

Reference: 20160227

16 February 2017



OFFICIAL INFORMATION ACT COMPLAINT

I refer to your Official Information Act request received by Treasury on 25 June 2016. Your request was for:

“...copies of any material prepared by The Treasury this year on regional economic performance, particularly in New Zealand. I am particularly interested in any analysis or advice - whether supplied to the Minister or his office, or for use internally - on the economic performance of Auckland relative to the rest of the country (whether cyclically or structurally).”

As you are aware I wrote to you on 12 July 2016 declining your request under the following section of the Official Information Act:

- section 9(2)(f)(iv) – to maintain the current constitutional conventions protecting the confidentiality of advice tendered by Ministers and officials

At the time of your request Treasury was updating its advice and analysis on economic performance, including Auckland's performance, and any implications for government policy. The advice and analysis was to be included in the Treasury's updated strategic documents, including the next Long-Term Fiscal Statement.

Subsequent to my response, you requested that the Office of the Ombudsmen investigate my decision to withhold information covered by your request.

This letter is to advise you that, following the release of our Long-Term Fiscal Statement (He Tirohanga Mokopuna), I have revisited my decision and am now able to release the relevant material to you.

Information Being Released

Please find enclosed the following documents:

Item	Date	Document Description	Decision
1.	25 May 2016	Covering note:Te Miro regional forum (final)	Release in full
2.	25 May 2016	Background paper: Te Miro regional forum (Final)	Release in full
3.	3 June 2016	Slide pack for forum: Te Miro regional forum (Final)	Release in full

We intend to send a copy of this reply letter and release material to the Ombudsman.

Please note that this letter (with your personal details removed) and enclosed documents may be published on the Treasury website.

This fully covers the information you requested. You have the right to ask the Ombudsman to investigate and review my decision.

Yours sincerely

Matthew Gilbert
Manager Economic Performance & Strategy/Regulatory Quality Team



Information for Release

1.	<u>Covering note Te Miro regional forum (Final)</u>	1
2.	<u>Background paper Te Miro regional forum (Final)</u>	4
3.	<u>Slide pack for forum Te Miro regional forum (Final)</u>	18

Covering note for Te Miro Forum:

Taking a local view: Economic Performance & Living Standards

Purpose of this Forum

1. The regional variation in living standards across New Zealand is one of several significant issues where Treasury needs a clearer position in our refreshed narrative. Beyond recognising this variation, we should aim to provide a Treasury view on when/whether it is appropriate for government to contribute to economic development initiatives in specific communities to raise living standards, and how they could do so.
2. There is a further pragmatic reason for reviewing our position: we think governments are increasingly likely to intervene, so even if a regional economic development approach is not our first best advice, we still need to be able to support them to implement their policies in a way that minimises risks and trade-offs.
3. The ELT is looking for our advice on these issues to inform a conversation in July. ELT is looking for a view on regional economies that supports our strategic intentions, takes a living standards approach, and reflects our increasing focus on investment to minimise future liabilities. This Forum and subsequent ELT discussion will feed into the narrative refresh project.
4. A successful outcome of this Forum would be a broad agreement that, while not a prima facie justification, significant spatial differences in economic performance may suggest potential for government economic interventions to raise living standards. We recommend adopting a set of principles around when and how spatial interventions may support economic and social inclusion objectives.
5. We have tested/explored the ideas here via the Treasury Board, the Narrative Prosperity Group, regional stakeholder workshops, the Analyst Forum, and a Principal Adviser discussion. Our thinking has been informed by cross-agency discussions, with MBIE and MPI in particular. We have also taken advice from NZIER and other external experts. A further Te Kohao Committee may be useful after the Forum.

Issues for the Forum

Strategic framing and choices [slides 1 – 8]

6. Economic performance varies markedly across and within regions (eg regional GDP per capita, average/median incomes, employment levels). Choice of spatial unit makes a big difference in this analysis, since different spatial levels tell different stories.
7. Prima facie, regional variation does not indicate a “problem”, or provide a case for spatial economic intervention, since the industrial composition of regional economies influences average incomes and regional GDP. And other positive local factors can offset lower incomes (such as cheaper housing).
8. However, regions that show...
 - high and persistent unemployment;
 - high and persistent levels of deprivation; and
 - low productivity in sectors that should be strong...

could be subject to place-specific factors (government or market failures) that are barriers to raising living standards (also driving fiscal costs such as welfare liability, and opportunity cost of lost output).

9. Some New Zealand sub-regions do appear to show these characteristics with associated implications for the living standards of those populations, especially Māori.¹
10. In simple terms, and given our intentions and economic context, the Treasury faces strategic choices either to:
 - a) adopt a (more) active approach to reallocate people and mobile resources out of poorly performing areas to more prosperous areas [is this practical on a large scale? what about people's attachment and connections to places and communities?]
 - b) rely primarily on social development policies to raise living standards and adopt a "laissez-faire" economic approach [is this enough to raise living standards where employment opportunities are scarce, and there is path dependence?]
 - c) consider policies to raise economic performance in poorly performing areas in tandem with social development policies (an extension of social investment) [can governments do useful things to encourage higher performance and at what cost?]

Discussion point: Does the Treasury agree with this strategic choice framing, and which option will best support higher living standards? Is it better to think about a policy framework that combines all three strategic responses?

Principles for intervention [slides 9-11]

11. Regional economic development policy poses unique challenges, including the need to avoid: displacing activity, leaning against efficient forces of agglomeration, and delaying inevitable adjustments.
12. Drawing on OECD research and advice we suggest these principles for central government involvement in regional economic development:
 - a) evidence of spatial market or government failures that are resulting in under-utilisation of local or regional skills or other assets (viable comparative advantage), with associated deprivation;
 - b) interventions should primarily leverage private capital, to reduce cost/risk to taxpayers. Where public funding is sought (eg for infrastructure), proposals should demonstrate investment-readiness through an appropriate business case or equivalent. Business cases should take a living standards perspective that gives weight to the social inclusion benefits of an investment;
 - c) leadership and commitment by local stakeholders and private sector partners;
 - d) interventions need to be developed at the spatial level which captures most of, if not all, the economic benefits and (preferably) costs of the intervention;

¹ Particular sub-regions with long-term economic deprivation and poorest growth outcomes include: The Far North and the Kaipara harbour, Thames/Coromandel and the Hauraki District, Eastern Bay of Plenty, South Waikato, areas North and South of Gisborne, parts of Manawatu/Whanganui (including Ruapehu, Rangitikei, Whanganui, and Tararua, Horowhenua) EGI (15) 148, *Regional Economic Development Programme*

- e) economic and social interventions to be designed and delivered together (such as linking local skills/education interventions with emerging industries).

Discussion point: Does the Treasury agree with these principles? Can we develop a better sense of principles? Are they too risk averse rather than opportunity-focussed? (ie what about thinking more about exploiting local advantage/strength than looking for government/market failures?)

Approach to the Forum

This forum is one in a series to fill in the gaps and provide an update to our economic narrative. Here is how we are planning on running today's session.

What	Who	Time
Intro for the session	Gabs	5 mins
How the session will run	Kirsty	2 mins
Presentation of slides	RED team	8 mins
Discussant	Girol	10 mins
Analyst report back	Udayan	5 mins
Table discussions on strategic choices (slide 8) <ul style="list-style-type: none"> Does the Treasury agree with this strategic choice framing, and which option will best support higher living standards? Is it better to think about a policy framework that combines all three strategic responses? 	Table facilitators	15 mins
Table discussions on principles (slide 10) <ul style="list-style-type: none"> Does the Treasury agree with these principles? Can we develop a better sense of principles? Are they too risk averse rather than opportunity-focussed? (ie what about thinking more about exploiting local advantage/strength than looking for government/market failures?) 	Table facilitators	25 mins
Report back	Table facilitators	15 mins
Wrap up	Gabs	5 mins

Further reading

[Slide pack](#)

[Background note](#)

Background paper: Taking a local view – Economic Performance & Living Standards

Purpose

1. This note provides background to the June 2016 regional economic development Forum slide pack.
2. We have not traditionally looked at economic performance or living standards through a regional lens, and hence the Treasury does not have a clear position on the regional variation in living standards across New Zealand. Nor do we have view on when/whether it is appropriate for government to contribute to economic development initiatives in specific communities to raise living standards, and how they could do so.
3. It seems timely to begin addressing these gaps, for a number of reasons:
 - significant public interest in regional variation in economic performance/average incomes/regional GDP per capita (eg Auckland vs regions narrative, “zombie towns”)
 - strong appetite from local government, iwi, and other stakeholders to engage with central government on their economic development priorities – from our most to least prosperous regions
 - Treasury’s focus on raising Maori living standards, and Maori Economic Development – there is a strong regional/place-based aspect to this
 - Treasury’s focus on social inclusion goals – when socially-focussed policies alone may not be enough to raise living standards, and there may be value in complementing them with more “economically-focussed policies”
 - Treasury’s focus on investment – and the desire to make a greater or smarter early intervention to minimise liabilities
 - new thinking from OECD and elsewhere about regional policy following earlier failed policies
 - updating *Holding on and Letting Go* – we need to have a TSY view these issues

Regional economic development policy

4. Regional economic development policy aims to raise the economic performance of distinct regions within a national economy. The choice of regional unit is important, and can vary depending on policy objectives and the nature of an intervention.
5. Regional economic development policy poses unique challenges. These include:
 - *discerning when a regional economic approach is appropriate*. Regional variations on their own may just reflect compositional differences rather than market or government failures that are holding back performance (absent such failures a social development policy alone may be more appropriate);
 - *designing policies that minimise risks and trade-offs* (with key risks around: displacing activity, leaning against efficient forces of agglomeration, and delaying inevitable adjustments); and
 - *choosing the appropriate “spatial level” for analysis and intervention*. What do we mean by “region” and “regional”?

