8 billion.¹³
- 2.19 Economic growth has been strong since around 1999 (averaging 3.7 per cent to 2004), with a slight easing of growth since 2005, as shown in Figure 2.1. Real GDP growth was 1.2 per cent in the March 2007 quarter showing a strengthening.¹⁴ The key drivers of this growth have been service industries and household consumption.

8 World Bank and the International Finance Corporation, *Doing Business in 2007: How to reform, comparing regulation in 175 countries*, Washington, 2007.

9 New Zealand GDP is approximately one eighth of Australia's GDP. Invest New Zealand, *NZ Facts and Figures*, Website viewed 27 August 2007, <<http://www.investmentnz.govt.nz/section/14341.aspx>>.

10 Department of Foreign Affairs and Trade, *New Zealand Country Information*, July 2007, p. 5. Website viewed 24 August 2007, <http://www.dfat.gov.au/geo/new_zealand/nz_country_brief.html>.

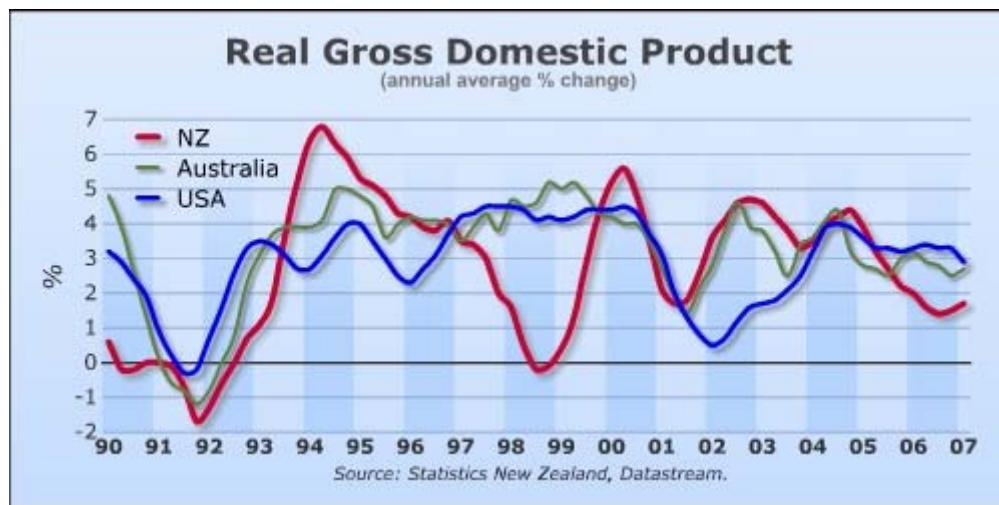
11 Invest New Zealand, *NZ Facts and Figures*, Website viewed 27 August 2007, <<http://www.investmentnz.govt.nz/section/14341.aspx>>.

12 Statistics New Zealand, *New Zealand in Profile: An overview of New Zealand's people, economy and environment*, 2007.

13 Statistics New Zealand, *New Zealand in Profile: An overview of New Zealand's people, economy and environment*, 2007.

14 Invest New Zealand, *NZ Facts and Figures*, Website viewed 27 August 2007, <<http://www.investmentnz.govt.nz/section/14341.aspx>>.

Figure 2.1 Real Gross Domestic Product New Zealand 1990—2007



Source Reserve Bank of New Zealand, *Key graphs, GDP Growth*, 2 July 2007

The 'white gold' boom

- 2.20 While Australia is experiencing a resources boom, the New Zealand economy is experiencing a dairy boom. New Zealand's top merchandise export is 'milk powder, butter and cheese' with a value of NZ\$5.8 billion in 2006 and accounting for 15 per cent of New Zealand exports.¹⁵ New Zealand has an impressive 25 per cent of the world trade in dairy products.
- 2.21 New Zealand's dairy production is very efficient. Livestock graze outside—they are not housed in winter as is the case in Europe—and are therefore grass-fed, not corn fed. Corn-fed stock are more expensive to feed and this has been exaggerated by increased demand for corn cropping for bio-fuel use.¹⁶ With increasing grain prices, dairy farming has become relatively uneconomic and thus the worldwide supply of dairy product has decreased. This has led to higher prices for dairy commodities. Australia's drought conditions, which have reduced Australian dairy export, have added to this environment.
- 2.22 The second part of the New Zealand dairy boom equation can be attributed to the rise in the standard of living in many highly populated Asian countries. As people become more affluent they demand more protein. Soy protein is becoming more expensive and thus the rise in the

15 Statistics New Zealand, *New Zealand in Profile: An overview of New Zealand's people, economy and environment*, 2007.

16 The emissions footprint of New Zealand livestock is less than European livestock but methane emissions remain an issue.

demand for dairy. This increase in demand has coincided with a worldwide reduction in supply, further boosting prices for dairy product.

- 2.23 Dairy is New Zealand's number one export and as such the increase in the commodity price has led to elevated terms of trade and an appreciation in the value of the New Zealand dollar.¹⁷ This has had a number of impacts on the New Zealand economy. These include the reduction in merchandise export competitiveness and reinforcing the high current account deficit of NZ\$13.9 billion for the year to March 2007.¹⁸ This is a slight reduction from NZ\$15.2 billion for the year to June 2006, which then represented 9.7 per cent of GDP.¹⁹
- 2.24 The New Zealand dollar has been steadily appreciating, approximating US75c and AUS89c in June 2007. Concern over the level of the dollar and the impact on New Zealand export performance led to the Reserve Bank of New Zealand intervening in the foreign currency market in 2007 to dampen the exchange rate.
- 2.25 The delegation heard that the high dollar is not so much the issue as is the volatility in the exchange rate which makes it difficult for exporters to plan an export program or strategy.

Inflation and interest rates

- 2.26 New Zealand's consumer price index rose 2.6 per cent in the year to December 2006 and had eased slightly to 2 per cent by the year ended June 2007.
- 2.27 The economy is at full employment with a record unemployment rate of 3.8 per cent to the March 2007 quarter.²⁰ This has led to labour and skills shortages in pockets of the economy.
- 2.28 As the New Zealand dollar appreciated imports became cheaper. Despite this, domestic inflation has increased. The inflation figures released on 16 July 2007 were higher than anticipated.

17 At the time of the visit the New Zealand dollar was around US78c and this was after currency intervention by the New Zealand Reserve Bank on 11 June 2007.

18 Reserve Bank of New Zealand, *Economic Indicators, A4 Labour Market and Balance of Payments*, March 2007 quarter.

19 This was the highest level of the current account deficit since the 1975 oil shock. Department of Foreign Affairs and Trade, *New Zealand Country Information*, July 2007, p. 5. Website viewed 24 August 2007, <http://www.dfat.gov.au/geo/new_zealand/nz_country_brief.html>.

20 Invest New Zealand, *NZ Facts and Figures*, Website viewed 27 August 2007, <<http://www.investmentnz.govt.nz/section/14341.aspx>>.

2.29 At the time of the delegation's visit the Reserve Bank of New Zealand (RBNZ) had moved the official cash rate (OCR) three times since 8 March 2007, each a 25 basis point move. Prior to that the rate had not been moved since 8 December 2005.

