

# The evolution of the New Zealand economy

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# Overview of the session

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1. Focus and timing

2. Simple structural discussion

3. Exports matter – where are we?

4. Path dependence, trading environments and institutions

5. Wrap up

# Focus and timing

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Invitation was:

- ▶ be more speculative
- ▶ to stretch out the timetable – look out 3-5 years

So, approach:

- ▶ Underlying issues - what matters eventually
- ▶ Brief review of the setting
- ▶ Look ahead
- ▶ Unanswered questions

# Structure

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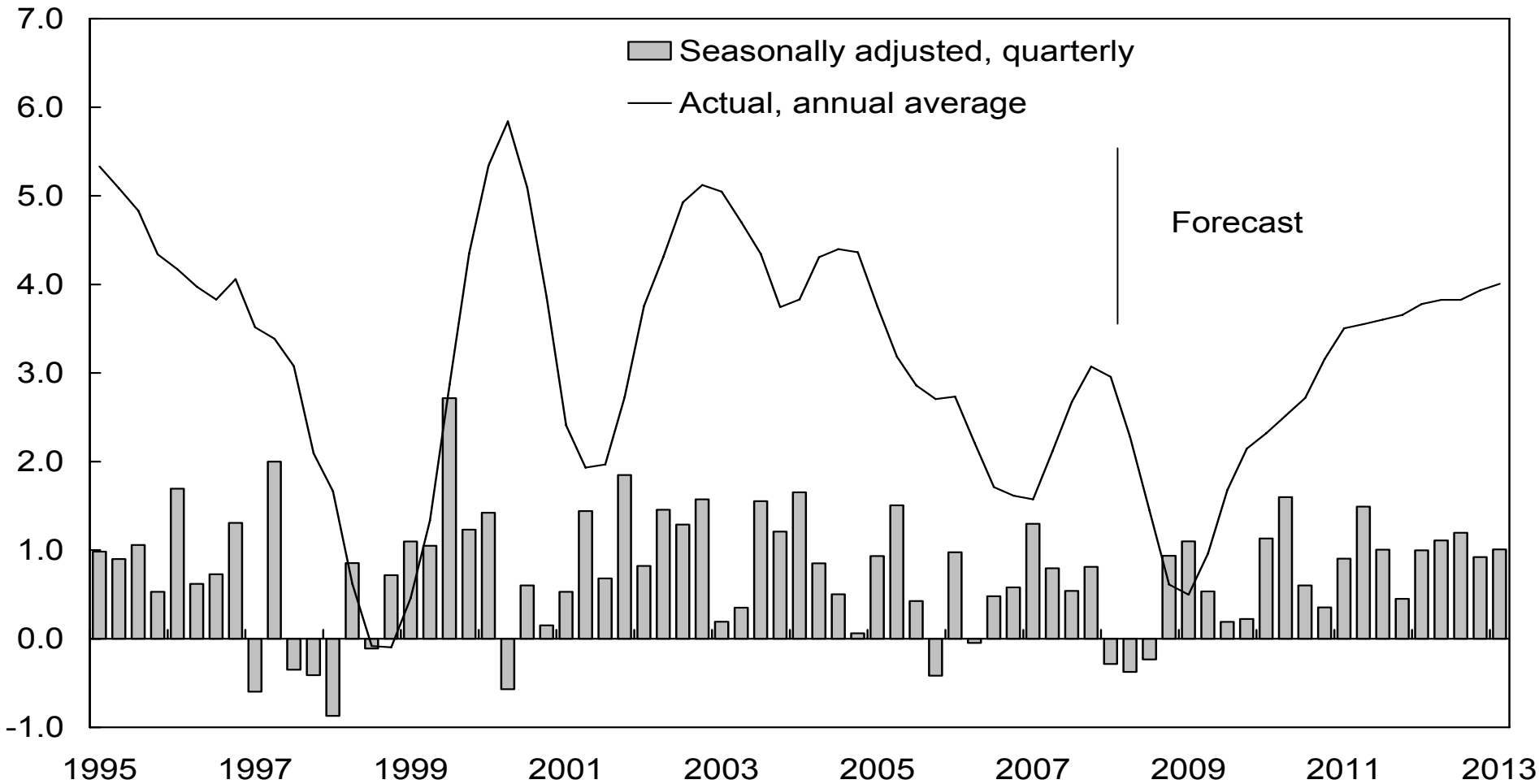
Want to consider 2 aspects:

- ▶ What's been happening to the production sector?

