Promoting Social Inclusion in the Commonwealth: the UK, Asia, Australia and New Zealand

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Redesigning the Welfare State in New Zealand

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Abstract

New Zealand’s colonial legacy is only partially reflected in the unique welfare state that developed from the late 1890s. From austere 19th beginnings, described by Thompson as ‘a world without welfare’, and the legacy of the Great Depression, the post war period saw the full flowering of an inclusive, non-contributory, welfare state based on principles of egalitarianism and full employment. The ‘cradle to grave’ perception of this protection was attacked progressively in a major free market economic transformation from the mid 1980s. The separation of economic and social policy that ensued was associated with one of the fastest growths in inequality in the OECD, and the rise in unfamiliar experiences of social exclusion and widespread lowered perceptions of standards of living. When the economic benefits of the transformation proved disappointingly small, sections of the business world pointed to a failure to lower taxes, and spending, especially spending on the welfare state. The welfare state had however been seriously weakened in its ability to provide the basic protections through reduced benefits, tight targeting and tax cuts. The election of a center-left coalition in 1999 held the promise of a softening and moderation of the singular focus on the economy and the terms ‘social inclusion’ and ‘social capacity’ began to enter into the official discourse. This paper reviews the progress under the Labour/Alliance coalition and highlights the dilemmas for social inclusion in the prevailing economic orthodoxy.
Introduction

A major purpose of this conference is to discuss the rise of social exclusion associated with globalisation and to seek solutions with possible regional policy convergence. Many dimensions of social exclusion in New Zealand can be identified: increasing inequality\(^2\), income insecurity, loss of traditional means of employment, low pay for unskilled work, casualisation of work, long hours of work, decline of family life, poor outcomes in health and education, loss of culture, alienation, loss of a national sense of social cohesion to name but a few. Different ethnic groups have been affected differently, for example, Maori and Pacific Island peoples have fallen further behind the European population on income and other average social indicators of well being\(^3\) (Ministry of Social Policy, 2001b; Mowbray, 2001).

New Zealand is a small exposed trading nation that has proceeded more quickly than many other nations with deregulation of the economy, removal of tariff protections, privatisation of state assets, labour market reform and promoting the ideals of free market competition. The rise of social exclusion and widespread perception of lowered standards of living are associated with both the neoliberal reforms commenced in the early 1980s and a radical redesign of the welfare state in the 1990s. In turn these reforms have contained the seeds of disappointment. Economic outcomes have been lack-lustre, inspiring a new willingness in the 2000s to discuss the meaning of social inclusion and a new view of the interrelationship between economic and social policies.

At the beginning of the 21\(^{st}\) century, there is an incoherence in New Zealand welfare state policy, but little debate about the reasons for it. A sharp contrast in the treatment of the old and young is apparent, with likely intergenerational conflict as the demographic changes of the next 20 years unfold. The official discourse nevertheless now includes

\(^2\) New Zealand is reputed to have experienced the fastest growth in inequality in the OECD (Statistics New Zealand, 1999).

\(^3\) An example of relative disadvantage is that a Maori baby boy living in the most deprived area of New Zealand can expect to live 15 years less on average than a European baby girl in the least deprived area (Howden-Chapman et al., 2000).
words like ‘poverty’ ‘social inclusion’ and ‘social capability’ but how these concepts are likely to be given practical manifestations is unclear. The election of a centre left coalition in 1999 has seen some of the more dramatic changes of the 1990s reversed, but the cold winds of economic reality for a small open commodity-based country in a globalised world have encouraged a cautious and conservative approach.

It is now critical for New Zealand to reexamine the traditional reasons for the welfare state and explore the shape of a new welfare state that can better shield citizens from the harsher aspects of globalisation. While developments in welfare in New Zealand, a small isolated nation, need to remain consistent with regional trends, there is also a role for NZ to contribute her experience to the evolution of regional social policy.

The past informs the present

New Zealand’s colonial legacy is only partially reflected in the unique welfare state that developed from the late 1890s. Thompson (1998) describes the New Zealand of the 19th century, as ‘a world without welfare’. When the largely young and hardy immigrants from the old country came to New Zealand they sought to reinforce with even greater vigor the strong anti-welfare mood becoming apparent in 19th century Britain. The dominant ideology was that individuals should be self-reliant and that families should care for their own (Thompson, 1998).