2.30 Following the delegation's visit a further 25 basis point rise occurred on 26 July 2007. In the RBNZ's press release on the day of the rise the Governor, Dr Alan Bollard stated:

The New Zealand economy is running strong. We are recording continued big increases in international commodity prices, especially dairy, reflecting solid world demand for our products. This is very good news for New Zealand. Given this positive situation, some of the negative commentary circulating about the economy is unwarranted. However, the continued tight labour market, high capacity use, and rising oil and food prices all point to sustained inflationary pressures. That is why we are increasing the OCR today.²¹

2.31 The cash rate now stands at 8.25 per cent—approximately 1.65 percent above Australia's official cash rate after the Reserve Bank of Australia's cash rate move on 8 August 2007.

Reserve Bank intervention in the foreign exchange market

2.32 The New Zealand dollar rose 3.2 per cent in June 2007 on the previous month, but was 18.1 per cent higher than June 2006. It was sitting at 25 per cent above purchasing power parity.

2.33 The Reserve Bank of New Zealand intervened in the foreign exchange market and for the first time bought foreign reserves (thus selling New Zealand dollars) to dampen the value of the dollar which they believed to be out of sync with the economy and unsustainable in the medium term.

2.34 In the RBNZ's recent press release on the raising of the official cash rate to 8.25 per cent the Governor, Dr Alan Bollard noted:

The New Zealand dollar has reached very high levels recently, driven by US dollar weakness and New Zealanders' heavy demand for borrowing. This level of the currency has been hurting exports. The high New Zealand dollar is not sustainable medium

21 Reserve Bank of New Zealand, *Reserve Bank raises OCR to 8.25 per cent*, 26 July 2007. Website viewed 27 August 2007, <<http://www.rbnz.govt.nz/news/2007/3074597.html>>.

term and investors should understand this. The higher OCR now gives strong incentives to New Zealanders to save.²²

Labour market

- 2.35 Despite the dairy boom not creating many extra jobs in New Zealand (as at March 2007 the agricultural sector employed 7.2 per cent of New Zealand's workforce) the country is enjoying full employment with unemployment at a record low of 3.8 per cent, being one of the lowest rates in the OECD.²³ The demand for labour has mainly come from service industries.
- 2.36 Wages and salaries are around 25 per cent lower on average than those in Australia.²⁴ As the cost of living is comparable to that in Australia and with easy work entry across the Tasman (including mutual recognition of qualifications), skilled labour has been migrating to Australia.
- 2.37 There are approximately 1 million New Zealanders working offshore. With a population of around 4.2 million this amount is considerable.
- 2.38 The delegation heard that New Zealand needs to move to global wage and salary levels to retain a quality labour force. This issue occurs in Australia, but the exodus is far smaller.²⁵ The tight labour market is leading to growth in labour incomes but with that comes inflationary pressures.

Productivity

- 2.39 New Zealand is experiencing a labour market conundrum of low unemployment but lower productivity than would be expected in an economy at or near full capacity. Multi-factor productivity fell 1 per cent in the measured sector to March 2006 while labour market productivity grew by 0.7 per cent in the same period. This is illustrated in Figure 2.2.
- 2.40 This productivity puzzle has also been raised by the Governor of the Reserve Bank of Australia, Mr Glenn Stevens, as a perplexing phenomena occurring in Australia as well.²⁶ However, New Zealand is confronted with

22 Reserve Bank of New Zealand, *Reserve Bank raises OCR to 8.25 per cent*, 26 July 2007. Website viewed 27 August 2007, <<http://www.rbnz.govt.nz/news/2007/3074597.html>>.

23 Invest New Zealand, *NZ Facts and Figures*, Website viewed 27 August 2007, <<http://www.investmentnz.govt.nz/section/14341.aspx>>. Also, OECD, Statistics Portal – Labour, *Unemployment Statistics*, 10 August 2007.

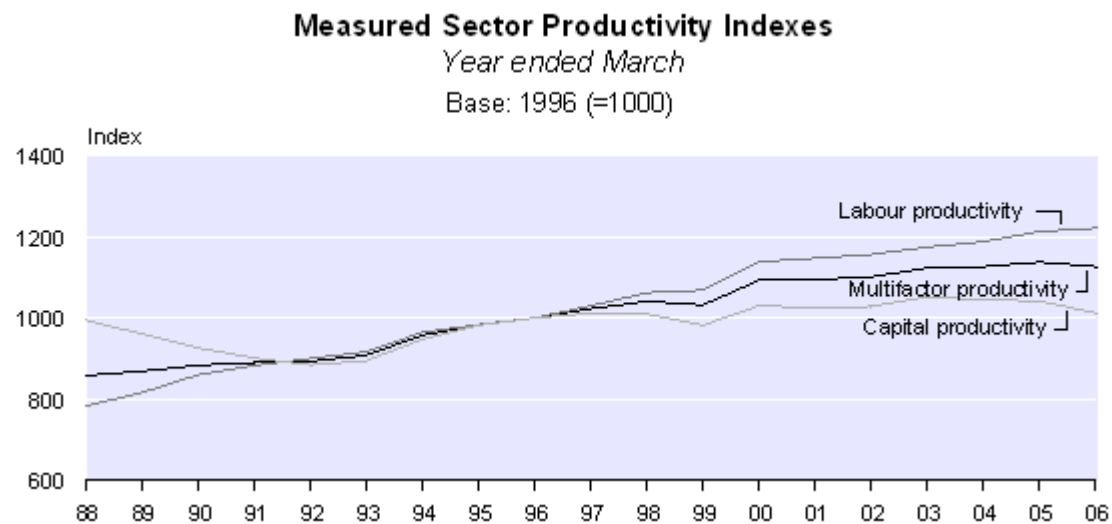
24 OECD, *Comparison of Wage Levels*, Gross Wage in National Currency, 2004. Website viewed 27 August 2007, <<http://www.oecd.org/dataoecd/33/28/34545117.pdf>>.

25 As examples, there are approximately 60 000 Australians working in Hong Kong and 10 000 in Dubai.

26 Mr G Stevens, Governor of the RBA, *Transcript*, 21 February 2007, p. 16.

this issue on a larger scale – Australian productivity averages 30 per cent more than New Zealand's.

Figure 2.2 Measured sector productivity indexes year ended March 2006: base 1996 = 1000



Source Statistics New Zealand, *Productivity Statistics 1998-2006 (revised)*

2.41 In the media conference release of the Budget 2007 papers in December 2007 the Minister of Finance, Dr Michael Cullen gave some possible reasons behind New Zealand's sluggish productivity:

The economy is clearly in good heart. Businesses are becoming more confident about the level of their own activity and the tight labour market suggests businesses are holding on to staff in anticipation of a recovery. Indeed, Treasury forecasts a considerable lift in labour productivity over the next two years. This is essential if we are to enjoy a higher sustainable level of economic growth in the future.²⁷

2.42 There is also suggestion that some of this problem is associated with skilled labour moving offshore, being replaced with semi and unskilled labour. Approximately 600-700 New Zealanders leave for Australia each week. Even though the country received net migration most of those leaving are single people who are participating in the workforce, whereas most immigrants were families and thus not all of these people participate in the workforce.

27 The Treasury, Budget 2007 Press Release, *New Zealand Economy Proves Resilient*, the Minister of Finance, the Hon Dr Michael Cullen, 19 December 2006. Website viewed 27 August 2007, <<http://www.beehive.govt.nz/ViewDocument.aspx?DocumentID=28128>>.