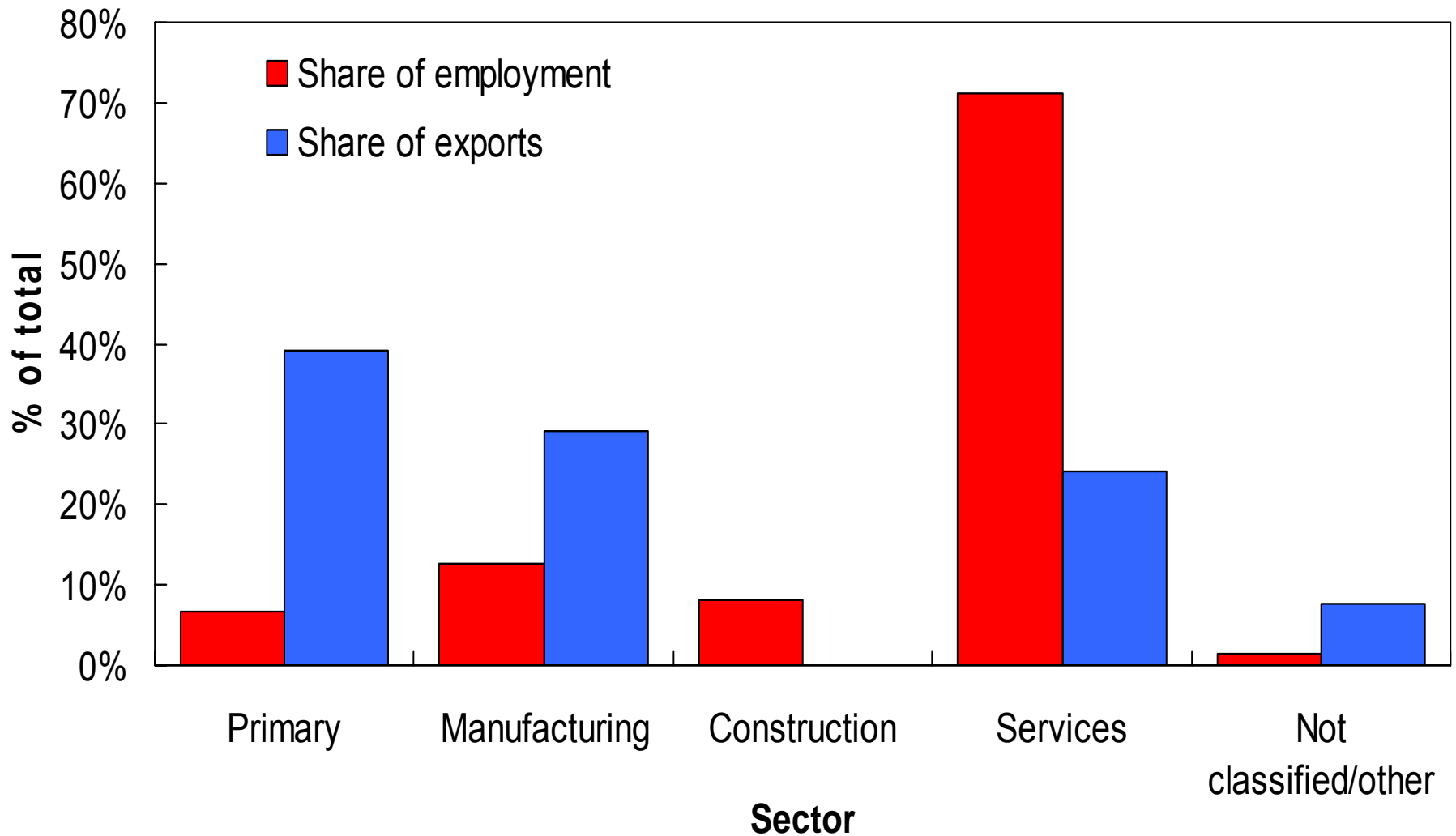
Or, because for small 'rich' countries the drivers are external:

- ▶ What's been happening to the international sector?