Early laws in New Zealand formalised family responsibility. Destitute Persons' legislation imposed obligations on the relatives of the needy with deductions from wages by employers often enforced for this purpose. While the workhouses and Poor Law were hated parts of the old country and not explicitly recreated in the ‘new country’, other

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4 For example, following a briefing to the incoming government in 1999 on living standards (The Treasury, 1999), there have been a rash of reports on the social inclusion theme. The latest contribution ‘Towards an inclusive economy’ (The Treasury, 2001), is supported by other research projects both within Treasury and in other government departments such as the Ministry of Social Policy and the Ministry of Social Development.

5 For example the Labour/ Alliance government acted decisively to return the collective Accident Compensation scheme (ACC) to its former status as a social insurance programme after significant parts of it were privatised by the former government. Likewise, indexation changes to the state pension which reduced its generosity over time were reversed. In employment law the Employment Contracts Act 1991 was replaced by a softer version called The Employment Relations Act 2000.
strictures such as charitable aid had much the same impact. In spite of romantic notions of New Zealand being the cradle of civilization in terms of the development of the welfare state, the moves to wide collective responsibility were both reluctant and late. Even following the introduction of the old age pension in 1898 the remnants of an anti-welfare attitude were strong. So strong indeed that throughout much of the first 30 years of the 20th century, only around 30% of those eligible by age for the pension collected it (Thompson, 1998).

**1938 social security act**

A critical insight (see for example (Barr, 1998, 2001)) is that the welfare state has been as much about insurance for the middle classes as about the relief of poverty. The welfare state bearing the ‘cradle to grave’ image that originated in the Social Security Act of 1938 can therefore be viewed as not only a response to the relief of hardship but also as a practical answer to obvious failures of private insurance markets. The risks of old age ill health and unemployment exposed by the Great Depression required a social insurance approach broadly inclusive of all citizens. The post-war period saw the full flowering of an inclusive, non-contributory, welfare state based on principles of egalitarianism and full employment. The Royal Commission on Social Security (1972) emphasised the inclusive ‘participation and belonging’ objective of welfare provisions rather than the mere relief of poverty. Innovative polices in the 1970s included the introduction of a no-fault accident compensation scheme, a new benefit for sole parents, and expansion of universal pensions for all over the age of 60.

Unprecedented increases in unemployment in the 1980s placed new pressures on social welfare benefits. These had been designed for largely temporary income assistance in a fully-employed economy. Traditional welfare benefits such as sickness, domestic purposes (sole parent), unemployment were subject to tight income testing, while additional welfare assistance was subject to wider tests of means, including asset testing. The rise of the New Right and the demolition of the traditional welfare state in the 1990s

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6 In Thompson's words we have had 'a rather arrogant view of history and our own hallowed place in it’ (Thompson, 1998).
held portends of a return to the values of the ‘world without welfare’ of the past. But the early 'world without welfare' depended crucially for its success on the state playing an active role in other ways. Land and home ownership was actively encouraged by state assistance, while for much of the early period, massive government public works made employment readily available. Of course neither of these underpinnings were apparent in the 1990s, making the exhortations to self-reliance for all by the New Right somewhat of an empty rhetoric.

The 1991 reforms

The presumption behind the structure of welfare benefits in the post war period was that the realistic alternative to a benefit was a full-time adequately paid job. The growing reality however was that for increasing numbers of people displaced by the economic reforms, part time insecure and casual work was all that was available. These tensions were recognised in several papers throughout the 1980s. Treasury economists expressed concern about fragmentation and inefficiency in the delivery and administration of welfare payments. They also stressed the problems of overlapping income tests and the work disincentives of the high effective marginal tax rates that are implicit in such tests. In some ranges of income, EMTRs could approach 100%. In the 1990 briefing papers they wrote:

*As a general rule, the more people facing higher effective marginal tax rates over longer ranges of potential income, the greater the costs to society and the greater the probable loss of output.*

*An indication of the effect of such scales is the fact that very few people are in jobs with an income at the level where the maximum rate of benefit abatement applies; instead they tend to have no job at all, rather than work for little gain. This is worrying since it discourages part-time work, which may be the most appropriate employment for some beneficiaries. (Treasury1990)*

High levels of benefits were identified as a major factor preventing a more gradual abatement system. In December 1990, it was announced that benefits would be cut significantly (see Box1) and a taskforce (the Change Team on Targeting Social Assistance) was established to design a new system of targeted social assistance. The

7This section draws on (St John & Rankin, 1998)
policy document that emerged was the background paper for the wide-ranging reforms announced in the 1991 Budget\textsuperscript{8}.