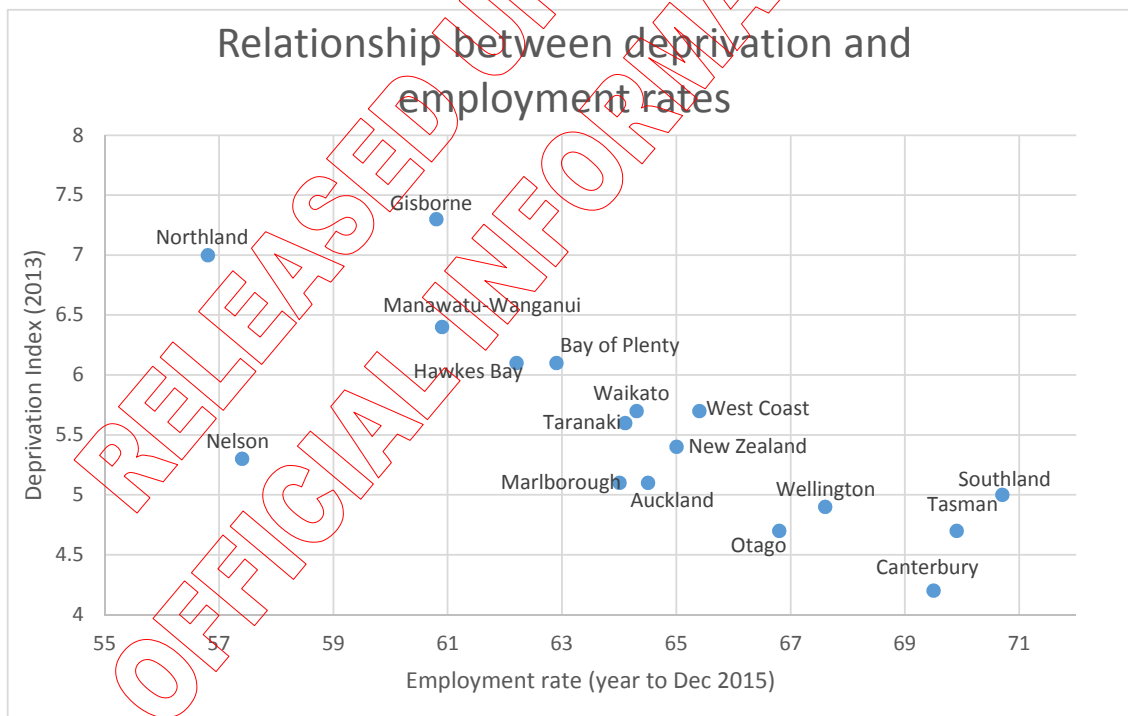
6. A robust regional policy needs to take account of these challenges. The principles and roles described later in this paper are intended to address these challenges.
7. We argue that locally-led, government-enabled initiatives have the potential to lift economic performance in deprived places, and for New Zealand as a whole, if they are focused on unlocking under-utilised potential. These initiatives can complement and leverage the return from social interventions.

The New Zealand context...

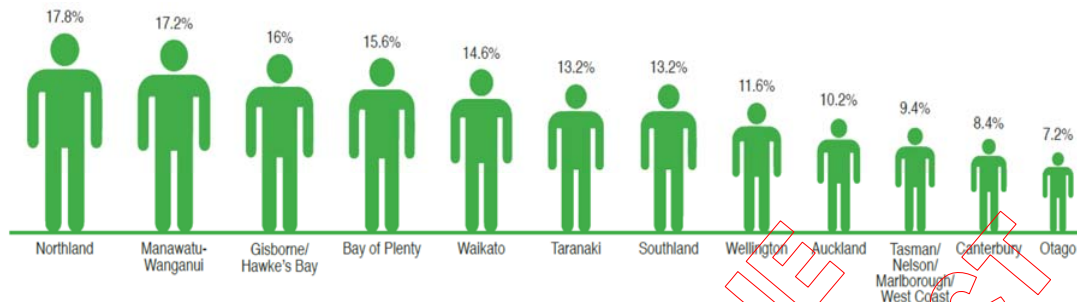
8. As *Holding on and Letting Go* notes, “New Zealand is a good place to live for many New Zealanders. Measures of quality of life, which combine measures across a range of economic, social and environmental indicators, typically rank New Zealand well compared with other higher income countries. New Zealand does particularly well on measures of health, civic engagement, education, environment and life satisfaction. However, these overall measures mask a lot of differences within these categories and across different groups of New Zealanders.”
9. One of those differences that our Narrative doesn’t (yet) mention is how the level and nature of economic activity, GDP per capita, and average incomes vary across (and within) regions. There are many reasons for this variation, with the composition of regional economies accounting for much of the difference.
10. As agglomeration and clustering theory predicts, our more urban services-based regional economies (Auckland and Wellington and to a lesser extent Christchurch) are relatively more productive and generate higher incomes than our more resource-based regional economies. The more resource-based economies also tend to be more subject to volatile performance, while the more urban services-based economies grow less rapidly but more consistently. Other trends are at play too, in particular, trends towards urbanisation and a greater role for services-based industries.
11. This generates a picture of quite uneven levels of GDP per capita across New Zealand’s regions (see the following chart). But it’s not immediately obvious what this means for living standards, or any roles for government. Different levels of GDP per capita partly reflect sectoral composition of regional economies and regional sectoral strengths rather than necessarily implying market or government failures.
12. Different average income levels across regions also do not tell the whole story about living standards since costs of living also vary (housing especially), and there are other amenities that can offset lower incomes. GDP at a regional level also disguises a lot of sub-regional variation, such as between northern and southern Waikato, or western and eastern Bay of Plenty.
13. However, we can still draw some broad conclusions. Some spatial areas show persistent low incomes, high unemployment, high deprivation, and low productivity in sectors where they should be relatively strong (such as tourism or primary industries). This suggests that factors other than industrial composition are driving outcomes. There may instead be an interaction of people and place-specific factors that is holding back living standards – such as systemic human capital and institutional weaknesses.



Regional GDP 2015 – Statistics New Zealand, 2016 - http://www.stats.govt.nz/browse_for_stats/economic_indicators/NationalAccounts/rgrp-YeMar15-infographic.aspx



Source: New Zealand, 2016 and MBIE, <http://www.mbie.govt.nz/info-services/business/business-growth-agenda/regions/web-tool-for-desktop-2015#theme/deprivation-index/map/barchart/2013/new-zealand?left-transform=absolute&right-transform=absolute>)



Percentage of New Zealanders (aged 15–24) not in education, employment or training (NEET) within each region

Source: Statistics New Zealand, 2014 (for 12 months to September 2014); Youth Statement on Regional Goals, 2014

Growth priorities: what are the roles of regions and cities?

14. Regional variation is not a new issue, and New Zealand's experience is not unusual. Modern economies produce highly variable economic outcomes across places and show dynamic shifts as the nature and location of activity shifts.
15. The risk is greater when local economies are dependent on the fortunes of a narrow range of industries, and fail to adapt to changing circumstances (such as the end of a minerals boom, or the movement of manufacturing offshore). The wind-down of a critical employer / industry can be the beginning of a wider downward spiral that is hard to reverse. Some regions have never been especially prosperous.
16. There are powerful forces underpinning and sustaining these outcomes. These include the productivity effects that favour the spatial concentration of certain industries in particular places (agglomeration), leading to a disproportionate share of output being produced in these areas. There is a high degree of self-reinforcing path-dependence in these processes, although the original source of the pathway may have been a historical accident.
17. Our Treasury preference is usually to encourage or permit the continued concentration of economic activity in key centres (forces of agglomeration) where returns are expected to be greatest. Resources and activities should be allowed to flow between regions over time. Agglomeration suggests productivity benefits from large diverse cities and clustering suggests some businesses benefit from being in smaller but specialised cities. This means higher economic performance but spatial differences.
18. This view was reinforced by the 2010 economic geography debate, which emphasised the importance of agglomeration (and Auckland especially), and implicitly downplayed the economic significance of "non-agglomerating" areas:

4. **Agree** that economic geography is a relevant consideration in domestic policy making in the following areas (while noting it needs to be balanced against other factors):
 - a) Industry and innovation policy – economic geography lends weight to focusing government interventions on specific sectors, but this should be balanced against the risks of government failure and 'picking winners' as noted in the narrative.
 - b) Agglomeration – economic geography suggests domestic policies should support/increase economic density in order to increase productivity in the economy.

19. In the New Zealand context, Lincoln economist Paul Dalziel expresses the alternative views in these terms:

One view argues that there are strong economic forces causing the strength of some regions and the decline of others and that central government should not seek to help the latter because this will only take resources away from strong regions, to everyone's detriment. One version of this argument emphasises the importance of large cities in knowledge-based economies, suggesting that investment in Auckland should be the main priority.

Another view argues that all regions can participate in a knowledge-based economy, but that different approaches are required in different parts of the country. This view recognises that effective policies for Auckland will not be the same as effective policies for Gisborne, New Plymouth, Westland or Invercargill, but argues that all regions need effective policies for their economic wellbeing. The formulation of effective, knowledge-based policies in this view requires healthy working relationships between central and local government with the close involvement of local business and community leaders.

20. The first view aligns with a traditional Treasury perspective on the operation of a market-based economy. We tend to accept variable economic performance across places, and eschew interventions that risk displacing resources from their highest return. These views are informed by the well-known instances of unsuccessful industrial and regional development policies. We are concerned to ensure the smooth operation of market forces, and to avoid various kinds of government failure. Displacement is not the only risk, but also a potential reduction in economic activity if policy moves the economy away from an efficient allocation of economic activity. Agglomeration increases the costs of this.

