

Hon Bill English  
Minister of Finance  
Parliament Buildings  
WELLINGTON

Dear Bill

### **Value for Money and Budget 2009: Vote Economic Development**

This letter provides you with my advice on improving value for money within Vote Economic Development.

The Ministry of Economic Development has now completed its "line-by-line" expenditure review of Vote Economic Development. This involved considering each output class (and in many cases sub-outputs) against the criteria provided in the Cabinet paper on the value for money exercise, and agreement with me was reached on which outputs were low value or discretionary activities, and which were activities inconsistent with Government priorities.

This review included government funding being paid to, or through Crown entities within the Vote (i.e. New Zealand Trade and Enterprise [NZTE] and the New Zealand Venture Investment Fund Ltd).

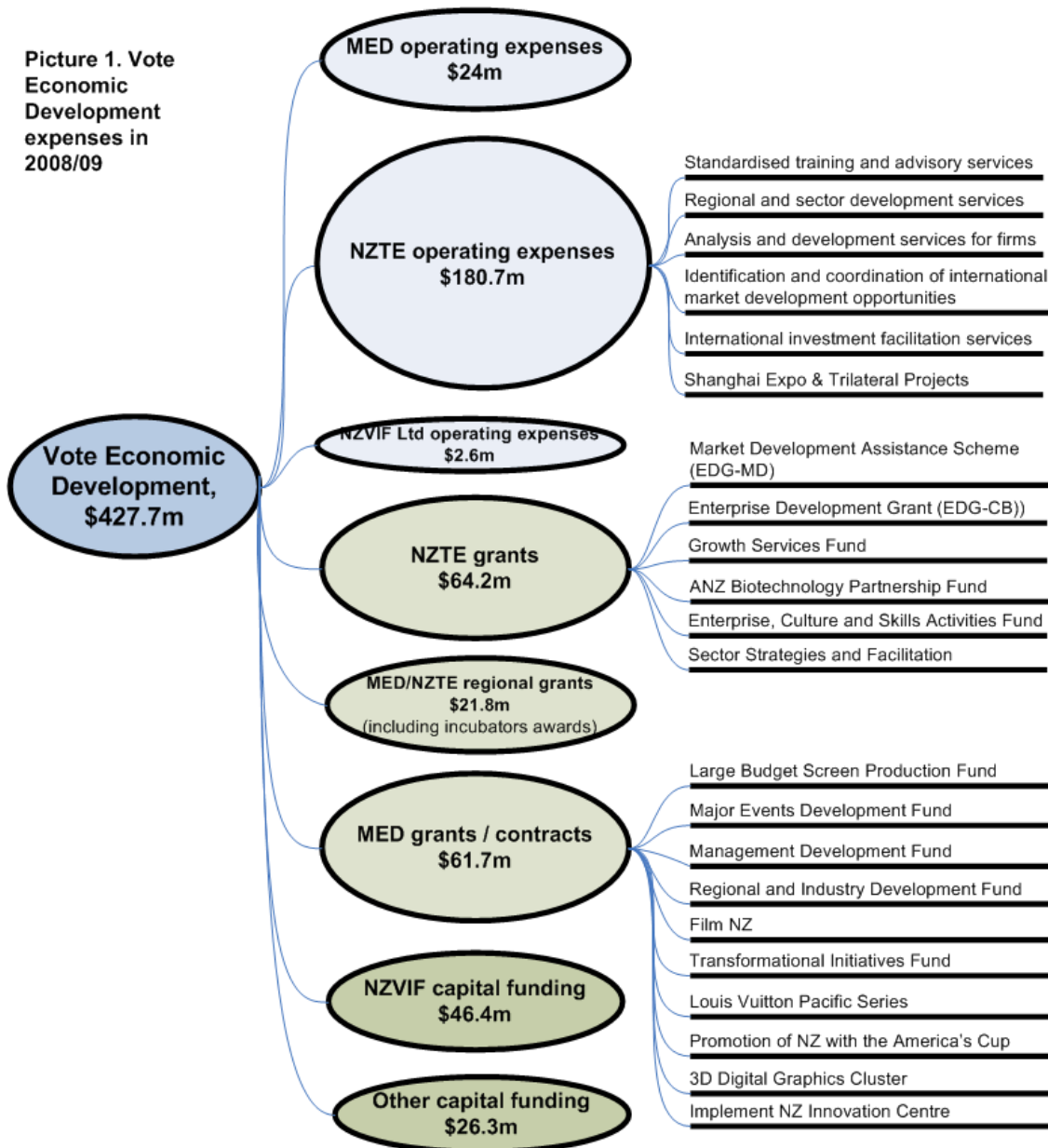
To ensure all savings were captured, the Ministry of Economic Development also undertook a separate value for money review of departmental outputs with a view to identifying further savings across all activities within MED - not just those low priority ones identified through the line-by-line process. This includes corporate support services for the Ministry. Some of the savings identified through this exercise fall under Vote Economic Development and have therefore been incorporated into the savings for the Vote. Further detail on this review is contained in the covering letter from myself, and the Chief Executive of the Ministry of Economic Development, on the Ministry and how it undertook the Value for Money exercise.