The 1991 Budget document *Welfare that Works* (Shipley, 1991) claimed to present an 'integrated approach to social security and social assistance'. The problem of high effective marginal tax rates that compound as social assistance becomes increasingly targeted was to be solved:

> Although any targeting system involves a reduction of total support as family income rises, the system will be designed in such a way that people are better off earning additional income and moving from dependence to independence. The reduction in assistance will not be in sudden steps because that would mean some people might be discouraged from earning more if the final result is a drop in the total of earnings and income assistance. (This is sometimes known as a "poverty trap"). Instead, assistance will be phased out over a range of income so the effects of the drop in assistance on total earnings will be less severe. Support for different services will be phased out service by service. (p18)

*Welfare that Works* put forward a vision of a seamless, global system of abatement of all social assistance. A single family income test and a single phase-out rate were to apply across all forms of social assistance using family accounts.

> The phasing out of assistance with access to social services as individual circumstances improve encourages people to move quickly from state dependence to independence, and so contribute to building opportunities for people. (p 52)

There was little emphasis on the fact that the more that is included for abatement, the longer the income range over which abatement applies, and the more people are affected\textsuperscript{9}. Family accounts was a fatally flawed concept and unworkable, not least because of the nature of the modern fragmented and fluid family who circumstances are

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\textsuperscript{8} These reforms included redesigning ACC, housing assistance, employment law, superannuation, health, students loans and allowances. Entitlement to social assistance to be restricted to the ‘genuinely needy’, not as of right as a citizen. See (Boston, Dalziel, & St John, 1999) for full analysis of reforms.

\textsuperscript{9} It seems likely that the rate of abatement would have needed to be as high as 50%. Lower rates were considered but these would prolong the abatement range unrealistically. Unfortunately, a rate of abatement of 50% coupled with marginal tax rates of 21% or 33% gives rise to effective marginal tax rates of 71% or 83%. And, even with a 50% abatement rate, the range of income over which a couple or an individual might be affected is long.
not readily summarised for abatement purposes using a smart card\textsuperscript{10}.

**Box 1  Welfare Changes 1990-1993**

- Most benefits, such as the Sickness, Domestic Purposes Benefit and Unemployment Benefit were cut by between 5\% and 27\% from April 1991. These cuts have not been restored.

  The age for youth rates for the unemployment benefit was extended to the age of 25. Stand down periods were lengthened and generally the eligibility rules, especially for the unemployment benefit, were tightened. The rates of abatement of benefits for other income were not changed, and the level of exempt income was held at levels last adjusted in 1986\textsuperscript{11}.

- The universal family benefit, a non-taxable per child universal benefit of $6 a week, was amalgamated from 1991 with Family Support and from that time all family assistance became targeted using the test of combined parental income. There is now no universal benefit for families such as still applies in the UK. For recent changes See Table 3.

- Allowances for tertiary students under 25 became fully conditional on parental income even in cases when parents are divorced and whether or not both parents actually contribute to their son or daughter's support. Students who borrow from the state for fees and living costs must repay this assistance plus interest, at the rate of 10 cents in each extra dollar earned above a low minimum. In 1999 interest on the loans of student still studying was removed.

  Certain health subsidies, formerly universal, were restricted to those in low income families through the introduction of the Community Services Card. Later, in 1996, as a concession to the real difficulties faced by families visits to the GP were made free for all children under 6 by the provision of a $32.50 subsidy. A visit to the GP can be approximately $40-50. With the card, a subsidy of $15 applies for an adult and $20 for a child. These subsidies remain unadjusted for inflation.

- Housing reforms that took effect from 1 July 1993 brought about a rationalisation of all former assistance into an income and assets-tested accommodation supplement.

- National Superannuation was to become a tightly targeted social welfare benefit to be applied for only by the poor. However the legislation, which was passed on Budget night 1991, was subsequently overturned in response to public pressure. The age of eligibility for NZ Superannuation

\textsuperscript{10} Reports of the Prime Ministerial Review Committee on the Reform of Social Assistance (1991) obtained under the Official Information Act show how impractical the idea of family accounts really was. Eventually, in a brief, barely-reported announcement the family accounts project was abandoned in 1993.

\textsuperscript{11} Some improvement to abatement for the DPB took place in 1996.
was raised from 60 to 65 between 1992 and 2001.

Although many other aspects of *Welfare that Works* also proved unworkable\(^\text{12}\), the move towards an ever more tightly targeted welfare state proceeded. Far from the 1970s ideals of ‘participation and belonging’, the social policy of the early 1990s was driven by concepts of self-reliance, targeting and a movement away from universal provisions of all kinds (Boston et al., 1999). Box 1 sets out the major reforms of the 1990-1993 period, noting any changes since then. Once the technocratic solution to overlapping income tests in the form of family accounts was discredited, it could be argued that the rationale for a total targeting approach also disappeared. In sharp contrast to the highly integrative view taken in *Welfare that Works*, many of these reforms proceeded regardless in isolation one from another, intensifying rather than solving the welfare mess and poverty traps identified by Treasury in the 1980s (St John & Rankin, 1998).