21. In reality, a choice between regions and cities is a false dichotomy, since the two play complementary roles in the national economy. Instead, it probably makes more sense to think about how parts of the economy complement each other, and how to strengthen connections between them (for example, thinking about the upper North Island as a regional economy, and thinking about the infrastructure network that will best support that region's growth.)

22. Recent OECD research and policy advice emphasises the economic and social value of raising the performance of lagging regions, and indicates conditions for successful interventions. The OECD's report *Promoting Growth in all Regions* discusses the results of research across member countries' regional economies. The report concludes that regional policy should be more than an extension of social policy. Instead, raising

regional growth performance is treated as an integral aspect of inclusive growth, with potentially positive effects for resilience, and fiscal health:

To put the matter simply, when less-developed regions' growth potential is not tapped, they are likely to become social problems. There is a strong case for the proposition that regional policy should be approached as an element of a growth promoting structural policy package, rather than a compensatory social policy instrument. The corollary is that if regional policy is not pursued in the interest of broad-based growth it is likely to become, of necessity, a form of redistributive social policy. And since development tends to be path-dependent, the longer such policies remain in place, the harder it will be to overcome their legacies. The departure from the region of firms and of the most promising elements of the workforce – particularly younger and higher-skilled workers – will reinforce its relative backwardness, while dependence on external transfer will erode governance capacities and foster a culture of dependence. [p.4]

23. This is a story that seems to fit some of New Zealand's regions well, including the fact that government spending per capita is heavily weighted towards our least economically prosperous regions, effectively acting as a national social transfer system. Greater economic performance in these regions would not only boost the prosperity of those communities, it would also boost our economic resilience and diversity, and reduce fiscal costs.
24. This is also consistent with an investment approach which involves greater or smarter early interventions to minimise liabilities
25. The OECD approach should not be a recipe for pushing against strong structural forces or delaying necessary adjustments. Instead, it should be consistent with a dynamic view of economies. As the report notes:

Economic geography is lumpy; policy-makers cannot make a "flat earth", and they should not try. People and firms are mobile and there is no point trying to freeze production or settlement patterns in place. Neither, however, should policy-makers neglect the fact that large inter-regional disparities do raise issues in terms of equity of access to services and access to economic opportunity. [p.4]

26. However, while the OECD story does seem to fit some of our regions' experiences, we could question whether this story fits our specific circumstances – notably our small population size and remoteness.

Social inclusion focus: People vs places...?

27. Our usual approach to deprivation and providing social service favours generic people-based policies. Such people-based policies target financial support and government services based on need rather than location. Policies are typically focused on equipping people to take advantage of job opportunities rather than seeking to create those opportunities.
28. We are implementing a "social investment" approach, the application of rigorous and evidence-based investment practices to social services to achieve better long-term results for people. The question is whether investment in economic opportunities - not necessarily financial investment - should be part of the social investment toolkit.
29. On their own, people-based policies may not be sufficient to lift people out of poverty and build their independence when economic opportunities are scarce in their communities.

Welfare can provide for basic needs, but employment provides sustainable independence, and a range of important non-monetary benefits. Training schemes may build human capital, but that may not be realised when there are few employment opportunities.

30. This may not matter if people are able to move to places with better economic opportunities. But it is important to recognise the constraints people may face in moving. While people are often prepared and able to move to where there are better economic opportunities, this may not always be possible. Often it is the most vulnerable that will be left behind in places of economic decline.
31. Moreover, a living standards framework approach implies that people are concerned about more than just income, and are not 'indifferent to place'. Rather, people are often emotionally, culturally, and socially connected to particular communities and want them to prosper, with economic opportunity being important to that prosperity. This connection can be especially strong for iwi, and may be strengthening (?).
32. Given the wide variation in regional strengths and aspirations, economic opportunities will often be specific to particular places, so that our general economic and regulatory settings may need to be complemented with tailored local approaches – potentially for national and local economic gain.

Treasury's role – Strategic Intentions

33. Our Strategic Intentions (appear to) call for an active role in promoting the performance of regional economies in the interests of inclusive growth, with a particular focus on Maori living standards.¹
34. Our intention that “People have the capability and opportunities to participate in society and the economy” commits us to:
Develop strategies for supporting inclusive growth including addressing regulation of labour market settings and reducing variations in regional underemployment.
35. Our intention that “There is a faster improvement in Māori living standards” commits us to:
Identify opportunities for the Māori economy at a regional level, through the cross-government regional growth studies (Northland, Bay of Plenty, Manawatu, Whanganui and East Coast)
36. A successful approach to these intentions could support our intention that “New Zealand has an internationally connected and competitive business environment”. This intention commits us to:
government activity providing the foundations for a strong business environment that raises productivity and ensuring the sustainability of our natural resources working collaboratively with other agencies to deliver on the Government's Business Growth Agenda.

¹ Treasury Strategic Intentions <http://www.treasury.govt.nz/abouttreasury/strategicdirection>

Objectives and approaches to policy

37. In response to regional variations in economic fortunes, most if not all OECD countries operate some form of regionally-focussed economic development policy. There is a range of objectives for such policies:

In some countries, balanced development is a constitutional imperative. In others, evening out living standards is taken as a given, and a basic objective of government. For most, spatial fairness of opportunity is seen as necessary on social justice grounds, and to help national solidarity and cohesion. (Corban)

38. To this list, we could add resilience, and making sure the full potential of all resources in the economy are well-used.
39. *Promoting Growth in all Regions* is critical of traditional approaches to regional development that sought to “prop up” lagging regions through subsidies and fiscal transfers to sustain failing industries, or to pick winners – “an approach that yielded very poor results.” [p.1] This, again, is consistent with New Zealand experience, where such policies have risked delaying necessary and inevitable structural change and have been costly blind alleys.
40. If these earlier approaches have been stark failures, what is recommended? The OECD research points to a number of common factors that have helped lagging regions to converge with leaders. Key among these are local leadership, identification of local opportunities, and horizontal and vertical collaboration between the layers of government and other stakeholders:

The most common formula for success appeared to be a simultaneous improvement in the horizontal coordination of policies, regional institutional capacities, infrastructure provision and human capital development.” [10]

Catch-up growth cannot be achieved via a top-down subsidy-based approach. It requires a coordinated effort at a regional level to identify local assets and remove policy and other barriers to their mobilisation” [12]

41. John Whitehead laid out essentially this position in a 2005 speech to Local Government New Zealand, *Economic Growth - A Regional and National Challenge*.
42. Whitehead argued for “policies that promote efficiency and provide the supportive infrastructure for growth in a sustainable and balanced way, typically manifested as an emphasis on partnerships.”
43. This would include: “making the most of regional comparative advantages – rather than imposing a one-size fits-all approach across the board. And that means identifying and making the most of distinctive characteristics and resources of regions that can be exploited economically over the long term. The seafood industry in Nelson, or the art deco character of Napier, are two obvious examples.”
44. Developing “regional capability” would also be important, meaning not just the “skills, physical capital and finance in the region, but more particularly from our point of view the institutions, networks and infrastructure that support economic activity.”
45. And in summary “this means that economic development must be locally driven if it is to be effective, not “top down”. More poetically, what we want are centres of excellence, not cathedrals in the desert. In practice, a fully “bottom up” approach may be too extreme – different regions are at different stages of development, and regional

development should always contribute to national goals as well. But “pre-packaged” programmes are not an answer.”

46. From our Narrative workshops and other evidence, it is clear that economic development is a priority for local government, iwi, and other local stakeholders. From our least to our most prosperous regions, there is a real interest in developing local economies. Many of them are designing or implementing economic development strategies. There is wide variation in their needs, aspirations, capability, opportunities, and constituencies. And the nature of the engagement sought from government reflects this.
47. Local authorities and iwi are often keen to set their own levels of aspiration, and to lead their economic strategies. This means that central government can be less concerned with what to aim for. Instead, we can focus on what support is appropriate to provide to enable local aspirations – and this will vary.

When should government provide direct support to economic development initiatives?

48. We think the case for an economic development focus is strongest where there is evidence of spatial market or government failures or where there are significant limits to mobility.
49. We propose that the Treasury adopt a set of principles to guide government decision-making in this area. The principles below reflect:
 - a recognition that differences in the mix of people and businesses in different places will always mean differences in economic performance between places;
 - a focus on government catalysing interventions (rather than significant new spending) to bring under-utilised economic potential into use;
 - OECD recommended best-practice (Promoting Growth in all Regions);
 - a living standards focus on inclusive and sustainable prosperity;
 - local stakeholders setting levels of aspiration
 - forecasted Government liabilities for social development and welfare spending in communities (consistent with an investment approach)

Principles to guide central government involvement in regional economic development

1. evidence of spatial market or government failures that are resulting in under-utilisation of local or regional skills or other assets (viable comparative advantage), with associated deprivation;
2. interventions should primarily leverage private capital, to reduce cost/risk to taxpayers. Where public funding is sought (eg for infrastructure), proposals should demonstrate investment-readiness through an appropriate business case or equivalent. Business cases should take a living standards perspective that gives weight to the social inclusion benefits of an investment;
3. leadership and commitment by local stakeholders and private sector partners;
4. interventions need to be developed at the spatial level which captures most of, if not all, the economic benefits and (preferably) costs of the intervention;

5. economic and social interventions to be designed and delivered together (such as linking local skills/education interventions with emerging industries).
50. It is important to choose the appropriate “unit of account”, or regional level of analysis. When thinking about infrastructure network investments, a macro regional view (eg top half of the North Island) will be most relevant. Thinking about labour markets might mean thinking about the links between Canterbury and the West Coast. However, when we look at specific local community strengths – such as Opotiki – a more micro lens will be appropriate.

What are the potential roles for government?