- 2.43 The delegation heard that improving productivity was a key challenge for New Zealand.

Fiscal policy and future fund

- 2.44 Fiscal surpluses have been run for the past 15 years. In 2001, in view of fiscal surplus accumulation, the Government chose to set-up a 'future fund' to provide partial funding for the New Zealand national pension scheme.²⁸ This fund is called the New Zealand Superannuation Fund and will be discussed in more detail in Chapter 4.
- 2.45 Fiscal policy has recently been more expansionary with greater expenditure on infrastructure, in particular roads and energy facilities and on social policy. The Minister of Finance noted on budget day 2007:

The improved fiscal position will allow the introduction of a significant business tax package to take effect from 1 April 2008 and improves our ability to tackle other priorities such as climate change. Budget 2007 will also continue our progress in building a unique national identity and meeting the aspirations of families, young and old, to be healthier and more secure through initiatives to enhance our world class education, healthcare and social services.²⁹

Capital market and infrastructure

- 2.46 As a small and geographically remote country it is important for New Zealand to have strong transport and telecommunications infrastructure. While some areas of infrastructure are robust, others need investment.
- 2.47 New Zealand ports and airports are very efficient. There were a number of reforms in the late 1990s which led to these improvements. However, the country is experiencing some infrastructure deficits; primarily in transport infrastructure. Investment is also required in utilities infrastructure, particularly energy and water.

28 The fund was established under the *New Zealand Superannuation and Retirement Income Act 2001*.

29 The Treasury, Budget 2007 Press Release, *New Zealand Economy Proves Resilient*, the Minister of Finance, the Hon Dr Michael Cullen, 19 December 2006.
<<http://www.beehive.govt.nz/ViewDocument.aspx?DocumentID=28128>>.

- 2.48 The delegation heard that tradeable water rights are an issue. In the Canterbury region 90 per cent of water resources are allocated and the demand for water is set to double over the next ten years.
- 2.49 High speed broadband internet penetration is seen as a way to connect New Zealand with the world market and therefore of high priority. This is a challenge due to the thin spread of homes in New Zealand and the economics of rolling-out broadband to homes. Broadband is considered a way to attract foreign direct investment and to enable creative services to be delivered.
- 2.50 New Zealand has experienced some issues raising capital for projects because of the low pool of savings in their domestic market. The economy is heavily reliant on foreign capital, much of which comes from Australia.
- 2.51 The need for a strong capital market has led to policies to encourage New Zealanders to save. The most important of these has been the development of KiwiSaver – an auto-enrolment superannuation savings scheme – which commenced on 1 July 2007. KiwiSaver is discussed in Chapter 4.

Household demand and housing affordability

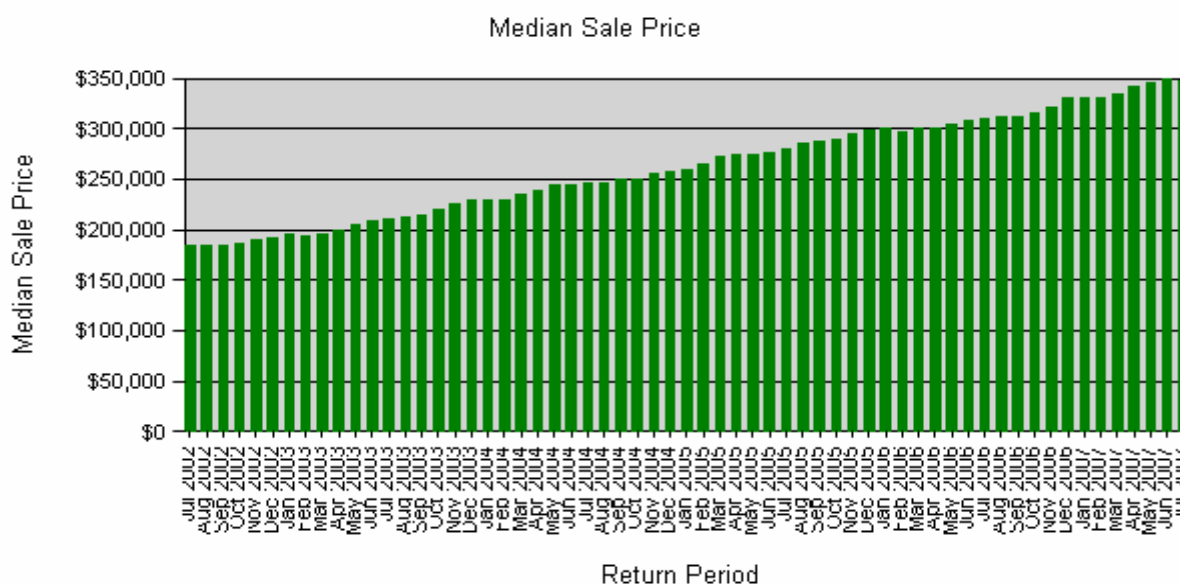
- 2.52 New Zealanders have a history of hesitancy to invest in the stock market. This may have been related to losses experienced in the stock market crash of 1987 which, on average, affected New Zealanders more than it did Australians.
- 2.53 Unlike in Australia, New Zealanders have not experienced the marketing and take-up of shares by ‘mums and dads’ when large, previously government owned bodies were publicly floated. Australians were introduced to the notion of holding shares in this way and through the de-mutualisation of well-known membership bodies (like NRMA Insurance Limited). Australians hold the highest share ownership in the world, at around 55 per cent total share ownership.³⁰ In comparison, New Zealand direct share ownership was around 23 per cent in 2005.³¹

30 Australian Stock Exchange, *International Share Ownership – Comparison of Share Owners: Key Highlights*, September 2005, p. 2.

31 Australian Stock Exchange, *International Share Ownership – Comparison of Share Owners: Key Highlights*, September 2005, p. 2.

- 2.54 New Zealanders have instead enthusiastically invested in real estate, which has created a property boom. Median dwelling prices have almost doubled in the past five years, as exhibited in Figure 2.3.³²
- 2.55 The investor-led boom has been exacerbated by lenient capital gains tax rules plus the ability to deduct rental losses against income. Capital gains tax liability is dependent upon whether the owner 'intends' to make a capital gain at the time of asset purchase. Additionally, New Zealand has experienced net migration and that has fuelled demand for housing.
- 2.56 Ironically, home ownership in New Zealand has fallen. The country once had the highest level of home ownership in the developed world. Home ownership has fallen from 74 per cent in 1991 to 68 per cent in 2006.³³ The fall in home ownership has been greater than the fall in home ownership in Australia.³⁴

Figure 2.3 Median selling prices of dwellings in New Zealand between July 2002—July 2007



Source Real Estate Institute of New Zealand, *Market facts: Median selling price July 2002-July 2007*

32 Real Estate Institute of New Zealand, *Market facts: Median selling price July 2002-July 2007*. Website viewed 27 August 2007, <<http://210.48.74.140/reportingapp/default.aspx?RFOPTION=Report&RFCODE=R100>>.

33 Housing New Zealand, Housing New Zealand Corporation, *New Zealand Housing Strategy – Homeownership*, 26 September 2006. Website viewed 27 August 2007, <<http://www.hnzc.co.nz/hnzc/web/research-&-policy/strategy-publications/nzhs/online-version/area-3---homeownership.htm>>

34 Absolute home ownership levels are similar. In August 2001 Australia had a home ownership rate of 69 per cent. Australian Bureau of Statistics, *Australian Social Trends 2003*, cat. 4102.0, ABS, Canberra, June 2003.