The Ministry also wrote to Crown entity chief executives, asking them to undertake a similar exercise for the Ministry in assessing the cost effectiveness of their activities, and identifying savings that could be freed up. NZTE has been able to make savings of \$8m of operating expenses in 2008/09, which has been included in the total savings for this Vote. In relation to NZTE operational savings for 2009/10 and out-years, these are reflected in the Cabinet paper: Reversing Unfunded Budget Commitments for ET: Innovation, or within this value for money exercise. Allowance has been made in 2009/10 for up to \$2.5m of transition costs (project costs and redundancies), as NZTE re-focuses its activities on a smaller number of high potential firms and operationalises the results of this exercise. If all of this funding is not required, it will be possible to return further savings to the Crown.

Besides the value for money exercise, the development of a broader view on what government wants to do with business assistance programmes, including how much it wants to spend, and who it wants to deliver them, will be part of the review of Business Assistance. I have instructed my officials to work

closely with the Department of the Prime Minister and Cabinet and the Treasury in framing up and progressing this review.

## Overview of the Economic Development Vote



Vote Economic Development is primarily used to deliver services and grants to firms. Success is measured through the extent to which such firms grow (internationalise, up-skill, increase profits and investment, increase productivity) and pass on benefits to the wider economy.

In addition, because Vote Economic Development is the ownership Vote, departmental capital injections for the Ministry of Economic Development are made via this Vote.

Appropriations for Vote Economic Development within the baseline are \$355.0m for 2008/09, \$351.4m for 2009/10, \$324.8m for 2010/11, \$310.7m in 2011/12 (note these figures do not include capital)<sup>1</sup>.

Many of the line items in the Vote have been evaluated through an independent and rigorous process. This includes evaluations of specific funds and services as well as an expenditure review of business assistance. Many of the evaluations are subject to independent peer review. Significant institutional and policy changes have resulted, and in some instances, non-performing programmes have been disestablished. The body of evaluation information has helped the value for money analysis.

More recently, MED's evaluation of the Growth Services Fund shows a net positive return (i.e. the specific benefits to business and the economy exceed the cost of assistance provided, based on very robust analysis). Evaluations are also underway of the Venture Investment Fund, NZTE's standardised training and advisory services output class, Kea New Zealand, and the Buy Kiwi Made campaign. A report on the evaluations will be provided, and discussed with me, when they are completed.

## Proposed savings

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The following table outlines potential savings within Vote Economic Development for 2008/09, 09/10, 10/11, 11/12, at the output class level. More detail on where savings are coming from and why, and why savings may not have been offered in relation to some output classes is contained in the detailed line by line excel spread sheet attached as appendix one to this letter.

<b>Vote Economic Development: Output Class</b>	<b>2008/09 Savings</b>	<b>2009/10 Savings</b>	<b>2010/2011 Savings</b>	<b>2011/2012 Savings</b>
Standardised Training and Advisory Services	0.5m	0.50m	0.50m	0.50m
Regional and Sector Development Services	-	0.30m	2.30m	2.30m
Analysis and Development Services to Firms	3.0m	-	1.75m	1.75m
International Investment Facilitation Services	-	2.00m	1.90m	2.10m
Investment Fund Management		0.26m	0.26m	0.26m
Market Development Assistance Fund and Enterprise Development Fund	-	10.00m	30.40m	30.40m

<sup>1</sup> These figures include money that will be transferred in the March Baseline Update and the estimated spread of Multi-Year appropriations between years.