Although the government was determined to balance the budget, cutting government spending was not the main reason given for these changes. It was claimed that the welfare state actually created poverty by encouraging state dependency. So lower social welfare benefits and tighter targeting were required to push people into finding paid work. However, the numbers on benefits actually rose in the 1990s especially the numbers on sickness, invalids and domestic purposes benefits (Work and Income NZ, 2001)\(^\text{13}\). Economic growth was seen as the only way to solve the problem of poverty. However, the consequence of policy changes has been that, in spite of low or no economic growth, economic benefits appear to have been redistributed toward the highest deciles (see Table 1). In spite of the strong economic recovery in the mid 1990s, the evidence is that, especially among families with children, relative poverty remains a major social problem.

\(^{12}\) Along with the abandonment of Family accounts, part user charges for hospitals were abolished, superannuation changes were abandoned.

\(^{13}\) The percentage of children whose parents received their main income from benefits, as a proportion of all children under 18, also rose from 25% in 1990 to 28% in 1998 (Department of Social Welfare, 1999).
in New Zealand (St John et al., 2001)\textsuperscript{14}.

Table 1 Mean Household equivalent disposable income 1982-1998

\begin{center}
\begin{tabular}{ |l|c|c|c| } 
\hline
Deciles & 1982 & 1998 & \% change \\
\hline
1 & 11,522 & 9,557 & -17 \\
2 & 17,875 & 16,793 & -6 \\
3 & 20,535 & 18,728 & -8.7 \\
4 & 23,891 & 21,539 & -9.8 \\
5 & 27,710 & 25,785 & -6.9 \\
6 & 32,071 & 30,654 & -4.4 \\
7 & 37,025 & 36,295 & -2 \\
8 & 43,157 & 43,730 & -1.3 \\
9 & 50,483 & 53,419 & 5.8 \\
10 & 67,057 & 91,291 & 36 \\
\hline
All households & 33,139 & 34,789 & 4.9 \\
\hline
\end{tabular}
\end{center}

Source: (Mowbray, 2001)

The economic framework

New Zealand is a small exposed trading nation. In the pursuit of free trade NZ has proceeded more quickly than many other nations in removing tariff protections and promoting the ideals of competition. The goals of economic and social policy since the mid 1980s have stressed achieving and maintaining low inflation, removing economic distortions, lower tax and fiscal prudence with the primary purpose of enhancing the growth of Gross Domestic Product (GDP).

Separation of economic and social policy

Since the Reserve Bank Act was passed in 1989, monetary policy has had a singular

\textsuperscript{14} Virtually all the relative unofficial poverty levels suggest a fifth of all New Zealanders are in relative poverty. In 1996, 26\% of all children aged under 15 were living in households in the bottom income quintile, 23\% in the next to bottom quintile, and only 11\% in the top quintile. This percentage can change according to the adjustment for household size. Using a different household equivalence scale, Easton finds that 30-35\% of all children are in the bottom quintile (Carson & Easton, forthcoming)
focus on keeping inflation low (0-3%). The only policy tool used to achieve low inflation has been high interest rates. There has been no obligation placed on the operation of monetary policy to consider distributional implications of tight monetary policy. The Fiscal Responsibility Act 1994 requires fiscal prudence and places emphasis on achieving operating surpluses and repaying public debt. There is no requirement to monitor social impact. The choices between tax cuts, spending on infrastructure such as schools, roads, water systems and hospitals, repaying debt, or buying shares, are not required to be evaluated in social impact terms.

One aspect of fiscal prudence has been the shift from direct funding of tertiary education to loans to students. By reducing what would otherwise be spent on education, increased operating surpluses have been lent to students, creating an 'asset' on the Government’s balance sheet. Under the guise of accepted accounting practice, the government's fiscal position has appeared sound but the dubious nature of the student loan asset, its future gargantuan size, and its impact on the attitudes of young skilled New Zealanders who find overseas salaries more appealing are now beginning to be realised. While student loans are an asset of the government's, they are not, of course an asset for the country as a whole.

The third Act in the economic framework, the Employment Contracts Act 1991, designed to free up the labour market has been abolished and replaced by a softer version, the Employment Relations Act 2000. However the case for a ‘Social Responsibility Act’ which might balance the otherwise narrow economic focus of these three defining Acts has received limited attention (Boston, St John, & Stephens, 1996).