- 2.57 New Zealand household debt is very high while household savings are low. As previously mentioned this is a dual cause of monetary policy concern – reigning in household demand and yet encouraging savings. On average, New Zealand households are spending 15 per cent more than they are earning. Some of this has come from mortgage equity withdrawal.

New Zealand securities market

- 2.58 The average New Zealand sharebroker holds a quarter to a half of all portfolios in Australian equities. Australia is also the first country for New Zealanders to invest in after New Zealand. New Zealanders hold very little US stock. This situation is somewhat generated by the mineral stocks in Australia and the favourable tax treatment of New Zealand and Australian stock.
- 2.59 New Zealand is a massive recipient of foreign direct investment from Australia. In 2006 Australia contributed a substantial 46 per cent of all total foreign direct investment in New Zealand.³⁵ There is far more liquidity in Australia than there is in New Zealand. As a consequence, the New Zealand economy has a larger proportion of off-shore ownership than Australia.
- 2.60 Acquisitions and mergers are seen as more of a problem in New Zealand than in Australia because Australia has foreign ownership caps whereas in New Zealand there are no ownership caps, excepting New Zealand's Telecom. This makes New Zealand a private equity target. There have already been a number of private equity deals in New Zealand which have taken businesses off the New Zealand Stock exchange.

35 Inland Revenue Department, *New Zealand's International Tax Review: A direction for change – A Government discussion document*, Minister of Finance & Minister of Revenue, December 2006.

Central bank roles, operations and accountability

The Reserve Bank of New Zealand—regulatory powers

Independence

- 3.1 Like Australia's Reserve Bank the independence of the Reserve Bank of New Zealand (RBNZ) has bi-partisan support. It is enshrined in the *Reserve Bank of New Zealand Act 1989*.
- 3.2 Prior to the 1989 Act the RBNZ's powers had rested with the Bank's Board and the Board was charged with implementing the monetary policy of the government of the day. However, the 1989 Act gave the Bank the ability to make adjustments to monetary policy with 'operational autonomy'—no day-to-day political involvement. With the shift to independence the Governor of the Reserve Bank became accountable for the Bank's actions and as a consequence accountability and transparency measures became very important.
- 3.3 The framework of accountable autonomy is that the Governor is the primary decision-maker with the Board providing a monitoring role and reporting on the Governor's performance. The Board does not direct the Bank's policy. This differs from the Reserve Bank of Australia (RBA) where the Bank's Board is responsible for monetary policy decisions.

Role of the Reserve Bank of New Zealand

- 3.4 The RBNZ has three major roles. These include operating monetary policy to maintain price stability; promoting the stability of the financial sector and meeting the currency needs of the public.
- 3.5 The RBA's three major roles are very similar – operating monetary policy; maintaining financial system stability and promoting safety and efficiency of the payments system.

Primary role—monetary policy

- 3.6 The Bank's primary function is to ensure financial and economic stability through the operation of monetary policy. The RBNZ has been overseeing monetary policy since the Bank's inception in the 1930s.
- 3.7 Since March 1999 New Zealand monetary policy has been exercised through decisions by the Bank on the state of the official cash rate. The Bank affects the official cash rate by setting the interest rate on overnight loans in the money market, which affects the costs of borrowing and influences the level of demand in the economy.
- 3.8 The use of monetary policy is defined in the *Policy Targets Agreement* (PTA)¹. The PTA is an agreement negotiated and signed by the Minister of Finance and the Governor of the Reserve Bank of New Zealand. The current PTA, signed on 24 May 2007, is designed to ensure price stability and it aims to achieve this by containing inflation within a target range of between one and three per cent 'on average over the medium term'.² New Zealand was the first of the developed countries to follow an inflation targeting regime, introduced in 1990. The target was initially zero to two percent, which the Bank achieved by 1992.
- 3.9 The PTA is similar to Australia's *Statement on the Conduct of Monetary Policy*, a statement which records the understanding between the Governor of the Reserve Bank of Australia and the Australian Government on key aspects of monetary policy. Both the RBNZ and the RBA sign a new agreement when a new Governor is appointed however the PTA has been changed intermittently, adopting different inflation target ranges on the

1 Made under section 9 of the *Reserve Bank of New Zealand Act 1989*.

2 Policy Targets Agreement 2007. Website viewed 22 August 2007, <<http://www.rbnz.govt.nz/monpol/pta/3027051.html>>.

agreement.³ The PTA forms the basis of the accountability structure of the Reserve Bank of New Zealand. This is not the case in Australia.

- 3.10 The third Australian statement signed off on 18 September 2006 aims for medium term price stability with 'an objective of keeping consumer price inflation at between two and three per cent, on average, over the cycle'.⁴ The RBA has been using this target range since 1993 to achieve the Bank's three main goals of maintaining the stability of the Australian currency; full employment; and economic prosperity and the welfare of the Australian people.⁵
- 3.11 The RBNZ reviews monetary policy eight times a year, every six weeks, whereas the RBA reviews the official cash rate monthly, excepting the month of January, when it does not meet. The New Zealand official cash rate may be changed at other unscheduled times as a response to economic shocks.⁶

Foreign exchange intervention as an additional monetary policy tool

- 3.12 The RBNZ has the power under the 1989 Act to intervene in the foreign exchange market to calm disorderly market behaviour or market dysfunction. This sort of intervention can also be used as a supplementary monetary policy pool.
- 3.13 There is considerable debate in New Zealand about the RBNZ's primary role in foreign exchange intervention and whether foreign currency intervention is an appropriate supplementary monetary policy tool.
- 3.14 During meetings on the visit the delegation heard views for and against RBNZ intervention in the forex market. This was topical at the time of the visit, the Bank having intervened in the foreign exchange market on 11 June 2007, selling New Zealand dollars to buy foreign reserves. This was the first intervention of this kind since the floating of the New Zealand dollar in March 1985.
- 3.15 The intervention in June was designed to flatten the value of the rapidly appreciating New Zealand dollar (at an all time high in real terms) which was impeding the competitiveness of price-sensitive New Zealand

3 Under section 12 of the *Reserve Bank of New Zealand Act 1989* the bank has the power to override the PTA for a period of twelve months.

4 *The Third Statement on the Conduct of Monetary Policy*, 18 September 2006. Website viewed 22 August 2007, <<http://www.rba.gov.au/MonetaryPolicy/>>.