International Biotechnology Partnerships	2.00m	-	-	-
Enterprise, Culture and Skills Technology Fund	-	1.5m	1.5m	1.5m
Regional Partnerships and Facilitation	10.45m	0.8m	3.45m	3.45m
Management Development Fund	0.58m	-	-	-
Regional and Industry Development Fund	0.26m	-	-	-
Implement NZ Innovation Centre	-	1.20m	1.20m	1.20m
Policy Advice: Small Business	0.12m	0.13m	0.13m	0.13m
Policy Advice: Sectoral Leadership	3.39m	1.51m	1.51m	1.51m
General NZTE operating savings	8.00m	-	-	-
Loan to NZ Innovation Centre (capital)	4.00m	3.00m	3.00m	-
<b>Total Savings</b>	<b>32.30m</b>	<b>21.21m</b>	<b>47.90m</b>	<b>45.10m</b>

In addition to these savings, Vote Economic Development has also offered savings in the Cabinet paper: Reversing Unfunded Budget 2008 Commitments for ET: Innovation. These savings are outlined in the table below.

<b>Vote Economic Development: Output Class</b>	<b>2008/09 Savings</b>	<b>2009/10 Savings</b>	<b>2010/2011 Savings</b>	<b>2011/2012 Savings</b>
Regional and Sector Development Services	-	2.80m	4.20m	5.20m
Identification and Coordination of International Market Development Opportunities	-	0.70m	1.50m	1.70m
International Investment Facilitation Services	-	-	1.10m	0.90m
Major Events Development Fund	-	0.2m	0.2m	0.2m
<b>Total</b>		<b>3.70m</b>	<b>7.00m</b>	<b>8.00m</b>

This makes total savings within the Vote of:

	2008/09	2009/10	2010/11	2011/12
Savings in Value for Money	32.30m	21.21m	47.90m	45.10m
Savings in Unfunded Budget 2008 Commitments for ET.		3.70m	7.00m	8.00m
<b>Total Savings within the Vote</b>	<b>32.30m</b>	<b>24.91m</b>	<b>54.90m</b>	<b>53.10m</b>
<b>Percentage of savings within the Vote (these percentages are based on appropriations and do not include capital or capital savings).</b>	<b>7.97%</b>	<b>6.24%</b>	<b>15.98%</b>	<b>17.09%</b>

It is worth noting that a significant amount of savings/re-prioritisation has also already occurred within Vote Economic Development in the 2008/09 financial year to support a range of government priorities. This re-prioritisation includes \$16m from NZTE grants, and \$0.75m from NZTE marketing and communications, \$3m from non-departmental output expenses other and \$1m from MED baselines.

## Expense Transfers

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I am also seeking the following expense transfers within the Vote (the reasons for the transfer and the risks if the transfer does not occur are discussed in Appendix 2 to this report), which I would like to action these through the March Baseline Update:

- A transfer within Vote Economic Development: Departmental Expense: Policy Advice of up to \$0.5m from 08/09 to 09/10 for work on Rugby World Cup 2011;
- A transfer of \$0.6m from 08/09 from Vote Economic Development: Departmental Policy Advice to Vote Commerce Policy Advice in 09/10 for work on Government Procurement, contingent to Cabinet agreeing to the Government Procurement Review;
- A transfer from within Vote Economic Development: Non-Departmental Output Expense: Regional and Sector Development Services of \$0.650m from 08/09 to 09/10 for the Food and Beverage Taskforce; and
- A transfer from within Vote Economic Development: Other Expense: Regional Partnerships and Facilitation of \$3.5m from 08/09 to 09/10 for the Regional Strategy Fund.

## Discussion of some of the Critical Outputs in the Vote and Scope for Further Savings beyond this Value for Money Exercise

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### *Policy advice*

A total of \$1.63m in 2009/10 and out-years (a savings of 9.6%) has been found within the MED policy advice part of the Vote. These savings are a result of reductions in travel, consultancy, support costs and overheads and giving up current vacancies within the Vote. Also included are savings from removing the Growth and Innovation Advisory Board. This is the amount MED believes can be offered up as savings without compromising on delivery of the Government's priorities, or putting key service delivery outputs at risk.