# Production – GDP percent change

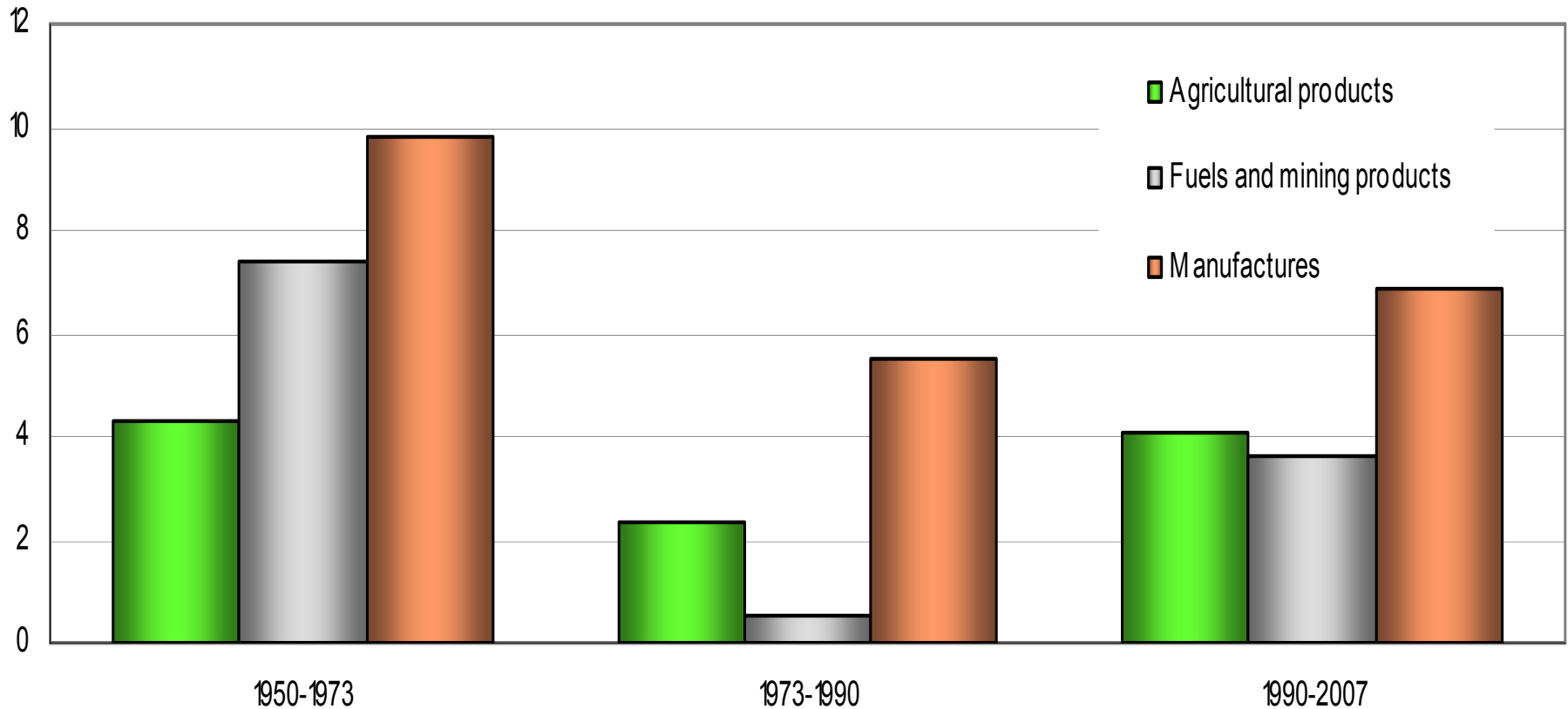


# International/domestic – what's up?

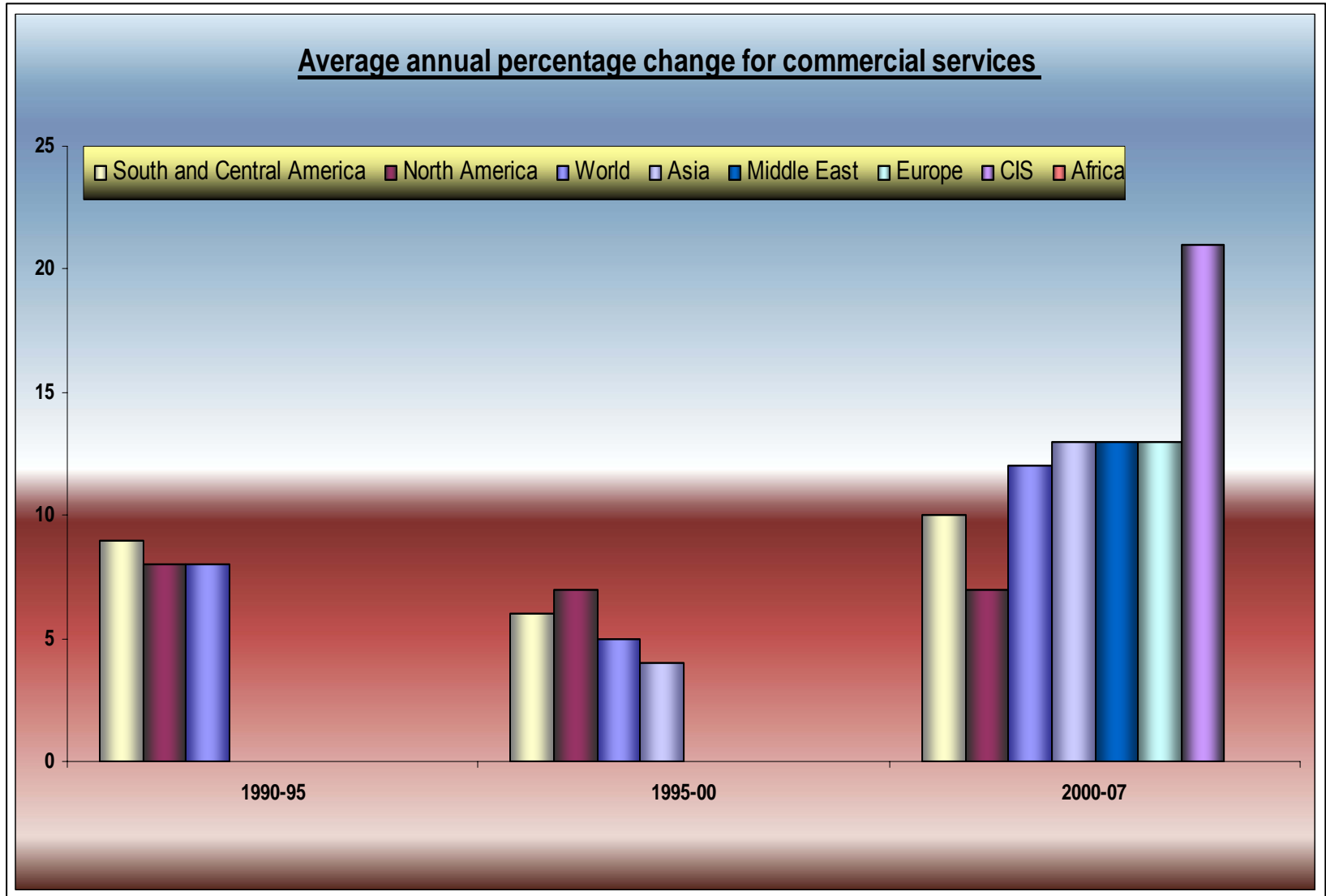


# Trade growth - goods

Average annual percentage change



# Services

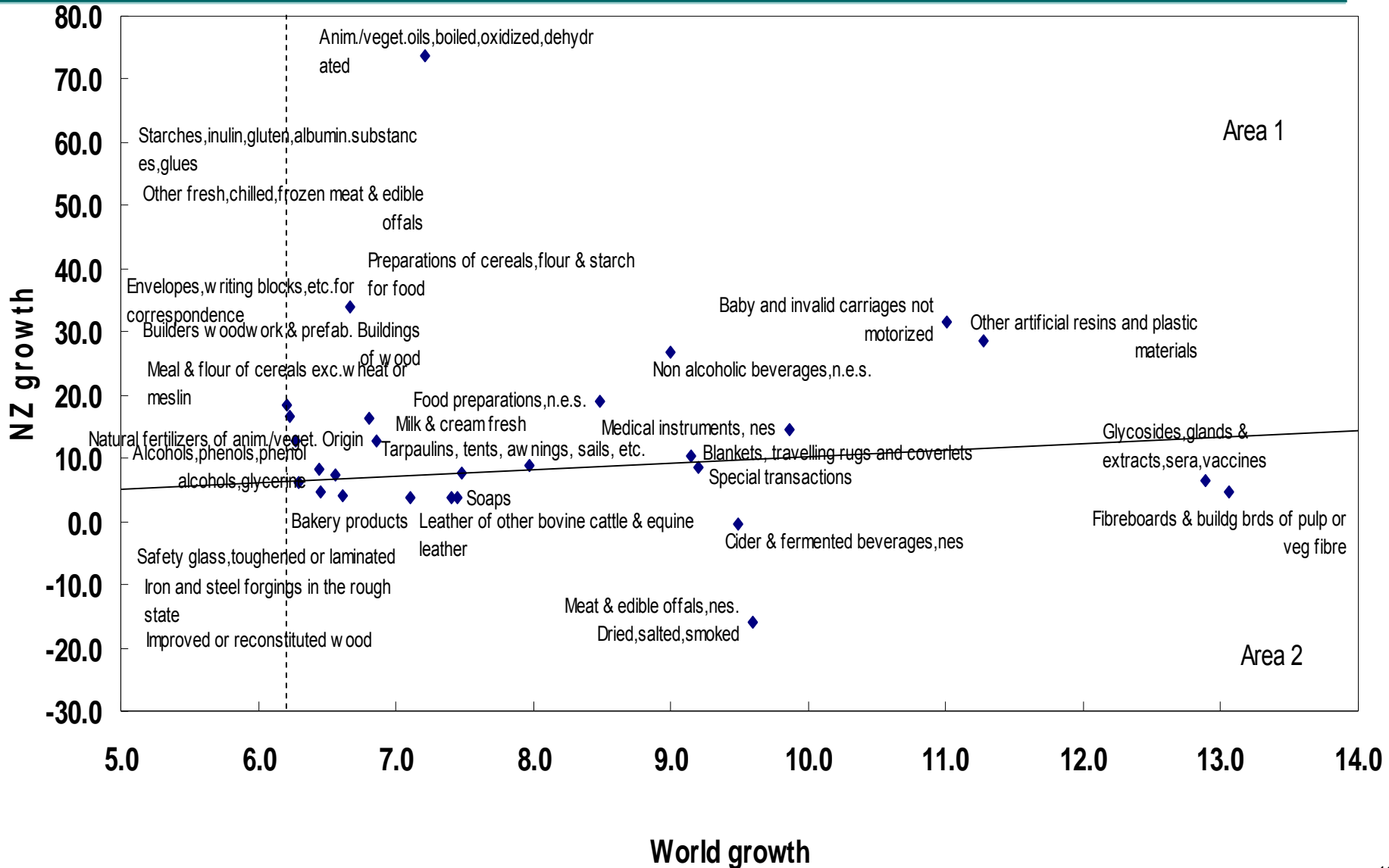


# What do we take out of this?

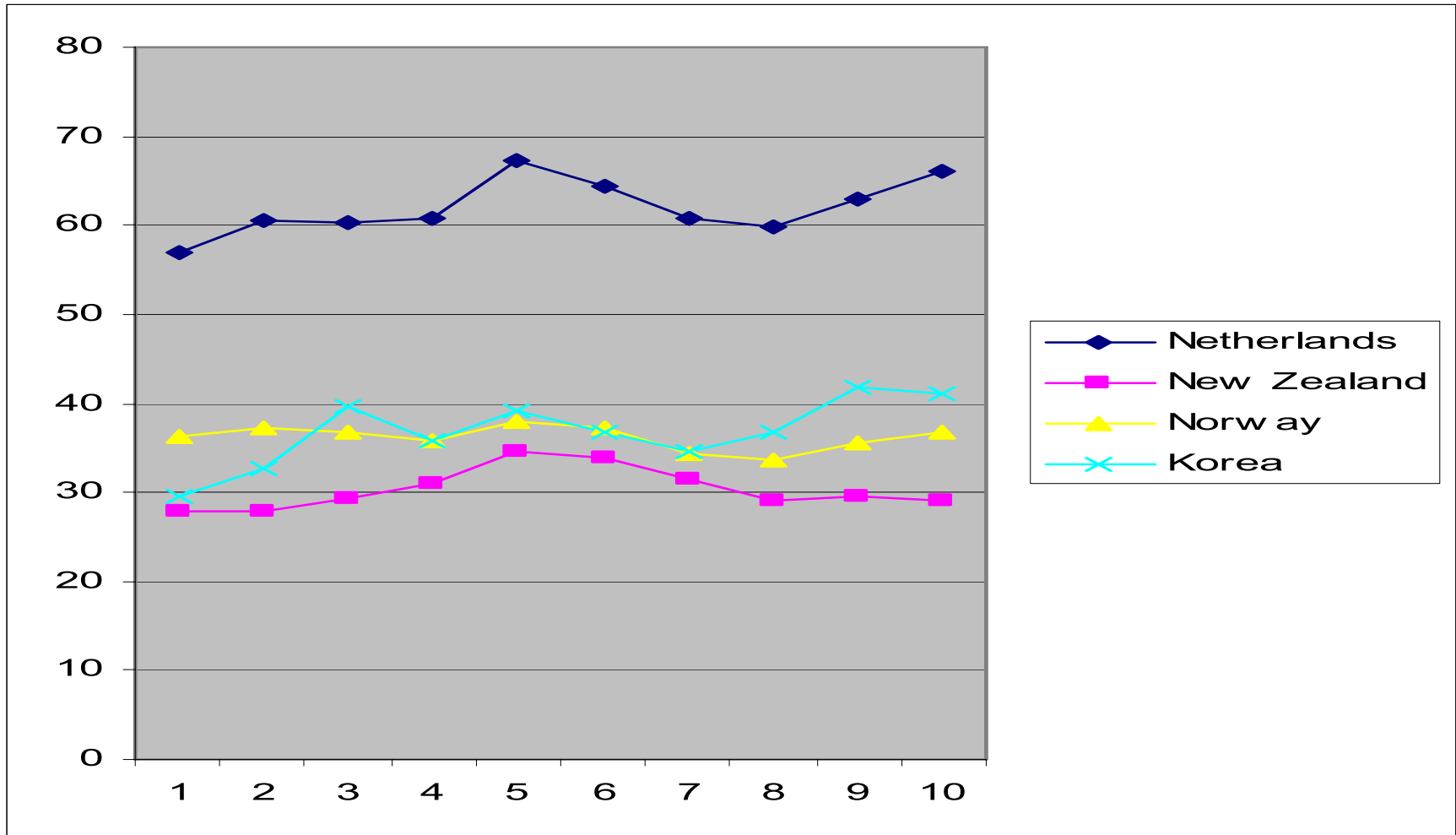
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- ▶ World economy rules
- ▶ We can only sustain tradeable production that is *reasonably* world competitive
- ▶ Globalisation has shifted the boundary between the tradeable sector:
  - ▶ 2 ways:
    - Lowered transport (or linkages) costs
    - Alternative models (shoot out in takeaway gully)