51. The government’s role in unlocking local economic potential should be tailored to local needs, opportunities, and capability. There’s no one size fits all approach. Our regions vary widely - c.f. Northland, South Auckland, West Coast, post-quake Canterbury. We need to take a place-by-place approach that acknowledges local circumstances (including potential) and the roles government can usefully play. These roles are as varied as rebuilding post-disaster, providing information, or matching local labour with local employers. Some regions are looking for close government partnership, others less so.
52. Consistent with our proposed principles, there can be a range of enabling roles for government. Most of these involve some cost to central government, but do not involve directly providing funding. Where funding is sought, private finance should be the first preference, but some proposals may need public investment (such as infrastructure).
 - helping communities to identify strengths and opportunities (eg through growth studies or similar,
 - strengthening local governance/institutions, and working to join-up local leaders
 - assisting with exploring specific opportunities (eg through developing business cases)
 - investing in infrastructure where this directly unlocks economic activity
 - working across agencies, local authorities, local people, and the private sector to coordinate and facilitate private investment in economic opportunities
 - addressing regulatory barriers/risks (eg Manuka honey)
 - engaging closely with local authorities to align (or deconflict) local and central plans (such as coordinating infrastructure investment with local economic development plans)
 - coordinating/finding links between social interventions and economic opportunities to ensure these approaches are complementary
 - providing relevant/tailored education/training to upskill local labour force for emerging opportunities
53. There is also a role for central government in ensuring it is “horizontally” and “vertically” coordinated, and that it continues to strengthen local institutions.

Case studies

54. To avoid misunderstanding, it is important to give examples of what we think this approach looks like in a New Zealand context. This will also help to make clear what we *don't* recommend.
55. The case studies summarised below share the following elements:
- the exploitation of underutilised potential, especially fixed location-specific factors of production, with minimal risk of displacing economic activities from elsewhere
 - central government playing a facilitating/coordinating role
 - local engagement and leadership
 - potential for positive social inclusion impacts
 - potential for positive growth impacts
 - sustainability, with minimal need for ongoing government involvement
 - strong private sector involvement and investment
56. We think these case studies are consistent with the OECD paradigm, a living standards approach, and our strategic intentions.
57. We also think the case studies also show a close alignment and complementarity between the objectives of He kai kei aku ringa (the Māori Economic Development Strategy and Action Plan), the Business Growth Agenda, and the social investment approach.

Case study 1 – Opotiki Harbour Development

58. The Opotiki Harbour Development Project is one of the key initiatives of the Bay of Plenty Regional Economic Action Plan designed to lift employment, incomes and investment across the region. The project is part of a community-led strategy to revitalise the economy of the eastern Bay of Plenty. The aim is to create a year-round navigable harbour entrance at Opotiki, utilising the vast natural resources of the region by allowing Opotiki to become a service and processing base for the aquaculture industry and other marine related industries. These harbour-related project have the potential to create 220 local jobs, boost household income by \$17 million per annum, and increase Opotiki's GDP by \$41-\$55 million per annum.
59. The sponsors of the project have asked Government for capital support of up to \$26 million to fund the construction of the harbour entrance as part of the overall project which has an indicative financial volume of \$200 million.
60. The Government has provided departmental resources in facilitating stakeholder engagement between regional sponsors and government agencies, enabling the sponsors to develop and submit a business case which applies the Better Business Case approach (i.e. Treasury staff to facilitate BBC workshops), and committing to a validation study which tests the commercial viability of the sea farms et al.
61. Once the study is completed, the findings will be incorporated into the final version of the respective business case and will form the basis for the final decision by Government on its support to the project as a "last funder".

Case study II – Peppers Carrington Resort

62. To unlock the tourism potential in Northland, central Government and regional partners have worked with private investors to enable the establishment of the Peppers Carrington Resort in Karikari, Northland. Private investment in the resort has been \$200 million. The creation of an environment that attracted this investment required a whole of Government approach in respect to infrastructure build, broadband, transportation and regulation around resource consensus.
63. In this context, the Government invested \$1.2 million to the Queenstown Resort College to support the establishment of the Tai Tokerau Northland campus in Paihia. The Government's support for the College was one of the key priorities as part of the Northland Action Plan as it upskills young Northlanders for a career in tourism, including the Peppers Carrington resort. The College will offer Diploma programmes to 50 students this year which will prepare local youth to meet the skills required for jobs in the resort specifically and the tourism industry more widely. Eventually the roll could grow to 350. The college has been developed with support from NZ Maori Tourism, and has attracted co-funding from private sources which highlights the collaborative focus it has

Case study III – Manuka honey

64. A scientific research programme is developing a robust science-based definition for monofloral Manuka honey to ensure consumers, overseas regulators, and industry can continue to have confidence in the safety and integrity of Manuka honey. This is particularly relevant to a number of our less prosperous regions, where Manuka honey is a growth industry.
65. MPI has committed significant resources to lead a science programme to support the development of a robust scientific definition for Manuka honey. Both departmental support as well as non-departmental resources to commission scientific research and development have been committed. Results from the programme are produced by a consortium of specialist service provider who are contracted by MPI. In collaboration with industry, MPI is planning to conclude this programme by the end of 2016.

What are the risks to manage from this approach?

66. We aim at balancing national prosperity goals with inclusiveness objectives. Finding this balance is likely to require flexible approaches to place-based interventions.
67. The principal risk from an approach that accommodates place-based economic development is that we undermine natural structural adjustment, and divert resources from higher value uses in the process.
68. We think that the principles described above will minimise this risk, especially the focus on catalysing viable commercial activities through bringing underutilised capacity into production. The emphasis on catalysing suggests government interventions that address market failures, rather than providing significant additional funding. In other words, we don't generally see lack of capital as the principal constraint. We also think it is important to have a realistic level of ambition: an equal level of prosperity across all regions is not realistic and not all places will thrive.
69. Some proposals may offer a good prospect of lifting national as well as local prosperity. The Opotiki Wharf development could be an example of that, where a one-off government infrastructure investment and business case support catalyses a commercially viable local industry (aquaculture).

70. But there could still be tradeoffs between national prosperity and inclusion, as you would expect with the application of the Living Standards Framework. This approach is likely to involve proposals that ask the government to accept a lower return than it might otherwise obtain in the interests of social inclusion. In those cases, we might think the case for intervention is strongest where there is a sizable “low prosperity” population with limited mobility or a strong connection to place.
71. We recognise a number of other risks and challenges to manage with place-based economic policies. These could be the subject of further work in coordination with other policy areas, social inclusion especially:
- in practice it can be difficult to identify to what extent the spatial distribution of economic activity is ‘efficient’ or there is ‘under-utilisation’ in a place
 - a policy that raises human capital may encourage outward mobility that leads to better outcomes for those people, but poorer outcomes for those who remain
 - how do we decide how much to invest in those isolated communities, where quality of life is adversely affected by isolation, poor or vulnerable infrastructure and unsustainable?
 - how do we ensure that more socially-focussed policies and place-based economic policies are complementary and there is real operational cooperation?

How should we think about small, declining communities with poor prospects?

72. Not all communities will exhibit latent economic potential that is amenable to the approach we’re describing.
73. In these cases, we would not recommend economic development initiatives as a key response. We would instead recommend a focus on maintaining basic services essential to a reasonable quality of life. This is often brought into sharp relief when costly infrastructure choices arise, or the continuation/availability of public services (schools, hospitals, justice services) is in question.
74. From a living standards perspective, these choices amount to tradeoffs between national prosperity, and local inclusion objectives.
75. Decisions of this kind will be inherently political. As policy advisers, we can assist decision-makers by illustrating choices via a living standards lens.
76. We would also point to the role of local authorities in devising appropriate strategies and responses. Some regions are clearly thinking about different responses reflecting varying local circumstances. Waikato, for example, is developing strategies that recognise different challenges and ambitions across the region.

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Taking a local view: Economic performance and living standards

Te Miro Forum
7 June 2016



Key issues

This Forum is one in a series of Forums filling in gaps and providing updates to our economic narrative. One of those gaps is how we think about economic performance and living standards, regionally and sub-regionally, at the level of cities and smaller communities.

Given our living standards approach...

