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What has caused the collapse of savings since 1987?

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1. Introduction

The Treasury discussion document *Saving in New Zealand – Issues and Options* is, in my opinion, a short-sighted document that fails to address the real economic issues facing ordinary New Zealanders. It is long on rhetoric and lacks any meaningful information, other than unreliable statistical data, about what has happened within the New Zealand economy, since the 1984 Labour Government.

2. The historical problem facing savers within New Zealand

The basis of every economic ill that currently plagues New Zealand is two-fold. The first is, we are, and remain, a low wage economy, the second is that investment and thus savings vehicles, have a history of unreliability and for the most part are inconsistent in their performance.

The most significant, and most destructive economic event encountered in recent times, was the 1987 stock market crash. Until this event, the average saver and investor considered the stock market to be reasonably sound, although most New Zealanders had a relatively poor grasp of the technical issues. The crash, a wholly contrived event, undermined public confidence in the stock market to such an extent that this market has been largely left to the institutional investors. This collapse has, in the opinion of the author, been a principle driver of private property purchases, as opposed to other forms of investment. Even today, some 23 years later, the average member of the public who experienced the crash, still vividly remembers the chaos it caused.

The current recession, beginning in 2007, has done nothing to restore public confidence in the stock market and has further eroded public confidence in alternative investments, including real estate.

3. Regulatory indifference

Much has been written in both specialist financial and general media forums about the inability of government to tackle the problem of what can only be described as 'self enrichment' by the owners of many of the finance and investment vehicles that have vanished into the hands of receivers, within the past two years. The very foundation of our savings industry has been discovered to be nothing but an illusion. This is not a matter of academic discussion or theoretical modelling, but the stripping of billions of dollars of savings from our economic base. The regulatory indifference to the initial collapses resulting from the current

recession, is nothing short of negligent. Yet again, it has severely undermined public confidence in almost every form of saving, other than the property market.

4. Skewed statistics

Dr Bollard, in his submission to the inquiry, has highlighted the problem of a lack of relevant statistical information upon which to base future planning and policy decisions. Treasury has suggested the need for a wider and more rapid accumulation of data. Given the rising number of offshore sources of capital, especially from Asian investors, this seems unlikely. The Craefar Farms saga illustrates the difficulty of tracing capital investments from countries like China. If New Zealand wishes to attract such large blocks of investment, the investors control the information about the investment, not the vendor. As global economic interdependence has accelerated, the government's ability to monitor and trace the source of funding has declined. Who knows if the latest tranche of investment funds to arrive in New Zealand came from the Colombian or Russian drug cartels? There is almost no way of telling.

As a consultant, I asked a number of clients why they refused to grow their business. In every case they cited compliance costs, GST and the unavailability of reasonably priced capital as the primary reasons. Many of my clients had come from senior management backgrounds and had suffered unemployment as a result of the radical changes brought about by what came to be known as, 'rogernomics'. They were all very competent producers, but given the lack of support, found it impossible to operate on any other level.

Once these clients had adjusted to a new life and business style – away from being corporate executives – they began to realise they only wanted a 'life-style' business. They no longer wanted to participate in corporate New Zealand, and wondered why they had ever done so. At that point many made the decision to become 'invisible' to the authorities. Some kept their earnings sufficiently low so as to avoid GST registration. Others deliberately ran their businesses at a loss. But all showed a high degree of ingenuity in avoiding the worst aspects of GST and compliance costs. All agreed that they would, or intended, to move into the property market where they were largely able to operate tax and compliance cost free. If you re-evaluate the statistics for property purchases and leveraging against dwellings, you will see the structural employment changes caused by the introduction of GST and the decapitating of middle management, closely match the rise in property development.

Essentially, these individuals replaced their corporate remuneration with tax-free returns from property development.

4. Savings. How can we protect them?

Most of us define savings as the surplus we retain after expenses. There are a number of esoteric economic models that add many more factors into the equation, but they are, in my opinion, largely irrelevant. Future earnings, as this inquiry proves, are largely illusory. Who, in 2008, would have predicted such a dramatic decline in the savings of America, other than the traders passing off worthless securities? No one in this inquiry has addressed this vital issue. The only thing that seems to have been contemplated is the increase of savings on a national scale. Savings, by their very definition, suggests something that has been set aside for use in the future. Given the wholesale fraud that has occurred throughout the international securities market, resulting in the destruction of billions of dollars of savings, how can we expect public confidence in any 'savings' scheme?

Given the globalisation of investment markets, no nation can guarantee the savings of its citizens. The Savings and Loans scandals of the Reagan era demonstrated the futility of government guarantees in the face of determined fraudsters. Yes, the depositors were government guaranteed for their deposits, but in turn the depositors were required to guarantee, through tax revenues – the very institutions that defrauded them in the first place!

5. Diversification?

It has long been of concern that New Zealand has failed to diversify its economic base. During the 1970's there was a determined attempt to remove what were considered essential industries. This was as a result of the Industry Development Committee policy (IDC). The motor assembly plants in Petone, Auckland and Nelson were all progressively closed because the motor companies did not want the cost of local assembly to impinge on their New Zealand profit margins. As a result, new vehicles became unreasonably expensive – I remember a new 1982 Mitsubishi 'Chariot', being offered for \$32,000, almost twice the price of a three-bedroom dwelling at that time. Such distortions were common, and I'm sure the reader will have experienced many examples themselves. But the cause of these distortions was a lack of diversification.