5 Enshrined in the *Reserve Bank Act 1959*.

6 As exhibited by the RBNZ after the 11 September 2001 terrorist attacks in America.

exports.⁷ Foreign currency was flooding in to take advantage of the high cash rate in New Zealand – running at 8.00 per cent in June 2007.⁸

- 3.16 At the time of writing New Zealand has the highest official cash rate in the industrialised world. As a result of this there has been heavy speculative activity in the New Zealand currency market which has inflated the value of the dollar beyond the appreciation accruing from dairy and associated primary industry commodity price increases.
- 3.17 Much of this speculative activity is coming from high saving countries like Japan (where the Yen has been at five year lows against the US dollar) and from the oil nations where the interest rate differential is significant. This has happened in both New Zealand and in Australia but the New Zealand differential has been greater than Australia's. Both markets are seen as good risks with the Governments' and banks stable and having strong central banks.
- 3.18 In June 2007 the Reserve Bank of New Zealand decided that the high exchange rate could not be sustained for the medium term. The level of the exchange rate was not analogous with other economic indicators including, inter alia, New Zealand's current account deficit which stood at around nine per cent of GDP in that month. The June action sent a signal to the market that speculation on the New Zealand dollar held risks.
- 3.19 The conundrum the Reserve Bank of New Zealand faces is how to reign in domestic inflationary pressures through tighter monetary policy but without unduly straining the export sector (particularly non-commodities exports) through an increase in the already high exchange rate.
- 3.20 The Deputy Governor, Mr Grant Spencer noted about the intervention:
- The Bank's primary monetary policy instrument is the Official Cash Rate (OCR). The foreign exchange intervention framework provides an additional tool for the purpose of trying to moderate the extremes of the exchange rate cycle.⁹
- 3.21 The RBNZ's foreign exchange intervention seeks to moderate peaks where the exchange rate does not reflect the true economy. The Bank's policy is to intervene only when the exchange rate is at 'exceptional levels'; when it is unjustified by medium term economic fundamentals; when intervention is
-

7 Although commodity prices have been high, export volumes have not been increasing. This may be linked to reduced investment in businesses.

8 The RBNZ moved the cash rate to 8.25 per cent on 26 July 2007 due to increasing domestic inflationary pressures.

9 Opinion article by Reserve Bank Deputy Governor Grant Spencer, 27 June 2007. Website viewed 24 August 2007, <www.rbnz.govt.nz/speeches/3049397.html>.

seen as consistent with the Policy Targets Agreement; and when market conditions make intervention opportune.¹⁰

- 3.22 The RBA has no history of using foreign exchange intervention as a supplementary monetary policy tool. However, since the floating of the Australian dollar in 1983 the RBA has intervened in the foreign exchange market on a number of occasions either to help drive equilibrium in the market, typically where the market has “over-shot” and asset prices have moved to levels ‘that do not seem reasonable in the context of a range of economic and financial developments’¹¹ or where conditions ‘threaten to create market disorder’.¹² Akin to the policy of the Reserve Bank of New Zealand this sort of intervention is not designed to achieve a particular level of exchange rate.

Accountability and transparency

- 3.23 Besides the formal scrutiny by the Board over monetary policy there are a number of other avenues of monitoring performed on the actions of the Reserve Bank of New Zealand. The New Zealand central bank’s 1989 legislation has a greater emphasis on providing accountability of the Bank meeting mandated objectives than it does on the Bank’s independence. The Bank is therefore subject to a wide degree of formal accountability.
- 3.24 RBNZ now publishes an annual *Statement of Intent*, a document designed to outline the way the RBNZ intends to operationally carry out its duties over the following three years. It includes the nature and scope of its function, predicted strategies to meet its objectives and resource issues. The Board is expected to consult with and take into account the views of the Minister of Finance when formulating the *Statement of Intent*.
- 3.25 Both central banks issue a quarterly Statement on the conduct of monetary policy which outlines the analysis behind their monetary policy decisions. However, only the Reserve Bank of New Zealand is required by legislation to publish such a document.¹³

10 Opinion article by Reserve Bank Deputy Governor Grant Spencer, 27 June 2007. Website viewed 24 August 2007, <www.rbnz.govt.nz/speeches/3049397.html>.

11 Reserve Bank of Australia, *Why does the Reserve Bank intervene in the foreign exchange market?* Website viewed 24 August 2007, <http://www.rba.gov.au/MarketOperations/International/ex_rate_rba_role_fxm.html>.

12 Reserve Bank of Australia, *Why does the Reserve Bank intervene in the foreign exchange market?* Website viewed 24 August 2007, <http://www.rba.gov.au/MarketOperations/International/ex_rate_rba_role_fxm.html>.

13 The *Reserve Bank of New Zealand Act 1989* requires statements are issued at least six monthly.

- 3.26 The RBNZ also provides brief commentary between the quarters, after it has reviewed monetary policy every six weeks. In contrast, the RBA only releases commentary in the interim periods if there has been a decision to alter the official cash rate.
- 3.27 The RBNZ publishes its forecasts of inflation, GDP, interest and exchange rates. It is also required by legislation to publish a public annual report.

Parliamentary oversight of monetary policy

Parliamentary scrutiny

- 3.28 The RBNZ's *Monetary Policy Statements* stand referred to the House of Representatives Select Committee on Finance and Expenditure (FEC) under section 15 of the *Reserve Bank of New Zealand Act 1989*. Each quarter, the day after the *Monetary Policy Statement* is released, the FEC meets with the RBNZ Governor to scrutinize the extent to which monetary policy has been conducted within the scope of the PTA. The FEC may have an independent adviser assist in the examination of the statements by briefing the committee before the hearing.
- 3.29 The FEC have no requirement to report to the House on the examination of the Monetary Policy Statement but this is general practice.
- 3.30 The Bank's Funding Agreement, which is agreed at five yearly intervals between the Minister of Finance and the Governor on how much of the Bank's income may be retained for operating costs, requires parliamentary approval. Thus, at least every five years the resources of the Bank are scrutinized.

Reviews—inquiry into the future monetary policy framework

- 3.31 The Finance and Expenditure Committee may inquire into any matter related to its subject areas as identified under the Standing Orders. As there is current debate in New Zealand surrounding what monetary policy instruments should be used by the Reserve Bank of New Zealand, the Finance and Expenditure Committee is conducting an inquiry into the future monetary policy framework.
- 3.32 Written submissions from the public closed on the last day of the delegation's visit, 19 July 2007.

3.33 The terms of reference for the inquiry are:

- to consider the causes of inflationary pressures;
- to consider the effectiveness of current monetary policy in controlling inflation;
- to examine the interaction of monetary policy with other elements of the economic policy framework including fiscal policy ;
- to examine the New Zealand economy's capacity for non-inflationary growth, and how it can be improved;
- to examine the role of productivity in the economy, how it can be improved, and the constraints upon it;
- to examine the recommendations from recent examinations of monetary policy including the joint Treasury and Reserve Bank of New Zealand's report entitled Supplementary Stabilisation Instruments; and
- to consider additional measures that could enhance monetary policy in New Zealand.

3.34 The inquiry has generated significant interest from the financial and business sectors, manufacturing and primary industries, academics, not-for-profit organisations and the general public. As at 20 August 2007 the FEC had received and authorised almost 100 submissions.

Matters of mutual economic and policy interest

Retirement savings

New Zealand superannuation

- 4.1 New Zealand superannuation provides a universal basic public pension. It is paid to all New Zealanders over age 65 irrespective of past income, current income or wealth. It is colloquially referred to as “65 at 65” because a single person living alone receives 65 per cent of what a pension-age married couple household receive. All rates are calculated from the married couple rate.
- 4.2 When New Zealand married couples reach 65 years of age, they receive, as a household unit, approximately 66 per cent of the Net Average Ordinary Time Weekly Earnings as a pension.¹ From 1 April 2007 a married or civil union couple receive after tax income of NZ\$426.24 per week from the public pension.² A single person household receives after tax income of NZ\$277.06 per week, while a single person sharing a household receives after tax income of NZ\$255.74 per week.