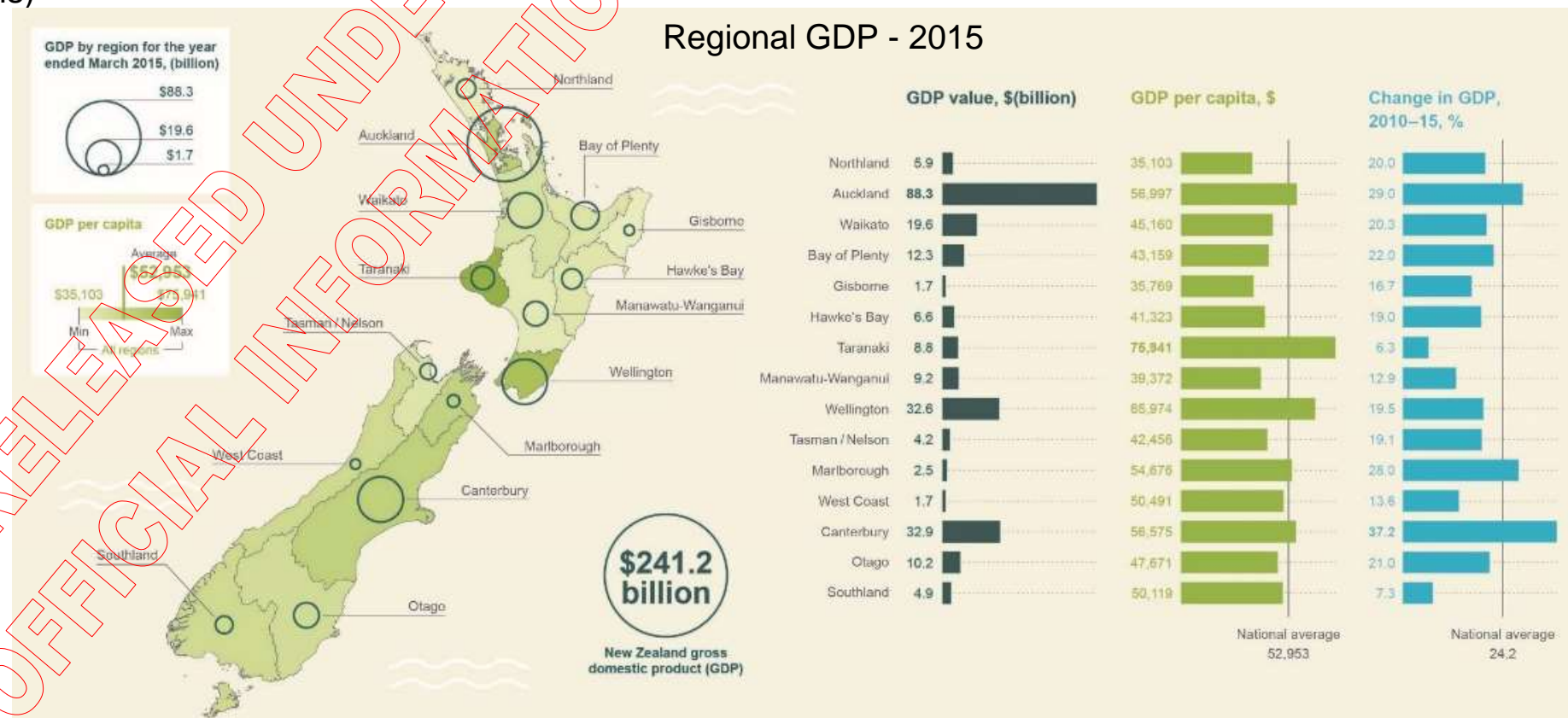
- how should the Treasury think about spatial variations in economic performance across New Zealand?
- how should the Treasury think about sub-regions that show persistently weak economic performance?
- if we take a regional economic development approach, what principles should guide central government involvement?



Policy and economic context

Our ambition is *Higher living standards for all New Zealanders*.

- economic performance/opportunity is an important element of higher living standards
- economic performance varies markedly across regions (regional GDP per capita, average/median incomes, employment levels)



How should we think about this variation?

- partly reflects sectoral *composition* of regional economies and regional sectoral strengths (would be surprising if we didn't see variation, importance of agglomeration and clustering)
- doesn't allow for *different costs of living (eg housing) and other aspects of living standards* (and people's choices) that offset lower incomes
- glosses over *sub-regional differences* (eg across Auckland, Waikato, or Bay of Plenty). Choice of spatial unit makes a big difference. (international comparisons difficult because of different units of analysis)
- so, prima facie, regional variation does not indicate a "problem", or provide a case for spatial economic intervention

When might weak performance indicate a local policy problem?

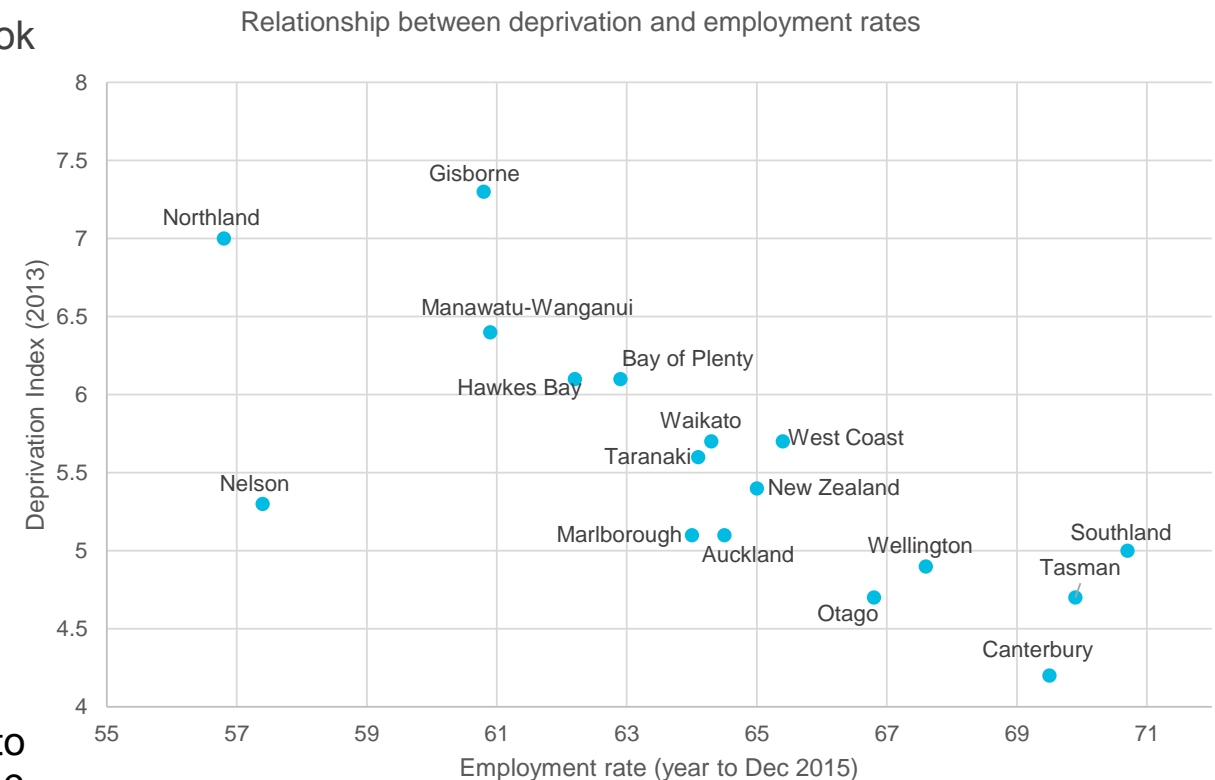
We don't have a sophisticated diagnostic tool, but we can look at a range of indicators, such as:

- high and persistent unemployment
- high and persistent levels of deprivation
- low productivity in sectors that should be strong

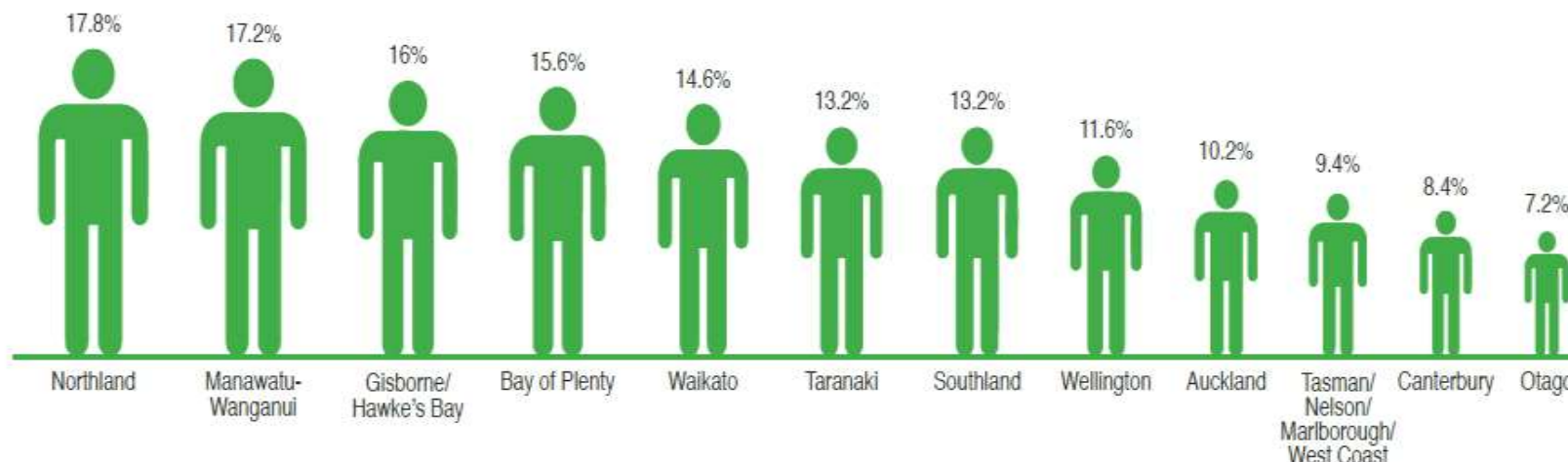
Areas with these characteristics could be subject to place-specific factors (government or market failures) that are barriers to raising living standards (also driving fiscal costs (welfare liability), and opportunity cost of lost output).

Social interventions, on their own, may not be sufficient to raise living standards where economic opportunities are limited.

Still hard to know what spatial level is most relevant – need to be flexible. Sub-regions could be more relevant than regions?



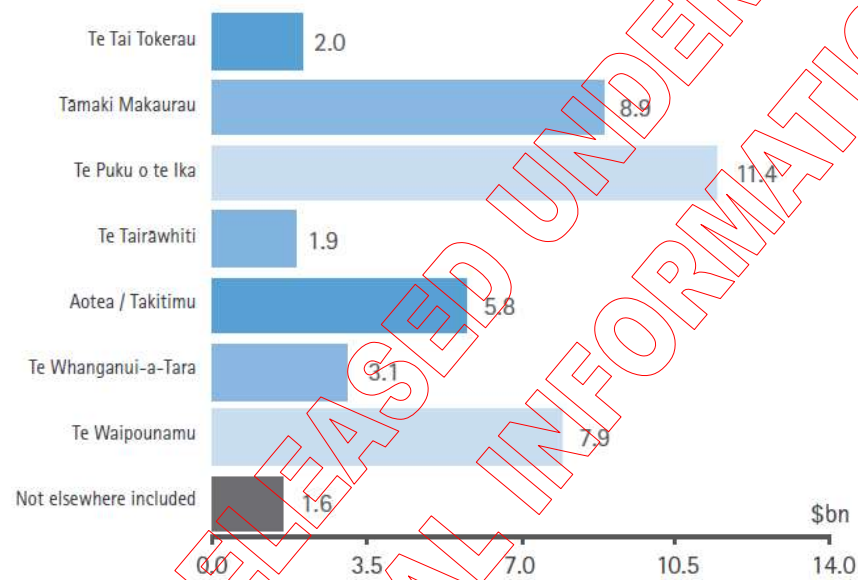
NEETs by region. Source: Statistics New Zealand, 2014 (for 12 months to September 2014); Youth Statement on Regional Goals, 2014



Regional growth studies:
some evidence of weak performance in sectors that should be strong, suggesting under-utilised potential.