  - ▶ Indications of where we are going - Stars

# Competitive factors – what are we good at?



# But that's globalisation?



# So what is going on?

## *The Distance Factor*

- ▶ “Trade distance” matters
- ▶ Gravity models try to get to grips with the problem of trading with foreigners.
- ▶ Uses equations based on physics “inverse square laws”:
  
- ▶ Distance elasticity in international trade is -0.9 (doubling the distance reduces trade by 90%), Leamer (2007).
- ▶ So negative relation of distance from worldmarkets to GDP per capita.
- ▶ New Zealand is an outlier to this rule. (With Australia, Singapore and China, Taipei). These are the only four countries where the rule does not seem to apply.

$$T_{ij} = G \frac{M_i^{\beta_1} M_j^{\beta_2}}{D_{ij}^{\beta_3}}$$

# What are we facing?

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- ▶ In these models “distance” clearly proxy’s all the trade influencing factors (our work suggests various factors from WTO membership to being an island matter)
- ▶ So it covers costs related to distance – but these are not fixed
- ▶ Surely have been shrinking over time (e.g. technology & relationships)
- ▶ (New Zealand’s outlier status is a product of history)

# Institutions matter – where are we?

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One factor is the way institutions function.

- ▶ They favour certain types of activity by making it cheaper or less risky
- ▶ We were set up in the previous centuries to trade with the UK in certain products
- ▶ We have made moves (under CER etc) to trade with Australia

Consider a small country with unified institutions:

- ▶ Faces usual choice of highrisk/ high return from concentration or low risk low return from diversification – what about institutions?

# Closing speculation

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So if we want to set ourselves to grow faster,

- ▶ Do we need to take more risks?
- ▶ Do we need to continue to reshape our structure? (so more adjustment assistance etc?)
- ▶ Or are we just in the wrong place at the right time?