1 Approximately 33 per cent of the National Average Wage each, which is subject to marginal tax. Legislated under the *New Zealand Superannuation and Retirement Income Act 2001*.

2 Net Average Ordinary Time Weekly Earnings based on the December 2006 quarter was NZ\$645.82 per week.

- 4.3 The universality of the scheme means it is administratively simple and as it is not means tested it encourages private savings and for people to continue to work past retirement age.
- 4.4 In contrast, Australia has a safety net Age Pension which is available for eligible Australians between the ages of 63 and 65.³ The pension is means tested, and as such, pension income is calculated on a sliding scale. In addition, Australia has a compulsory superannuation savings scheme which requires employees to contribute nine per cent of an employee's salary (when salary exceeds a certain income threshold) to superannuation. This contribution is preserved until an employee retires and reaches age 55 – 60.⁴
- 4.5 A public fund, the 'New Zealand Superannuation Fund', has been established in New Zealand to provide part pre-funding of the public universal pension.
- 4.6 The investment performance of the fund has been very good, returning around 15.3 per cent per annum.⁵ Growth is forecast to be around 8.2 per cent over the next ten years. The fund's current value is NZ\$13.3 billion as at 31 May 2007.⁶ This fund is legislated to have fund contributions and to always have surpluses. It will not be drawn down until 2028.

KiwiSaver

- 4.7 New Zealand ranks low in the OECD average of private superannuation schemes.⁷ There are currently 590 private schemes of which 431 are employer schemes and 120 are retail schemes. Approximately 638 123 New Zealanders currently belong to a private superannuation scheme; of those, 304 622 are members of employer schemes and 333 443 are members of retail schemes.⁸
- 4.8 Net household savings as a percentage of GDP have steadily declined since the late 1980s. This is likely to be partly related to the non-means

3 Men can access the Age pension at age 65. Pension age for a female is being raised by six months every two years so that by 2014 male and female eligibility age will be the same.

4 The preservation age will remain at 55 years for a person born prior to 1 July 1960, while for someone born after 30 June 1964 the preservation age rises to 60.

5 New Zealand Superannuation Fund, Performance, 31 May 2007. Website viewed 27 August 2007, <<http://www.nzsuperfund.co.nz/index.asp?pageID=2145831960>>.

6 New Zealand Superannuation Fund, Performance, 31 May 2007. Website viewed 27 August 2007, <<http://www.nzsuperfund.co.nz/index.asp?pageID=2145831960>>.

7 OECD Economic Survey of New Zealand 2007. Web site viewed 28 August 2007, http://www.oecd.org/document/10/0,3343,en_2649_34569_38394186_1_1_1_1,00.html.

8 Superannuation fund data provided by Inland Revenue New Zealand.

tested, bi-partisan supported public pension and partly because there is currently no portability of superannuation between private schemes. In addition, with a housing boom underway, much of household disposable income is being channelled into housing and not into financial assets or savings.

- 4.9 To encourage voluntary savings the New Zealand Government has introduced an auto-enrolment savings scheme, KiwiSaver, primarily for retirement income purposes, which commenced on 1 July 2007, just before the delegation's visit. This scheme is designed to complement New Zealand superannuation, not replace it.
- 4.10 A feature of the savings scheme is its portability between New Zealand employers. KiwiSaver schemes are offered by private superannuation providers and thus it is not a government guaranteed scheme. Much of the scheme collections are administered through the Inland Revenue Department – PAYE deductions include the contributions and are sent to Inland Revenue on the monthly schedule.
- 4.11 Automatic enrolment occurs when an employee commences with a new employer and they have an eight week window of opportunity to opt-out of the scheme. Existing employees and other savers (self-employed, beneficiaries etc) may elect to join KiwiSaver. The default contribution is four per cent of gross salary or wages but a contributor may elect to contribute eight per cent. A default KiwiSaver scheme is selected if the contributor does not choose their own KiwiSaver scheme.
- 4.12 The scheme involves employee, employer and government contributions. From 1 July 2008 employers will be required to contribute to the scheme for all employees participating in KiwiSaver.
- 4.13 There will be a three year transitional period of rising contributions starting at one per cent of an employee's gross salary and rising to four per cent by 1 April 2011. The employer does not have to make a contribution if an employee earns less than NZ\$26 000. At earnings exceeding NZ\$26 000 the employer matches the employee's contribution up to NZ\$20 per week. The scheme also provides tax credits to employees for their matched contributions to an employee's fund which reduces the cost of the scheme on the employer.
- 4.14 The scheme provides generous incentives – most focussed on creating a savings ethos and retaining people (and thus skills) in New Zealand. For example, the KiwiSaver scheme provides a \$1 000 savings bonus for new members and an annual fee subsidy. It also includes the ability to withdraw fund contributions for the purchase of a first home and provides

a deposit subsidy of up to \$5 000 per member. Another feature is the ability of contributors to take a 'savings holiday' for a period of up to five years, after a minimum of 12 months of contributions.

- 4.15 The scheme is expected to be taken-up by around fifty percent of the labour force by 2017. Very early feedback on the scheme indicated that a number of large employers were choosing to offer joint-contributions before the 1 July 2008 compulsory deadline.

Australia-New Zealand retirement savings portability

- 4.16 Whilst the New Zealand and Australian Governments wish to retain their skilled labour forces it is also recognised that a 'labour swill', where skilled workers move between economies, is a global phenomena.
- 4.17 As Australia and New Zealand share common bonds, trans-Tasman labour movements are expected to increase over the coming decades. Given this, the portability of superannuation between the economies is a growing issue, particularly as Australia has a compulsory superannuation system. This issue is likely to exacerbate with the commencement of New Zealand's KiwiSaver scheme.
- 4.18 In January 2007 the Australian and New Zealand Governments agreed to establish a retirement savings working group to consider the issue of portability of retirement savings across the Tasman.
- 4.19 The Australian Superannuation Guarantee Scheme is based on the principle of preservation until retirement age. Whilst KiwiSaver primarily follows the same preservation principles it allows a one-off early access to retirement savings for first home purchase.
- 4.20 In February 2008 the Australian Treasurer and the New Zealand Minister of Finance will meet for further discussions on this issue.

The New Zealand manufacturing sector

Current state

- 4.21 At the time of the delegation's visit to New Zealand the House Economics Committee was in the final stages of the inquiry into the state of Australia's manufacturing sector.⁹ The delegation was therefore interested

⁹ The report, *Australian Manufacturing: today and tomorrow*, was tabled on 13 August 2007.

to discuss the state-of-play in New Zealand's manufacturing sector, future directions and the current manufacturing strategy.

- 4.22 The New Zealand manufacturing sector has never been large. Its top five exports are dominated by primary industry products as can be seen in Table 4.1. These are dairy; meat; horticulture; forestry and tourism. Food and live animals account for more than half of all exports.¹⁰ Leading manufacturing sectors are food processing, wood and paper products, and metal fabrication.
- 4.23 New Zealand has not been strong at transforming primary exports into higher-value products and as such net exports comprise a similar proportion of GDP as they did in the 1980s. That said, if meat and dairy products are included in the figure, manufacturing accounts for a significant 63 per cent of New Zealand's exports.¹¹
- 4.24 The sector is growing, yet not as fast as other sectors. In line with this trend the share of manufacturing employment in New Zealand has been reasonably static, at around 14 per cent over the last ten years. However, the proportion of elaborately transformed manufactures has grown significantly—in 2005 they comprised 32 per cent of New Zealand's exports, up from 19.3 per cent in 1990.¹²
- 4.25 Australia is New Zealand's number one trading partner with approximately 21 per cent of its exports going to Australia.