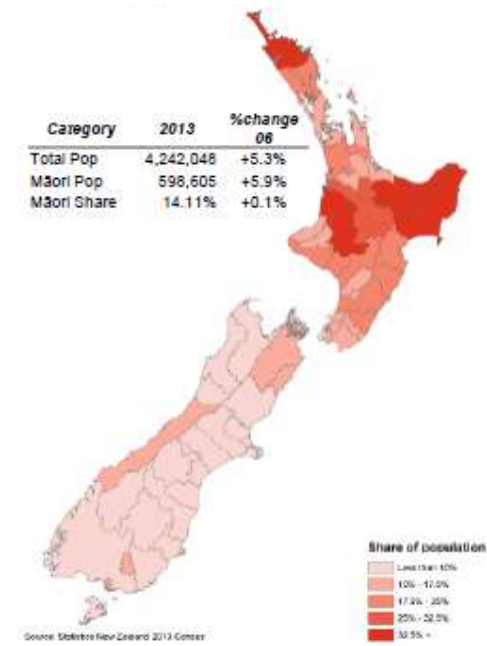
Māori Economic Development: Regional Context

Māori Asset Base by Rohe, 2013, \$ billion



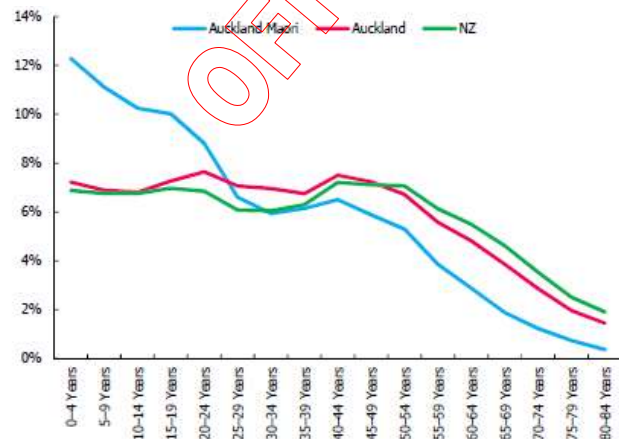
BERL, 2013

Māori Share of Population by District, 2013



Statistics New Zealand, 2013

Population by Age Group, Auckland/NZ, 2013



NZIER, 2015

There is a significant overlap between Māori population concentrations and/or the Māori asset base and the majority of regions that are priorities for Government (Northland, Bay of Plenty, East Coast and to a lesser extent Manawatu-Whanganui and West Coast).

Auckland is hugely significant, given that a quarter of Māori reside there, the majority are youthful but are less likely to be employed, highly skilled/paid and in business. - mirroring the Māori population as a whole.

Going forward, the Māori economy is likely to remain significant given the primary and permanent nature of many Māori assets and the growing proportion of Māori in certain regions potentially entering into the workforce.

Strategic framing and choices

Treasury strategic intention: *People have the capability and opportunities to participate in society and the economy*

- *develop strategies for supporting inclusive growth including addressing regulation of labour market settings and reducing variations in regional underemployment.*

Treasury strategic intention: *There is a faster improvement in Māori living standards*

- *identify opportunities for the Māori economy at a regional level, through the cross-government regional growth studies (Northland, Bay of Plenty, Manawatu-Wanganui and East Coast).*

In simple terms, and given our intentions and economic context, the Treasury faces strategic choices either to:

- adopt a (more) active approach to reallocate people and mobile resources out of poorly performing areas to more prosperous areas [is this practical on a large scale? what about people's attachment and connections to places and communities?]
- rely primarily on social development policies to raise living standards and adopt a "laissez-faire" economic approach [is this enough to raise living standards where employment opportunities are scarce, and there is path dependence?]
- consider policies to raise economic performance in poorly performing areas in tandem with social development policies (an extension of social investment) [can governments do useful things to encourage higher performance and at what cost?]

Discussion point: *Does the Treasury agree with this strategic choice framing, and which option will best support higher living standards? Is it better to think about a policy framework that combines all three strategic responses?*