Today, we are faced with a massive, and probably incurable, outbreak of disease in the kiwifruit orchards that will inevitably lead to the long-term damage of that industry. This is only one of a number of disasters that have threatened the overall economic survival of New Zealand. I well remember the chaos the supposed outbreak of 'foot and mouth' disease had during 1969(?) when the then Director-General of Agriculture, Sam Jameison, decided to test the farming community's response to such an event. That should have warned us that diversification was essential if we were to survive the economic damage such an event would bring. Yet we still cling to the myth that 'farming is the backbone' of the New Zealand economy. We must embark on a program of diversification as soon as practically possible and if necessary, mobilise Reserve Bank Credit to do so.

6. Comparing apples with oranges?

There have been a number of comparisons made between the New Zealand and Australian economies in the various submissions to this inquiry. In my opinion, it is a serious error to do so. The Australian economy is so different to that of New Zealand, there is no realistic basis for comparison. The State Government system has aspects our economy cannot, or will not, emulate. Australian states openly compete for population and thus development through a number of openly 'hidden' subsidies. Government contracts are usually supplied through Australian companies. Employment opportunities – especially in government - are openly biased towards Australian citizens. The idea that New Zealand will somehow 'catch up' with Australia economically, unless we undertake rapid diversification, is an impossible dream. The only realistic option is for the development of the oil and gas industries and mineral extraction. But in order to do this, significant political change will need to occur beforehand.

7. The politics of change

No change in the savings habits of New Zealand will occur without the consent of the population. Why would any right-thinking person invest in any venture they cannot be reasonably confident will be in existence just a few short years after start-up? Our industry desperately needs the benefit of the cheap capital afforded by the share market investor. But in order for that to occur, there needs to be quality investments. The average member of the public now realises that our economy is too small to withstand the vagaries of the massive international funds trading in our market. The ability to make meaningful savings begins with meaningful,

workable policies. The idea that the 'market' will somehow provide the benefits of a stable investment and savings environment is a dangerous myth.

There is only one strategy open to New Zealand and that is state controlled investment and savings. Kiwibank is one such scheme, but in order for it to survive it needs a cross party agreement that it will remain the property of the New Zealand people in perpetuity. 'Post Office Bonds' is another excellent scheme, but again, there must be a government assurance it will remain in New Zealand control.

8. Welfare issues

It is intrinsically unethical to blame the majority of unemployed for the lack of employment opportunities. This is the sole prerogative of the state and the monetary and economic policies it follows. It is a well documented fact that interest and exchange rate fluctuations directly affect employment opportunities. It is morally bankrupt to apply savings policies, designed in an economic environment that is totally inappropriate for this country.

Given the political upheaval that is occurring across Europe at the present time, the Savings Working Group should look very carefully at how they intend to manage what they euphemistically call 'government savings' (a code word for welfare benefit cuts) when the entire country is suffering significant economic stress. That the OECD and IMF may find our debt ratio to GDP unacceptable, is not the point. If Portugal can survive with debt levels at 350% of GDP, then our debt levels are insignificant!

9. Employment is the key

I am old enough to remember full employment and mothers that stayed at home with the children. I also remember that children's toys were almost unobtainable, post war, yet they were happier times for overall. Savings depends on employment. Investment in employment, especially a comprehensive apprenticeship programme is essential for the long-term development of the New Zealand economy.

A working community is a happy community. A working community is much less likely to be afflicted with the social ills unemployment brings. The savings in crime prevention, and thus social stability, alone makes this a worthwhile policy. We, as a nation, need to return to a course of sustainable economic development that allows for the reasonably managed use of our natural resources in concert with best industrial practices. The Pike River Mine disaster would not have happened had it not been for the unrealistic demand that access to the coal seam was via an underground tunnel. Given the methane risk it should have been an opencast mine. In strictly economic terms, we have lost 29 miners and the proceeds from the export of coal from the mine. Here is another example of unrealistic policies being enforced by a small group of radical eco-marxists, determined to make mineral extraction unrealistically expensive. Or have they been bought and paid for by a competitor?

We have unwisely subscribed to an almost open market policy, when our trading partners refuse to offer us reciprocal benefits. This policy has been unrealistically pursued in the hope local dairy and meat producers will gain access to a greater share of the international markets. Given the rapid rise of dairy and beef production in Argentina and Chile, countries that offer similar climate zones, to those in New Zealand, but at a fraction of the labour cost, how long does the Savings Working Group expect New Zealand to remain a major player in the world dairy and meat markets? It appears to me that what we do well – film-making would be one thing – we refuse to invest in. What we do poorly – wool production for instance – we refuse to cut our losses and continue to invest, directly and indirectly, in a largely unwanted product. We need to

adopt a rapid policy of import substitution as soon as practicable. The Japanese car industry is based on a policy of 60% local consumption and 40% exports. It has served them well over forty years. In fact, it has become such a part of the Japanese way of life, many Japanese buy vehicles to support the national industry, rather than out of necessity for their own transport needs.

The foundation of any savings policy must be the talent and ability of the people forming the productive base of our economic activity. It seems pointless to me to follow a policy of economic stagnation that impels the talent we need to make the savings our economy requires, to move off-shore. As Roger Douglas was reputed to have said; if it takes 5,000 uneconomic farms to be sacrificed in order to save the New Zealand economy, that is a small price to pay. This may have been the truest thing ever said about our economy.

The question the Savings Working Group must address is this; does the economy serve the nation, or the nation serve the economy?