**Tax reform**

New Zealand's tax system was radically reformed from the mid 1980s with the intent to level playing fields and remove distortions (Scollay & St John, 2000). In 1986, the Labour Government brought in a comprehensive Goods and Services Tax (GST), on almost everything except accommodation. Benefits were adjusted for the impact of GST when it began but a rise in the GST from 10% to 12.5% in 1989, was made without any further compensation. Moreover, the benefit cuts in 1991 effectively undid the original compensation.
A flat tax was announced in 1987 but was not implemented as intended. Instead, in 1988, taxes were substantially flattened\textsuperscript{15}. Combined with GST, and a subsequent failure to adjust the lower tax bracket for inflation, the impact of the new tax scale was significantly regressive. Higher income tax payers did face some base broadening as tax exemptions of all kinds were removed. However they had also been the beneficiaries of a system that has no proper capital gains tax and now has no death duties. The inequalities of reported income after tax and adjustment for household size as shown in Table 1, tends to understate the true position by failing to include imputed income from wealth.

**The tax and benefit package of 1996**

A new, lower tax structure, justified by emerging fiscal surpluses was announced in the 1996 budget. Taxes were cut substantially and family assistance increased (see Table 2 and 3).

**Table 2 New Zealand Tax Schedule for personal income tax**

<table>
<thead>
<tr>
<th>Bracket</th>
<th>Effective marginal tax rate* 1988-1996</th>
<th>Effective marginal tax rate* 1/7/98-1/4/00</th>
<th>Effective marginal tax rate* from1/4/00</th>
</tr>
</thead>
<tbody>
<tr>
<td>$0-9500</td>
<td>15</td>
<td>15</td>
<td>15</td>
</tr>
<tr>
<td>$9501-30895</td>
<td>28</td>
<td>21</td>
<td>21</td>
</tr>
<tr>
<td>30,895-38,000</td>
<td>33</td>
<td>21</td>
<td>21</td>
</tr>
<tr>
<td>$38,001-60,000</td>
<td>33</td>
<td>33</td>
<td>33</td>
</tr>
<tr>
<td>$60,000+</td>
<td>33</td>
<td>33</td>
<td>39</td>
</tr>
</tbody>
</table>

* Includes the low income earner's rebate

The government claimed that these measures would benefit low and middle income

\textsuperscript{15} In 1988 there were two statutory rates of tax: 24% up to $30,875, and 33% above that. A low income earners' rebate effectively changed this to three rates: 15% tax on income up to $9500, 28% on $9501-$30875, and 33% on income above that (Table 1).
families, but in fact high income earners gained the most. For every dollar of extra expenditure or forgone revenue in the programme, 40 cents went to non-family groups, 31 cents went to families in the top two income quintiles, and only 29 cents went to the ‘target’ group of low and middle income families (Dalziel, 1999a). Single earner families gained far more than low-income two-earner families, with some low income families gaining very little.

Table 3 Weekly maximum rates of Family Support and Child Tax Credit

<table>
<thead>
<tr>
<th></th>
<th>Prior to July 1996</th>
<th>From 1 July 1998 Family support</th>
<th>From July 1998 Family support and child tax credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>For the eldest child:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aged 0 to 15 years</td>
<td>$42.00</td>
<td>$47.00</td>
<td>$62</td>
</tr>
<tr>
<td>Aged 16 years or over</td>
<td>$42.00</td>
<td>$60.00</td>
<td>$75</td>
</tr>
<tr>
<td>For each additional child:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aged 0 to 12 years</td>
<td>$27.00</td>
<td>$32.00</td>
<td>$47</td>
</tr>
<tr>
<td>Aged 13 to 15 years</td>
<td>$35.00</td>
<td>$40.00</td>
<td>$55</td>
</tr>
<tr>
<td>Aged 16 years and over</td>
<td>$35.00</td>
<td>$60.00</td>
<td>$75</td>
</tr>
</tbody>
</table>

For families supported by benefits, benefits after income tax were unchanged and families on benefits were not entitled to the new child tax credit of $15 a week per child\textsuperscript{16}. The increase to Family Support, especially for the first child (Table 3) was miniscule compared to the tax cuts delivered to high income earner. Dalziel calculated the combined impact of the tax and family support package as only 7.4% to those in the lowest quintile of household income, and one third to top quintile (Dalziel, 1999a).

Overall the tax system in 2001 imposes a high burden on low paid workers. The first $9500 of income is still taxed at the relatively high rate of 15%. Despite inflation since 1986 of over 60%, the threshold for this bottom rate has not been adjusted. Meanwhile the top threshold of $30,875 has been raised to $38,000. On income of between $9501 and $38,000, the tax rate is now 21%. On income over $38,000, the top rate was 33%.