### *Improving business support programmes*

We have said that we want to see a rise in exports from around 30% of GDP to 40% and income parity with Australia by 2025. Meeting these goals requires a strong and resilient domestic economy and New Zealand firms that prosper internationally. Well-targeted and packaged Government support for New Zealand businesses will contribute to this goal.

The immediate goal is to consolidate and focus business support on those initiatives which are of most value to New Zealand firms and deliver greatest economic benefit. This requires an overhaul of our current business support programmes. This has assumed greater importance because of the economic crisis. Success will be demonstrated by effective support to business through the crisis and, in the longer term, improved productivity and more internationally competitive businesses.

I am using the current value for money exercise to drive the necessary changes to existing programmes, and further work will also be undertaken through the review of Business Assistance or other reviews/evaluations undertaken by the Ministry and other agencies. In some of the areas we have not offered savings until there is a review, some of the key areas are discussed below.

The original policy objectives for Management Capability Training were to develop the market for private provision of foundation management capability training. This objective has largely been achieved with organisations such as Economic Development Agencies, Chambers of Commerce, the New Zealand Institute of Management, Employers Manufacturing Association, and others now providing effective services on foundational practices. Additionally, providers currently contracted by NZTE to deliver Enterprise Training (Gosling Chapman and other training consultants) are also meeting demands of the business sector in this arena.

The Output Class this training is in is currently the subject of an evaluation which will provide valuable information on the effectiveness of the current services provided.

I believe some work needs to be undertaken to determine who is best able to deliver these services going forward. Any work would need to consider who is best placed to provide what services, and what costs may be involved to business (the current services are free). Any such review should be part of the Review of Business Assistance.

I have not, however, suggested any savings in 2009/10 and out-years for two reasons. First, some of small business package of initiatives in relation to the economic recession leverage off the existing programmes which makes it difficult to change these programmes in the short-term. Second, if a decision is made to move some of these services it will take some time to negotiate transition and price with any new providers.

MED and NZTE have reviewed NZTE's strategy for supporting exporting New Zealand firms. NZTE, in consultation with New Zealand firms operating in international markets, have determined that in order to improve the performance of the economy as a whole it is appropriate to target support on firms that have the realistic potential to achieve international scale and competitiveness. The key outputs for this have been examined as part of the Value for Money exercise.

MED and NZTE consider that NZTE's strategy will result in NZTE engaging more intensively with a smaller number of high potential exporting New Zealand firms, which allows a rationalisation and consolidation of expenditure required to support this approach. Areas where the bulk of the potential for savings have been identified are strategic and sector initiatives, Investment New Zealand, and Grants.

*[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]*

### *Sector Projects and Strategic Initiatives*

Sector Projects and strategic initiatives represent a significant proportion of NZTE's Regional and Sector Development Services output. As noted above, some immediate savings have been identified here. In addition, an evaluation of this activity is planned for 2010, and this could result in more significant savings.

Savings in this area would allow NZTE to focus increasingly on higher impact sectors where New Zealand has a competitive strength, and in particular to support the exporting focus. A more focused approach to sector and strategic initiatives will have flow on consequences to NZTE's activities in areas such as marketing and communications, and savings have also been obtained within these areas as a result.

### *Grants*

There is the potential for significant savings from consolidation and refocusing of the grants programmes administered by NZTE, such as the Market Development Assistance Fund, Enterprise Development Fund, and the Growth Services Fund.

I am proposing that the Market Development Assistance Fund be closed to new applications at the end of 2008/09, but that a further year would be allowed for previous clients to re-apply for grant funding. Allowing a further year for previous clients to reapply would allow the government and NZTE to better manage communications around closure (especially if a new exporting fund is set up, see below) and would enable firms to access money in a year where many firms will be finding it difficult in an economic recession.

NZTE, the Ministry of Economic Development and the Ministry of Foreign Affairs and Trade are also doing some work for myself and the Minister of Trade on the development of a \$30m fund to support firms to undertake a wide range of firm exporting activities, including market development and international management education (this would be more targeted than the current Market Development Assistance Fund). Alongside the range of other NZTE products and services supporting firm exporting, it is intended that a refocused grant fund could contribute to increasing New Zealand business success internationally.

Depending on the outcome of this work, I may seek Cabinet agreement to a re-focused grant or offer up additional savings.