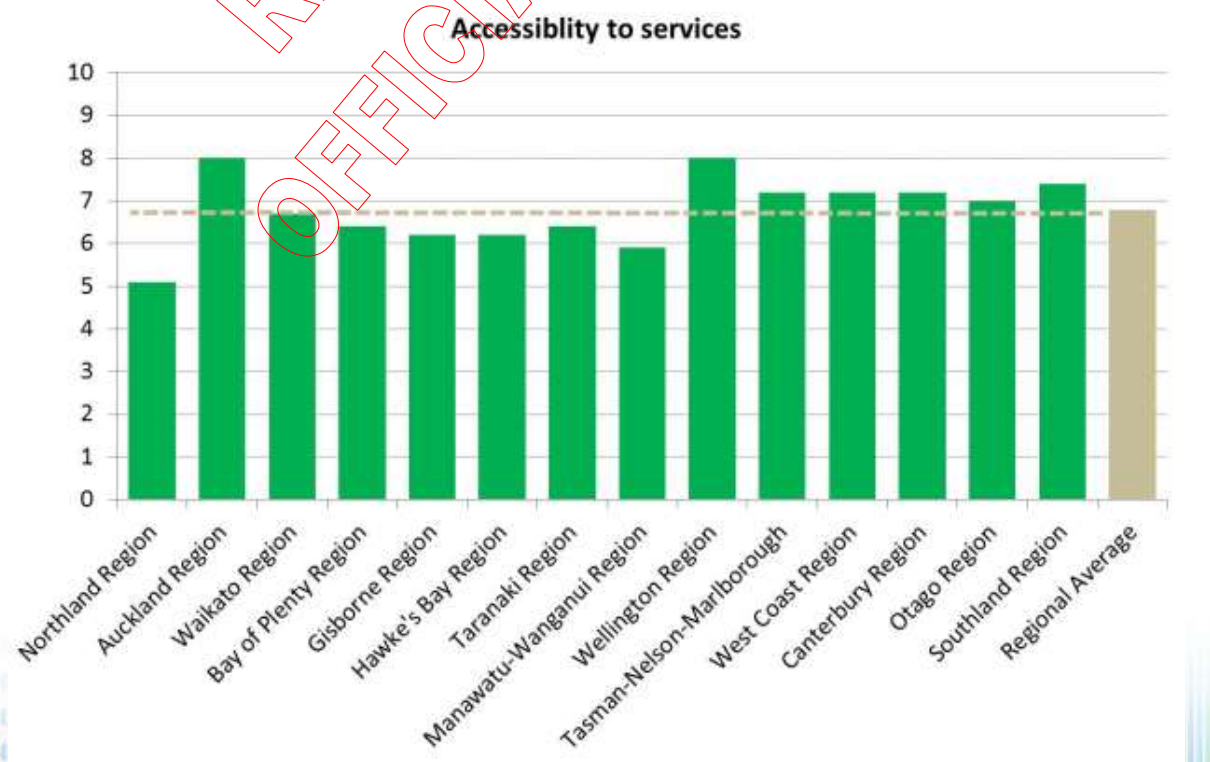
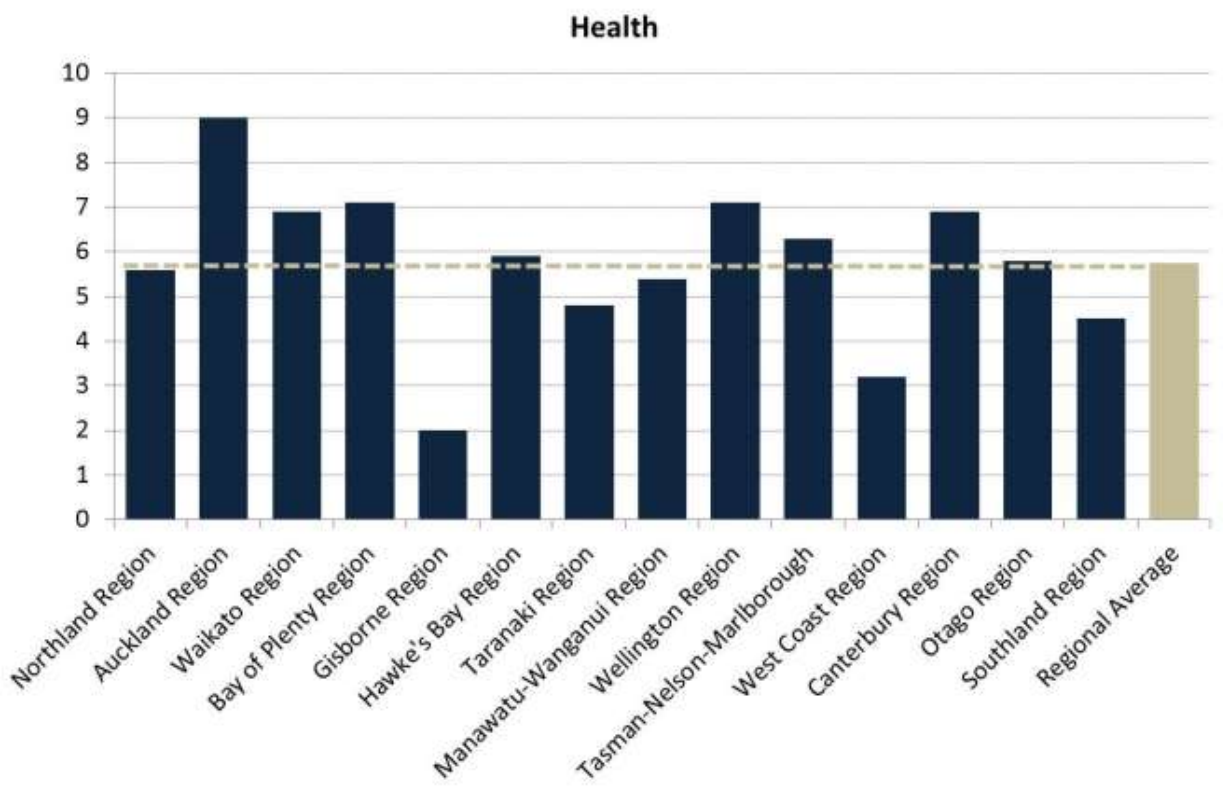
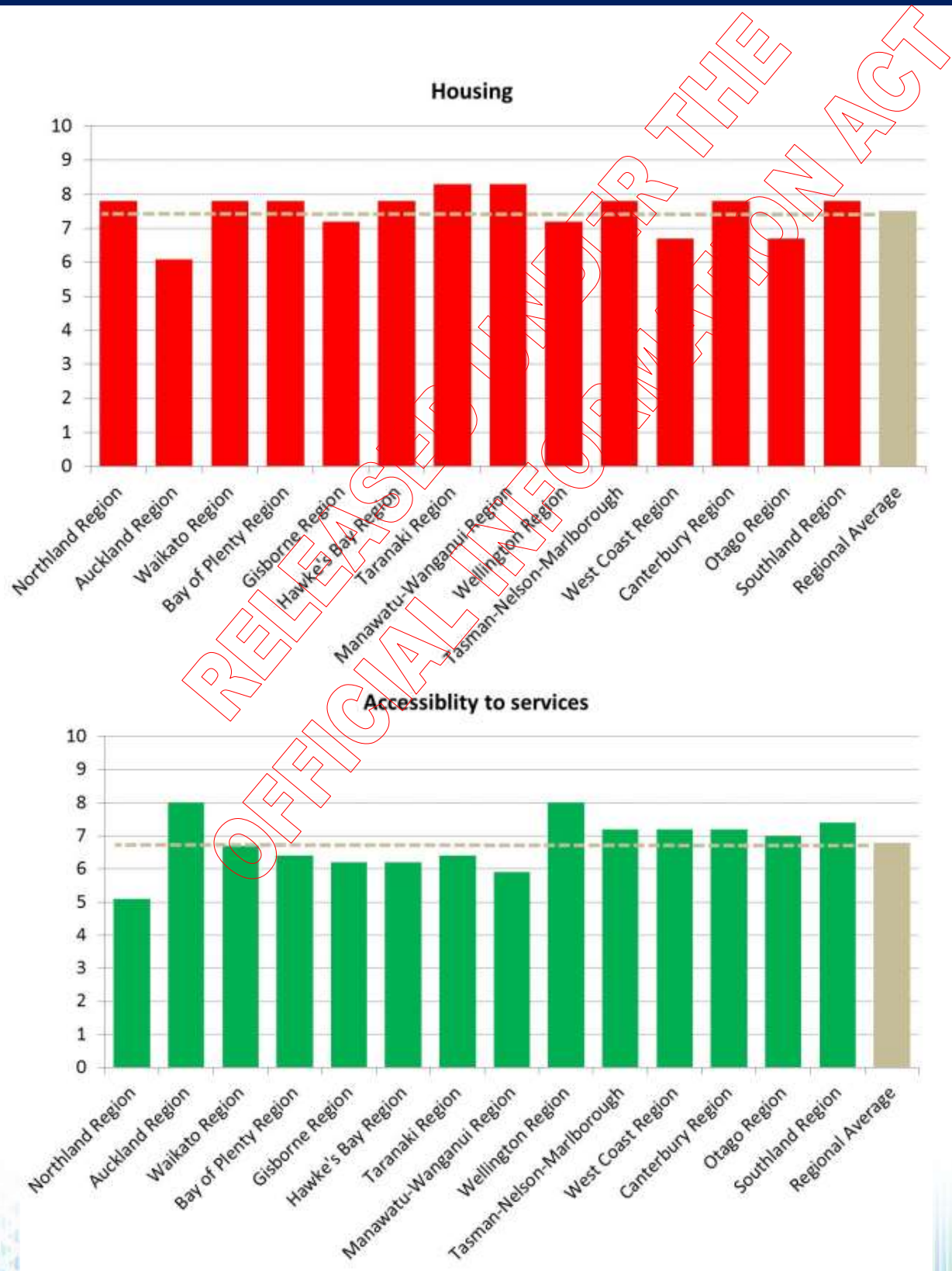
Principles to guide central government involvement in regional economic development

1. evidence of spatial market or government failures that are resulting in under-utilisation of local or regional skills or other assets (viable comparative advantage), with associated deprivation;
2. interventions should primarily leverage private capital, to reduce cost/risk to tax-payers. Where public funding is sought (eg for infrastructure), proposals should demonstrate investment-readiness through an appropriate business case or equivalent. Business cases should take a living standards perspective that gives weight to the social inclusion benefits of an investment;
3. leadership and commitment by local stakeholders and private sector partners;
4. interventions need to be developed at the spatial level which captures most of, if not all, the economic benefits and (preferably) costs of the intervention;
5. economic and social interventions to be designed and delivered together (such as linking local skills/education interventions with emerging industries).

Discussion point: Does the Treasury agree with these principles? Can we develop a better sense of principles? Are they too risk averse rather than opportunity-focussed? (ie what about thinking more about exploiting local advantage/strength than looking for government/market failures?)



Applying a living standards approach involves looking at all the key dimensions of people's living standards and across regions...



Source: <https://www.oecdregionalwellbeing.org/>



...And people in different regions may have different preferences and thus different priorities which we should respect

Which of these is more important to you personally?

You having a more secure/rewarding/enjoyable job

this one

OR

You having more and/or better relationships with friends/family/whānau/iwi/community

this one

« undo last decision

they are equal

skip this question for now »

Which of these is more important to you personally?

You having more/better skills/knowledge to be able to do the things you need/want

this one

OR

You having more time to do the things you want to do

this one

« undo last decision

they are equal

skip this question for now »

Which of these is more important to you personally?

You having more of a connection to your country/history/culture/heritage

this one

OR

You having more of a say on the policies/infrastructure your community/country adopts

this one

« undo last decision

they are equal

skip this question for now »

* 17. In which of the following regions do you live? Please select one.

- Northland
- Auckland
- Waikato
- Bay of Plenty
- Gisborne
- Hawke's Bay
- Taranaki
- Manawatu-Wanganui
- Wellington
- Tasman
- Nelson
- Marlborough
- West Coast
- Canterbury
- Otago
- Southland
- Other (please specify)

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Back up slides



Central government spending per capita is higher in more sparsely populated regions with low incomes

- regional expenditure broadly reflects the size of the population in each region. e.g. Auckland accounts for 34 per cent of New Zealand's population and 32 per cent of government spending
- most government spending is on social welfare, health and education, accounting for about 67 per cent of per capita expenditure
- average per capita expenditure estimated at \$17,826, ranging from \$21,364 in Gisborne to \$16,555 in Tasman
- spending tends to be higher in more sparsely populated areas with low incomes in the north and east of the North Island (for example Gisborne and Northland) and on the west coast of the South Island (reflecting a higher share of transport and health spending on the West Coast).
- spending tends to be lower in regions such as Auckland and the north of the South Island, where average incomes and employment rates are higher.
- variations reflect their different regional demography, needs and local economies.

Table 1 Core Crown spending by region (capex and opex)²

Region	Expenditure approach			Service approach			Population
	\$ millions	% share	\$ per capita	\$ millions	% share	\$ per capita	% share
Northland	2,750	4%	17,359	3,012	4%	19,014	4%
Auckland	24,140	31%	16,012	25,387	32%	16,839	34%
Waikato	6,679	9%	16,048	7,263	9%	17,450	9%
Bay of Plenty	4,707	6%	16,973	5,255	7%	18,952	6%
Gisborne	916	1%	19,565	1,000	1%	21,364	1%
Hawke's Bay	2,583	3%	16,663	2,866	4%	18,493	3%
Taranaki	1,634	2%	14,841	1,887	2%	17,136	2%
Manawatu-Wanganui	4,650	6%	19,999	4,400	6%	18,924	5%
Wellington	11,998	15%	24,481	8,674	11%	17,699	11%
Tasman	694	1%	14,345	801	1%	16,555	1%
Nelson	702	1%	15,062	789	1%	16,942	1%
Marlborough	771	1%	16,862	774	1%	16,937	1%
West Coast	613	1%	18,627	652	1%	19,825	1%
Canterbury	10,092	13%	18,060	10,668	14%	19,092	13%
Otago	3,603	5%	17,058	3,938	5%	18,647	5%
Southland	1,490	2%	15,696	1,645	2%	17,334	2%
New Zealand	78,020	100%	17,602	79,013	100%	17,826	100%

Source: NZIER, various Government departments

Table 2 Direct crown spending by region and type of expenditure ('expenditure approach')

2011/12 dollars per capita.⁵ Operating and capital expenditure.