\textsuperscript{16}The child tax credit is highly discriminatory as it only goes to those children whose parents meet the criteria of being independent from the state (Child Poverty Action Group, 2000)
until July 2000, when the Labour/Alliance government raised it to 39% for those earning over $60,000 pa. ACC levies add another 1.3% to basic tax rates.

**Is New Zealand overtaxed?**

While our tax levels are modest compared to other countries, many New Zealanders believe that they are overtaxed. In 1996, New Zealand’s total tax receipts came to just 35.8% of GDP, compared with the OECD average of 37.7% and the EU average of 42.4%. On average, the contribution from GST in New Zealand approximates the percentage for similar indirect taxes in other countries. The highest rate of income tax (33% until 2000, now 39%) is considerably lower than the OECD average top rate of 47.8% (OECD, 1999).

NZ government spending at 36.4% of GDP is modest compared to other successful countries (eg UK 37.8%, Norway 43%, Denmark 52.4% Germany 44.8%, Canada 42%). However, New Zealand is perceived by the business community to be a large government, high tax country. The New Zealand Business Roundtable\(^\text{17}\) repeatedly claim New Zealand has an inflated public sector, citing the case of Australia whose ratio is only 32%. International comparisons can however be misleading in debates over the size of the state. For example, in contrast to many other countries the state pension in New Zealand is fully taxed, with tax flows straight back to government, inflating both the tax and the spending figures. In Australia most old age pensioners pay no tax. Adjusting for tax on pensions alone would reduce New Zealand's government spending ratio a couple of percentage points. There needs to be a better understanding of these measurement issues if the debate over regional convergence in social policy matters is to be meaningful.

**Discussion**

The negative impact of the economic reforms on society has been charted by various commentators eg (Dalziel, 1999b; Easton, 1997a, 1997b; Jesson, 1999; J. Kelsey, 1993; Jane Kelsey, 1997) in reports published by New Zealand and international non-

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\(^{17}\) The NZBRT is an influential grouping of wealthy and powerful business leaders. See for example of their views ‘Government Spending could be slashed’ The Independent 29\(^\text{th}\) August 2001.
government organisations; and in regular reports by government agencies. But even on narrow economic indicators, the New Zealand experiment has been far from a success (Dalziel, 1999b). Rapid deregulation and privatisation, and the progressive withdrawal of the state from the economy, have been accompanied by lack-lustre growth, high interest rates, a widening of the income distribution, a ballooning current account deficit and overseas debt.

New Zealand’s net international investment position stood at -86B\(^{18}\) at the end of March 2001. In the last two years, along with Australia, New Zealand has benefited from higher commodity prices, a lower dollar and expanded tourism but the current account deficit remains high at around -4% of GDP (year ended March 2001). Tourist arrivals are close to 2 million people a year and there are fears that further expansion can only occur at the expense of the pristine environment on which tourism is based. Forecasts further out show a deteriorating current account deficit position even without the far-reaching events of the 11\(^{th}\) September 2001\(^{19}\). The accumulated impact of high and persistent current account deficits have serious implications for further indebtedness and the increasing foreign ownership of New Zealand’s productive assets.

By the end of the 1990s low inflation was achieved, but unemployment was still high, especially among the Maori population and the quality of much employment was low, with ongoing problems of low pay. The pressure from the business community for a lower overall tax burden, lower government spending especially on welfare, a switch towards more GST, lower company and lower flatter income taxes did not abate\(^ {20}\).

**Rediscovery of social and economic policy links**

In more recent times there has been an official recognition of the links between economic and social policy and a new willingness to debate the issues of social exclusion. One of the policy platforms of the incoming government was ‘Closing the Gaps’ a strategy

\(^{18}\) A measure of the extent to which NZ’s international liabilities exceed its international assets

\(^{19}\) Integrated Economic Services for example predicted a –7.6% CAD deficit by the year ended March 2005

designed to reduce the disparities between Pakeha and Maori. In a major break with tradition, the Treasury commissioned work on social inclusion This initiative is accompanied by work in other departments on social development and sustainable development, and at least three other companion papers from Treasury. The social indicators including low absolute incomes are acknowledged as being far from healthy

While acknowledging New Zealand’s strengths, it is not difficult to point to areas in which New Zealand currently falls short. Average material living standards have fallen relative to most other OECD countries; income inequality increased particularly in the late 1980s; the incidence of household poverty is too high; there are wide gaps in ethnic averages across a range of social indicator, there are poor outcomes in health and education among lower socio-economic groups; there are quite sharp divisions in values and attitudes on key socio-economic issues; and there are institutional weaknesses that trouble Crown-Māori aspirations and our levels of social capability more generally. Added to this is a regional picture of increasing deprivation in Northland and parts of Auckland, and stagnation in East Cape. Finally, there is the threat of more skilled young New Zealanders leaving for what they see as more prosperous foreign countries that are putting out the welcome mat for them.(The Treasury, 2001, p62)

In talking about the role of the welfare state, there is little evidence that sounder and more secure social insurance schemes to meet the uncertainties of the new economic order are being considered.