I believe it is important that the Large Budget Screen Production Grant be retained in its current form until an evaluation of the Grant is completed in 2011. I believe this sector is important. Further, the current grant funding levels are based on international comparisons and set at a level that creates the appropriate incentives for film makers to come to New Zealand.

### *Large Project and Regional Economic Development Funding*

As Minister of Economic Development I require the flexibility to be able to fund significant economic development projects which would have spill-over benefits to the rest of the economy and which do

not easily fit with current programmes and services being offered by crown entities (such as NZTE and the Foundation for Research, Science and Technology).

These projects normally require significant cross-government coordination by MED, the commercial skills and networks of NZTE and also robust independent financial and commercial advice.

Such projects are not entered into lightly. Firms must have the potential to generate large overseas benefits for New Zealand, and offer opportunities for other New Zealand firms to integrate their activities with the larger firm (i.e. must deliver significant economic returns to the economy as a whole and not just individual firms).

Currently provision for such projects is made in the Transformational Initiatives Fund (which is a one-off \$9.8m worth of funding), and I think it is important that this Fund is retained. *[information deleted in order to protect the commercial position of the person who supplied the information, or who is the subject of the information.]* Under the criteria of the Fund, you as Minister of Finance are also involved in any decision to provide funding for initiatives.

In addition, it is important that there is the ability for government to assist joint ventures or clusters of firms (often operating regionally) working together where there may be nationally significant economic benefits (particularly in areas of New Zealand's competitive strength) and where these may not occur without some government support and facilitation. *[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials.]*

Currently one of the only ways that such clusters of firms operating regionally can get funding is through the Enterprising Partnerships Fund. Through this contestable fund, the government co-invests in collaborative projects with industry and the regions in the public good aspects of projects that promote knowledge-sharing, facilitate innovation and international connections.

The Enterprising Partnerships Fund (EPF) has operated for one year so it is difficult to assess its impact. Past experience with joint regional-government major projects has resulted in variable economic impact. I am offering up \$10.45m in savings from this Fund in 2008/09, as there are no projects which are sufficiently advanced to warrant funding in this financial year. I am also asking my officials to review this Fund and to provide me with advice on whether this Fund should be re-focused to better align with government priorities or whether further savings should be given up. Any such review would also need to be linked into the Review of Business Assistance.

In addition, I am recommending that the Regional Strategy Fund cease from 2010. Each of the 14 regions currently get \$750,000 over each 3 year period.<sup>2</sup> This fund supports regions to plan for, action, monitor and communicate regional economic development strategies.

The current round of funding ceases in 2010. The Regional Strategy Fund appears to have been beneficial, in the sense that regions now appear to have a stronger sense of their economic strengths and priorities. Overall, we are seeing better collaboration between regional stakeholders.

However, we have not evaluated or quantified these benefits, and it is unclear whether ongoing government funding would add significant value for money. Further, we believe that many of the benefits will be realised by 2010, and that there are a range of other services that NZTE and others provide which are delivered regionally that means that we are still providing support to the regions. *[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials.]*

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<sup>2</sup> The Chatham Islands also has \$150,000 available over 3 years



## **Risks and Impacts of the Savings Exercise**

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In some areas the savings relate to scaling back or reductions in funding programmes, rather than any programme closures or significant cut-backs and no publicity will be needed.

However, the proposed reductions/changes to: Management Capability Training, Regional Development Programmes, the Enterprise Culture and Skills Fund, Investment New Zealand, the New Zealand Innovation Centre and the Market Development Assistance Fund will require careful stakeholder management and publicity strategies given the size of the savings and changes.

In the first instance any savings within MED, and NZTE operating which relate to personnel will be found from natural attrition or re-deployment of staff. However, in areas where services are discontinued there may be some redundancies. This makes the phasing of any savings important.

If the expense transfers for the Rugby World Cup 2011 and the Government Procurement Team do not occur, this would compromise MED's ability to effectively carry out the work programmes for the Rugby World Cup or the Government Procurement review. *[information deleted in order to maintain the effective conduct of public affairs through the free and frank expression of officials.]*

I look forward to discussing the results of this exercise with you.

Kind Regards

Hon Gerry Brownlee  
**Minster for Economic Development**

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