Region	Social Security and Welfare	Health	Education	Core Government Services	Law & Order	Transport and Communications	Other ^e	All expenditure
Northland	6,779	3,774	2,606	492	890	826	1,993	17,359
Auckland	5,250	3,037	2,700	603	813	915	2,695	16,012
Waikato	5,728	3,214	2,447	590	991	1,058	2,020	16,048
Bay of Plenty	6,181	3,687	2,894	559	632	1,054	1,967	16,973
Gisborne	7,036	3,797	4,315	488	757	933	2,240	19,565
Hawke's Bay	5,851	3,552	2,994	488	1,080	676	2,022	16,663
Taranaki	5,625	3,570	2,116	483	473	708	1,866	14,841
Manawatu-Wanganui	6,355	3,750	3,099	484	767	830	4,713	19,999
Wellington	5,859	3,322	3,364	3,290	1,966	1,164	5,517	24,481
Tasman	5,215	3,312	2,239	474	471	721	1,913	14,345
Nelson	5,833	3,320	2,355	484	470	423	2,176	15,062
Marlborough	5,957	3,325	2,067	468	436	571	4,039	16,862
West Coast	5,897	4,493	2,439	541	451	1,318	3,488	18,627
Canterbury	5,760	3,307	2,930	1,849	841	927	2,445	18,060
Otago	6,152	3,260	3,760	528	661	698	1,999	17,058
Southland	5,564	3,222	2,700	569	638	705	2,298	15,696
New Zealand	5,714	3,297	2,854	1,026	925	923	2,863	17,602

Policy to be informed by...

If we are considering policies to raise regional economic performance and living standards in these sub-regions, what factors should influence our thinking?)

- a recognition that differences in the mix of people and businesses in different places will always mean differences in economic performance between places;
- a focus on government catalysing interventions (rather than significant new spending) to bring under-utilised economic potential into use;
- OECD recommended best-practice (*Promoting Growth in all Regions*);
- a living standards focus on inclusive and sustainable prosperity;
- local stakeholders setting levels of aspiration;
- forecasted Government liabilities for social development and welfare spending in communities (consistent with an investment approach).



What roles should central government play in regional economic development alongside social inclusion/investment policies?

Consistent with our proposed principles, there can be a range of enabling roles for government.

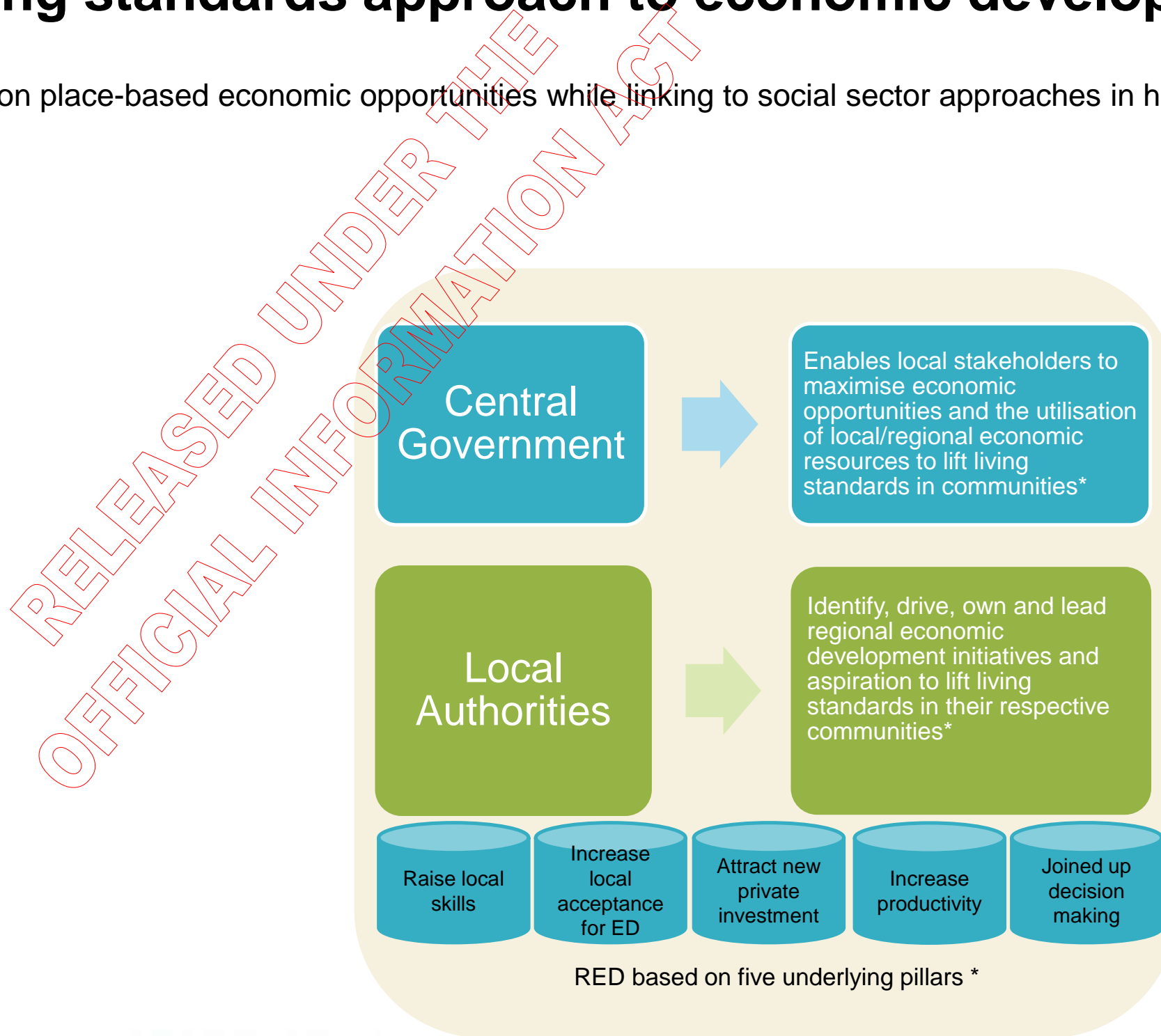
Where funding is sought, private finance should be the first preference, but some proposals may need public investment (such as infrastructure).

- helping communities to identify strengths and opportunities (eg through growth studies or similar);
- strengthening local governance/institutions, and working to join-up local leaders;
- assisting with exploring specific opportunities (eg through developing business cases);
- investing in infrastructure where this directly unlocks economic activity;
- working across agencies, local authorities, local people, and the private sector to coordinate and facilitate private investment in economic opportunities;
- addressing regulatory barriers/risks (eg Manuka honey);
- engaging closely with local authorities to align local and central plans (such as coordinating infrastructure investment with local economic development plans);
- coordinating/finding links between social interventions and economic opportunities to ensure these approaches are complementary;
- providing relevant/tailored education/training to upskill local labour force for emerging opportunities.



A living standards approach to economic development

Focuses on place-based economic opportunities while linking to social sector approaches in high deprivation areas



* identified by MPI

Some New Zealand examples consistent with these principles and roles

Peppers Carrington Resort in Karikari, Northland

Part of the Northland Regional Economic Action Plan



Objectives of the proposal

- Unlock the tourism potential in Northland
- Upskill local youth to take up roles in the resort and tourism sector more widely
- Central Government and regional partners have worked with private investors to enable the establishment of the. Private investment in the resort has been \$200 million.

Government support has been sought for

- \$1.2 million operating investment in the Queenstown Resort College to support the establishment of the Tai Tokerau Northland campus in Paihia
- The College will offer Diploma programmes to 50 students this year which will prepare local youth to meet the skills required for jobs in the resort specifically and the tourism industry more widely. Eventually the roll could grow to 350. Whole of Government approach in respect to infrastructure build, broadband, transportation and regulation around resource consensus that created an environment which attracted private investment
- Supported by NZ Maori Tourism, and has attracted co-funding from private sources.

Opotiki Harbour Development Project, Bay of Plenty

Part of the Bay of Plenty Regional Economic Action Plan



Objectives of the proposal

- Designed to lift employment, incomes and investment across the region by unlocking aquaculture potential
- Opotiki to become a service and processing base for the aquaculture industry and other marine related industries.
- Strong community-led strategy to revitalise the economy of the eastern Bay of Plenty
- Project has the potential to create 220 local jobs, boost household income by \$17 million per annum, and increase Opotiki's GDP by \$41-\$55 million per annum.
- The project is intended to reduce Central Government liabilities for social development/welfare spending in Opotiki by providing economic opportunities for the local labour force.

Government support has been sought for

- Capital support of up to \$26 million to fund the construction of year-round navigable harbour entrance at Opotiki as part of the overall project which has an indicative financial volume of \$200 million
- Departmental resources in facilitating stakeholder engagement between regional sponsors and government agencies, enabling the sponsors to develop and submit a business case

Manuka Honey Science Programme

Relevant to all four regions of the original Regional Growth Programme



Objectives of the proposal

- Science programme to develop a robust science-based definition for monofloral Manuka honey to ensure consumers, overseas regulators, and industry can continue to have confidence in the safety and integrity of Manuka honey.

Government role:

- MPI has committed significant resources to lead a science programme to support the development of a robust scientific definition for Manuka honey.
- Both departmental support as well as non-departmental resources to commission scientific research and development have been committed.
- Results from the programme are produced by a consortium of specialist service provider who are contracted by MPI.
- In collaboration with industry, MPI is planning to conclude this programme by the end of 2016.

What we heard at the narrative regional workshops

Confidence in local strengths and desire to build on these.

Real interest in developing local economies – from Iwi and local government (Many are designing or implementing economic development strategies.)

Willingness to set their own levels of aspiration, and to lead their economic strategies. (Means that the centre can focus on what kind of support/engagement it is prepared to offer, rather than thinking about targets.)

An eagerness to engage with central government, and expectation that the centre will be “joined up” (and frustration when it’s not)

A focus on collaboration with the centre, rather than expectation of “hand outs” (although some expectation that “community impact” be considered when moving the base for government services)