While necessary as a short-term safety net, the tax-benefit transfer system is not a realistic or desirable option to tackle in a sustainable way the problem of low absolute levels of income. Limits on the effectiveness of “passive” tax-benefit redistribution arise from the costs to growth of high marginal rates of tax, the international mobility of high-skill, high-income people, and the risks to social cohesion from having a large and expensive group of taxpayer-funded beneficiaries. An “active” approach to raising low incomes through policies that improve education and labour-market opportunities in the lower part of the distribution offers the best prospect to make a difference to distributional outcomes over the medium term. This is supported by a considerable weight of empirical evidence.

...Moreover investing in education and increasing labour-market participation are robust ways to improve social capability in dimensions such as increasing economic and social participation, increasing trust, improving health and reducing crime and victimisation. This win-win character of active policies makes them particularly attractive. (p63)
The incoherence of the welfare state in 2000s.

The intention of the new government is clearly to address issues of social exclusion, but while there have been piecemeal changes already such as to housing so far there has been little dramatic action. As noted above, the official strategy is to downplay the need for direct redistribution while emphasising the desirability of work.

In the ambivalence over the need for redistributive tax and welfare reform an incoherence has emerged, especially between the treatment of the old and the young. As noted below, the pension has been relatively unscathed and now ironically may provide a new model for social inclusion in the 21st century (St John, 2001; St John & Gran, 2001; St John & Willmore, 2001)

The old: a success story of social inclusion?

New Zealand has eschewed the approach of three pillars recommended by the World Bank and followed by countries such as Chile and Australia. Almost by default New Zealand has a basic minimum income guarantee (New Zealand Superannuation NZS) for all over 65. NZS is not income, asset or retirement tested. Residency criteria, not a contributions record establish entitlement. Being individually based and linked to average wages, it enables older people to largely achieve ‘participation and belonging’ even in the face of social change such as divorce, separation and remarriage, and changes in the labour market.

NZS remains popular and has survived many attacks. For example, changes announced to the state pension in 1991 which would have treated it like any other welfare benefit were reversed almost immediately because of the public outrage. In 1998 the surcharge introduced in 1984, a gentle income test affecting only the top 20% of superannuitants, was removed. This made New Zealand superannuation again a fully universal

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21 The government has sort to reverse some of the damaging impact of market-related rents introduced in 1991. The principal policy so far is the reintroduction of income related rents for those in the state houses. This has improved the income position of the very poorest of those renting, but the majority of low income families, markets rents still remain a significant factor in ensuring their ongoing poverty. There have been no moves to introduce assistance for home ownership for example.

22 The rate of NZS is a minimum 32.5% of the net average wage for a married person, with higher rates for single and living alone.
individually-based pension as it had been when introduced in 1976.

The reasons for the relative immunity of NZS from the welfare state reforms are political and complex; see for example (St John, 1992, 1999). The fact remains that NZS stands out as the only clear major example of universal provision in a highly targeted welfare system and in a tax system that offers limited progressivity. In terms of the objective of social inclusion, it must be judged a success, with the older population enjoying a relatively high standard of living compared to many of working age (Ministry of Social Policy, 2001a).

The superannuation fund

When the National Government in late 1998 attempted to recover lost revenue from the removal of the surcharge by lowering relativity between the pension and wages there was a huge outcry. The new Labour/Alliance government quickly reversed these changes and introduced legislation to lock in place the universal taxable individually based pension secured by partial prefunding. The Minister of Finance Michael Cullen outlined the intent in various speeches:

- *The basic intention of the scheme is to provide a sensible and secure basis for the long term provision of the first tier of retirement income*. Cullen 8/2/01

- *The Fund will allow us to maintain a universal pension that guarantees a basic minimum standard of living for superannuitants. It will finally give superannuitants some certainty about what the government will be able to provide for them. And they will know that they have to provide for themselves if they want a higher standard of living than NZS offers*. Cullen 14/12/00.