10 Statistics New Zealand, *Overseas merchandise trade*, Cat 53.900 Set 06/07 – 126, 26 February 2007.

11 New Zealand Trade and Enterprise, *Manufacturing +: A Vision for World Leading New Zealand Manufacturers – A Strategic Framework Shortform Report*, November 2006, p. 1.

12 New Zealand Trade and Enterprise, *Manufacturing+: A Vision for World Leading New Zealand Manufacturers – A Strategic Framework Shortform Report*, November 2006, p. 1.

Table 4.1 New Zealand exports—Top 15 commodities year ended May 2007

Commodity	NZ\$ million
Milk powder, butter and cheese	5 669
Meat and edible offal	4 426
Logs, wood and wood articles	1 932
Mechanical machinery, equipment	1 776
Aluminium and aluminium articles	1 213
Fruit	1 184
Fish, crustaceans and molluscs	1 149
Electrical machinery and equipment	1 103
Iron and steel	713
Wool	681
Textiles and textile articles	651
Casein and caseinates	645
Beverages, spirits and vinegar	640
Miscellaneous edible preparations	612
Wood pulp and waste paper	503

Source Statistics New Zealand

Future directions

- 4.26 New Zealand manufacturing faces many of the opportunities and challenges that Australian manufacturing faces. These include distance from European markets (yet proximity to Asia); expanded entry into global supply chains and/or off-shoring production; having innovative and niche products; and improving management skills and business operations.
- 4.27 Most manufacturers in New Zealand are small manufacturers. Out of 20 000 manufacturing enterprises, only 353 firms employ more than 100 staff. Seventy per cent of New Zealand manufacturers have fewer than five staff.
- 4.28 The delegation heard that the future of New Zealand's manufacturing sector, much like that of Australia, lies in design excellence and innovation strengths. The service side of manufacturing is also a largely untapped area of expansion.
- 4.29 Off-shoring of production is occurring in products that can be produced cheaper where labour costs are lower. 'Ice-breaker' and 'Pumpkin Patch' are two niche clothing brands where the design and research and

development is occurring in New Zealand but production is taking place in China. China is able to offer access to high quality production factories and plants located next to competitors who have the same freight costs.

- 4.30 As New Zealand has a small domestic market, much smaller than Australia's, it appears that some manufacturers are off-shoring not only for labour cost reasons but also to increase scale of production and to be closer to the large markets.¹³ For example, Fisher and Paykel, an iconic New Zealand brand, has recently established its parts plant in the US. Having lower transport costs outweighs the higher US labour costs for bulky goods.
- 4.31 However, producing off-shore is not always a successful strategy. Some manufacturers have brought production back to New Zealand because they want the design and production in the same place. There have been problems experienced by some manufacturers putting a business on Chinese soil; mostly associated with ownership or tenancy rights. Problems have also been reported in using Chinese manufacturers to produce goods, including quality and safety issues.

Government industry policy

- 4.32 The New Zealand Government is focussing on making the New Zealand economy a stronger global participant with firms and industries being more flexible and creative. The key to this strategy is investment in science and technology and acquiring and retaining knowledge and skills in New Zealand.
- 4.33 Being an economy with a strong primary industry focus future prosperity will be enhanced by providing more value-add at every level of production transformation.
- 4.34 The food and beverage sector is considered an important part of New Zealand's manufacturing sector. As such, the New Zealand Government has concentrated efforts in improving the competitiveness of industries in the food and beverage sector, including capability building and market development.
- 4.35 In November 2006 a group comprising industry, Government, unions and academia, the "Manufacturing+ Vision Group" (the Group), assessed the state of the New Zealand export manufacturing sector.

13 New Zealand's population is approximately 4.2 million; Australia's population is around 21 million.

- 4.36 The Group consulted with over 500 New Zealanders with manufacturing interests, assessing the global trends impacting the sector and how manufacturers were adapting to these trends. The project culminated in a report entitled *Manufacturing+: A Vision for World Leading New Zealand Manufacturers*. The report details the results of their findings; trends impacting New Zealand manufacturers; a model of best practice for manufacturers; and a set of recommendations for government policy, industry, trade associations and unions, education and research providers.¹⁴
- 4.37 The *Manufacturing+* report recommendations are contained in a quadrant of areas designed to transform the sector. These include:
- improving manufacturing capability;
 - improving manufacturing capacity;
 - improving the sector's profile; and
 - ensuring ongoing engagement of the manufacturing sector with Government.
- 4.38 The work of the Manufacturing+ Vision Group commenced in August 2005 and by the conclusion of the report key Government agencies were already working on the recommendations to improve manufacturing capabilities.

Housing affordability

- 4.39 New Zealand's housing boom has led to a doubling of house prices since 2002 and accordingly, rents have increased. Home ownership has also consistently declined over the past decade. There are many reasons why housing affordability has declined in New Zealand. It is a multifactorial issue.
- 4.40 Investor activity has been significant in the housing market, possibly because real estate is the culturally favoured investment option in New Zealand, but also because it has a privileged tax position.
- 4.41 Both the New Zealand and Australian tax systems are unique in having the ability to deduct losses on rental property. Both countries have capital gains tax on the sale of property, however in New Zealand, capital gains
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14 New Zealand Trade and Enterprise, *Manufacturing+: A Vision for World Leading New Zealand Manufacturers – A Strategic Framework Shortform Report*, November 2006, p. 3.

only accrue on the sale of a property if the original *intention* was to make a capital gain. The same capital gains tax framework applies to financial assets but these can not be negatively geared.

- 4.42 A demographic contributor to falling household affordability is the smaller size of households, and, like Australia, a rising and significant proportion of single households. There has also been significant net migration to New Zealand between the late 1990s and early 2000s which add to housing demand.
- 4.43 In addition to increasing real household income since the early 1990s, the deregulation of the financial market led to household's ability to borrow more for housing.
- 4.44 There have also been issues affecting the supply of housing in New Zealand including land availability, planning regulations and construction prices.¹⁵

House of Representatives Commerce Committee—inquiry into housing affordability

- 4.45 The New Zealand House of Representatives Commerce Select Committee is currently inquiring into the cost of housing in New Zealand. The committee's focus is on home ownership rather than broad housing affordability and the terms of reference specifically address first home buyers.
- 4.46 The terms of reference are to identify all components of the cost of housing for first home buyers in New Zealand and examine significant shifts over time.

15 The Reserve Bank of New Zealand, *Submission to the Commerce Committee on the Inquiry into Housing Affordability in New Zealand*, 14 June 2007, website viewed 14 August 2007, <<http://www.parliament.nz/enNZ/SC/Papers/Evidence/9/5/b/95bb598c361c4c4ba98f4f19f8140341.htm>>.