Critics have wondered how a scheme that is expected to provide at most 14% of the net cost of the scheme could ever provide such certainty or security. The intent has been clearly, to implement the fund and entrench it so that it would be difficult to dislodge:

- *My view is that the great and enduring consensuses on superannuation policy, like those in the USA and in Australia, have followed rather than led new schemes. They have followed by the law of political gravity. As the funds have grown, and as they have been seen by the population as a whole to be a clear indication of where their pensions are going to come from, they have become too strong a force to try and deny* (Cullen, 2001)

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23 The official reason given was the Asian crisis of 1998.
Other critics point to the opportunity costs of the fund. Money invested in the fund may be at the expense of many other worthwhile fiscal goals (English, 2001).

**Intergenerational issues**

Part one of the NZ Superannuation Fund bill locks into place the entitlement of each person, whether working or not, whether wealthy or not, to a generous universal pension. The baby boom retirement is likely to see the very affluent minority of older persons increase and the gap between the top and bottom of the distribution continue to widen. The difference between the percentage amounts clawed back in tax for the pensioner with no other income and those in the top 5% of the distribution is only 24%. It should be noted that for many wealthy older people the top rate of 39% rate is easy to avoid. The maximum rate many in this group pay is only 33%. The wealthiest of those over 65 get as much as 72% of the pension of the least wealthy (as compared to 0% with the surcharge). Thus the progressivity of the current system is very low if it is to support a universal pension of the magnitude of NZS into the 21st century.

In the context of a welfare state that is tightly targeted and a system in which children have lost the right to universal healthcare and a universal family benefit and students no longer have universal tertiary education, universal pensions are likely to become increasingly questioned as the strong criticisms of the Green party have demonstrated:

> Equity between and within generations is at stake as well. The Superannuation Bill provides certainty for present and future retirees yet as a society we do not offer the same certainty of state support for our young, our unemployed, our parents, our low income families or our sick.

> Indeed Child Poverty Action has commented this year that:

> “Increasingly, the obligation to pay into the superannuation fund will constrain the ability of government to increase either social welfare benefits or family payments. While there may be good arguments to support fiscal prudence, and the fund may prevent the further damage done by tax cuts, intergenerational conflicts have not been discussed. One outcome of the superfund may be a neglect of children’s increased levels of poverty.”

> The proposal feels uncomfortable for those of us over 40. We enjoyed free

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24 Tax-paid savings vehicles such as superannuation funds, can give this age group ready access to their money but have only a 33 per cent tax rate on fund earnings.
tertiary education and we are now looking forward to a guaranteed retirement income, whereas those people newly entering the workforce are burdened with student loans and at the same time will be required to contribute to the Superannuation Fund (Donald, 2001)

Even if the idea of the state accumulating some assets before the baby boom retirement may have some merit, debates about the division of future output between the old and the young, about the size of shares and the shape of NZS have not been resolved.

**Conclusion**

As the millennium approaches, we can see the issues in comparative international terms. This frames the welfare state choices in terms of either a European direction which is more universalist, generous and liberal, or an American one which is more targeted, limited and stigmatising. We can either recreate the collective arrangements of our early post war past in some form, or revert yet further back to our earlier more austere and moralistic past.

Treasury continues to see it in economic terms with statements that policies to promote increased opportunities for meaningful employment should be a priority to promote the inclusive economy. However there is little debate around the need for enhanced safety nets in the absence of such meaningful employment, nor is it clear what policies will produce the widespread well paid jobs on the scale that is required.

New Zealand enjoys a pension system, that appears to be inclusive for the elderly, and may even be a good model for other countries, especially as an alternative to the World Bank prescription of privatised pensions. In contrast to NZ superannuation, assistance to families with children and those on benefits has been highly targeted, and ungenerous. Technocratic solutions to high EMTRs have failed. Family assistance is the poor relation in the welfare system. Reflecting this, there have been no increases since 1998, and the latest budget provides for no increase in family assistance for inflation over the next five years. Other aspects of the welfare state, subsides for healthcare, child care subsidies, accommodation supplement, income that can be earned while on benefit are also neglected in terms of automatic protection from inflation.

Serious attention to the tax system including a review of the 1996 tax reductions may be
needed to find the extra revenue to extend more universalistic ideas to the working age population. A return to surcharge that might mimic the effects of more progressive tax for the old may also be needed to ensure intergenerational equity.

In the era of globalisation of economic activity and the new risks that this poses, it is important to emphasis the need for a strong welfare state, including a return to the past objective of belonging and participation. As Barr (2001) asserts:

> contrary to widely held views- the welfare state exists for reasons additional to and separate from poverty relief, reasons that arise out of pervasive problems of imperfect information, risk and uncertainty. [The] welfare state is here to stay since twenty first century developments do nothing to undermine those reasons- if anything the reverse.(Barr, 2001)

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