The terms of reference request particular attention is given to a detailed list of housing affordability factors, including:

- the effect on land supply, and therefore the price for land, of both
 - ⇒ restraints on land supply for new housing, and
 - ⇒ land 'wastage' through 'large section only' subdivisions.
- household ability to service debt, meet costs of ownership and the changing relationship between income, property prices and mortgage interest rates;
- impact of increasing demand for residential properties by investors;
- local authority planning and approval processes;
- charges and levies imposed at all stages of the housing supply chain;
- building material and building labour costs as compared with those in other similar economies and countries;
- access to finance for house building on multiply owned land;
- impact of changing preferences for home ownership;
- range of financing products available for first home owners.¹⁶

4.47 The inquiry is also to consider ways to improve the affordability of housing and to identify intervention programs to help individuals and families purchase a home. The terms of reference specifically seek input on 'shared equity', 'rent to buy' and 'sell and build state housing stock' strategies.

4.48 The inquiry commenced on 1 March 2007. As at 16 August 2007 the committee had authorised 41 submissions from a variety of interested parties including, amongst others, the building industry; community housing organisations; local government; the banking sector; unions; and the Reserve Bank of New Zealand.

Kiwi Bank

4.49 The delegation met with senior executives of the New Zealand Post Group, New Zealand's corporatised postal entity group, to discuss the

16 Web site viewed 24 August 2007, < <http://www.parliament.nz/en-NZ/SC/Papers/Summaries/3/f/0/3f0489134bc54372b31c7c9d8d129140.htm>>.

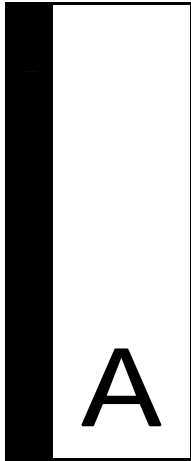
changes to the group's structure and the new wholly owned subsidiary enterprise, Kiwi Bank.

- 4.50 Kiwi Bank was established in 2002 to meet a niche that had developed in the New Zealand banking market.¹⁷ The rationale for the bank was that there was a gap in the market for people who wanted more community style banking and a bank that kept retail network hours.
- 4.51 In some New Zealand towns Kiwi Bank returned a face-to-face banking presence. Kiwi Bank reports that in some regions around fifty per cent of the population now banks with them. The bank's branches were initially located in post offices. Kiwi Bank now has an extensive network of around 300 automatic teller machines.
- 4.52 The three large banks in New Zealand are Australian owned banks—the NAB, Westpac and the ANZ. Kiwi Bank provides direct competition to these banks. Many initiatives developed by Kiwi Bank over the last five years have been followed by the major banks.¹⁸
- 4.53 The New Zealand Government provided NZ\$60 million in 2002 to help establish Kiwi Bank. In 2007 it has a customer base of around 5 000 with a NZ\$3.5 billion balance sheet. The New Zealand Post Group pays dividends to the Government.
- 4.54 By being innovative Kiwi Bank caters for the rural market but also to low and fixed income customers. Low income customers are most prone to receive late fees and default fees. Kiwi Bank has concentrated on educating customers about these issues and on interacting with customers through mobile phone text messages. For example, customers are advised by text message if a direct pay is due to be taken out of an account to avoid penalty fees.
- 4.55 To date the Kiwi Bank initiative has proven there is demand for a 'no-frills' bank in New Zealand. It has been a successful subsidiary venture of the New Zealand Post Group.

The Hon Bruce Baird MP
Chair
13 September 2007

17 Kiwi Bank website <<http://www.kiwibank.co.nz/about/>>.

18 For example no fees on children's accounts; low credit card charges; opening branches again.



Appendix A: Program

Sunday, 15 July 2007

Depart Australia

Arrive Auckland International Airport

8.00pm Informal delegation dinner at Orbit Restaurant, Sky Tower, with Dr Wayne Mapp, MP for North Shore

Monday, 16 July 2007

9.30am Delegation meeting

10.00am Meeting with the Hon Jim McLay ONZM, QSO, Executive Chairman of Macquarie Bank NZ, member of the Australia - New Zealand Leadership Forum, former Deputy Prime Minister and Cabinet Minister

11.20am Visit to Kelly Tarlton's Antarctic Encounter

Arrive Wellington

4.15pm Meeting with Mr David Skilling, Chief Executive, The New Zealand Institute – presentation on the trans-Tasman relationship

7.30pm Attend dinner at the residence of the Australian High Commissioner to New Zealand, His Excellency Mr John Dauth, with embassy staff, guests of Mr Dauth and New Zealand parliamentarians

Tuesday, 17 July 2007

- 9.00am Meetings with the Reserve Bank of New Zealand:
- Mr Grant Spencer, Deputy Governor of the Reserve Bank and Head of Financial Stability Department
- Mr James Twaddle, Manager, Financial Systems Policy
- Mr Michael Reddell, Special Advisor, Economics Department
- 10.45am Meeting with Mr Mark Weldon, Chief Executive Officer, New Zealand Stock Exchange
- 11.45am Combined meeting with the Inland Revenue Department, Ministry of Social Development and the Ministry of Economic Development on 'KiwiSaver'
- Meet with:
- Mr Michael Nutsford, Policy Manager, Inland Revenue Department
- Mr Geoff Rashbrooke, Principal Analyst, Ministry of Social Development
- Mr Jivan Grewal, Ministry of Economic Development
- Mr Laurence Tyler, Ministry of Economic Development
- Mr Peter Martin, Director, The Treasury
- Ms Siân Roguski, Senior Analyst, The Treasury
- 12.30pm Attend informal buffet luncheon as guests of honour of the New Zealand Australian Parliamentary Friendship Group, hosted by Dr the Hon Lockwood Smith MP
- 2.00pm Delegation is introduced to the House of Representatives and observe Question Time.
- 2.50pm Meeting with Dr Brent Layton, Director, New Zealand Institute of Economic Research
- 4.00pm Meeting with NZ Post Group Limited:
- Mr John Allen, Chief Executive, NZ Post Group
- Rt Hon Jim Bolger, ONZ, Chair, Kiwi Bank
- Mr Paul Brock, Acting Chief Executive Officer, Kiwi Bank

Wednesday, 18 July 2007

- 9.15am Call on the Honourable Margaret Wilson MP, Speaker of the House of Representatives of New Zealand
- 10.00am Meet with and observe Finance and Expenditure Committee (FEC)
Chair: Mr Shane Jones, MP
- 11.30am Tour of Te Papa Tongarewa, Museum of New Zealand, with members of the FEC, hosted by Dr Seddon Bennington, Chief Executive
- 12.30pm Luncheon at Te Papa Museum
- 2.00pm Combined meeting with Ministry of Economic Development and New Zealand Trade and Enterprise to discuss 'Manufacturing Plus' Strategy
Meet with:
Ms Kathe Huse, Senior Analyst, Ministry of Economic Development
Ms Phillipa Sanderson, Sector Manager, New Zealand Trade and Enterprise
- 3.30pm Call on Mr Phil Heatley MP, Opposition Spokesperson on Housing
- 4.30pm Call on the Honourable Mr Bill English MP, Deputy Leader of the Opposition and Opposition Spokesperson on Finance
- 7.00pm Attend dinner at the New Zealand parliament as Guests of Honour of the Honourable Margaret Wilson MP, Speaker of the House of Representatives

Thursday, 19 July 2007

- 9.30am Attend briefing on e-Committee with Ms Catherine Parkin, Senior Parliamentary Officer
- 10.00am Attend and observe Commerce Select Committee
Chair: Mr Gerry Brownlee MP
- 1.30pm Depart Wellington