Hon David Parker, Deputy Leader Labour, Spokeperson Finance
Speech to the Financial Services Council of New Zealand
Annual General Meeting

Wednesday 04 December 2013; 12:00pm

Pullman Hotel,
Auckland

Delivery time: 20 Minutes

Thanks for the invitation to be here.

It is a pleasure to speak with you this afternoon about our approach to retirement savings and sustainable superannuation.

But first, I want to address the wider context in order to explain how our superannuation and taxation plans fit neatly into our economic transformation agenda.

While our government debt has just hit $60 billion – net debt was zero five years ago – the books are heading back into surplus, which we support.

This is a good thing. When we were last in government, we ran nine surpluses in a row – one every year.

So we know a thing or two about running surpluses.

Being fiscally responsible is a given. We know we cannot write cheques we cannot cash.

I hold to the view that it is the effectiveness of public expenditure that counts. I favour measures which improve the economy and social justice to achieve egalitarian outcomes.

The looming pressures in health and superannuation caused by an aging population must be addressed, as must the serious decline in educational achievement.

The census breakdown of age cohorts came out just yesterday.

The number of people aged 50–69 years rose to 989,364, an increase of 21.5 percent since 2006. People in this age range made up 23.3 percent of the population in 2013, compared with 20.2 percent in 2006.

All five-year age groups within this age range showed an increase, particularly those aged 65–69 years, with a 32.0 percent increase, and those aged 60–64 years, with a 29.8 percent increase.

The age groups that showed the largest percentage decreases were:

people aged 35–39 years – down 11.3 percent

people aged 30–34 years – down 7.2 percent

people aged 10–14 years – down 6.3 percent

Although the overall population increased, there were fewer people aged under 15 years in 2013 (865,632 people) than in 2006 (867,576 people).

This reinforces the need to address superannuation.

My Southern Presbyterian roots make me naturally careful with the public purse, and so I am willing to deal with the age of eligibility for universal government superannuation, to ensure its viability. This is not populist politics. We are the only party in Parliament with over 1% support is willing to address it, because the politics, as opposed to the facts, are difficult. We propose lifting the age of eligibility by 2 months a year from 2020, reaching 67 years 12 years later.

The facts are clear. Government super costs have increased from 7 to 10 billion dollars since 2008. There are currently 5 in the workforce to every one person on super. That drops to 2 ½ per superannuitant in the coming decades.

Super already costs more than all benefits combined plus working for families and the accommodation supplement.

Perhaps most shockingly of all, within 2 years it passes government spending on education – preschool, primary, intermediate, secondary, tertiary and trade training combined. Today's statistics showing a drop in educational achievement are shocking and should cause us all to sit up. Addressing the age of eligibility gives government more choices in education.

We are brave enough to address this. Our priority is to preserve the sustainability of superannuation, and to be fair to all generations. We remain acutely conscious of the need to protect those who can't work past 65 in their normal occupation and need the equivalent of super, and are continuing to consult and work on this aspect of our policy.

But my ambitions for the economy go beyond a balanced government budget.

I am convinced that unless we grow the breadth and depth of our exports we will never cover the cost of our imports and interest, and will continue our lamentable record of 30 years of current account deficit.

I believe this is New Zealand's greatest economic challenge.

According to the IMF, New Zealand had the highest external deficit in the developed world last year.

Worse than Greece.

That sorry state of affairs is predicted to continue not just this year. For the next 3 years our external deficit is predicted to be worst in the developed world.

We have been living beyond our means for decades.

Unless we fix this, we will own less and less of our own country and our younger New Zealanders will have fewer opportunities to prosper in our own country.

We need to do more than talk about rebalancing the economy to ensure more high value exports and new jobs.

In short – we need to move **from volume to value.**

The solutions are complex and it is worth briefly considering how we got to where we are today.

A global energy crisis occupied the minds of Governments in the late 1970s. In New Zealand, coloured stickers appeared on our windscreens marking the ill-fated carless days.

How many of you remember carless days? When I mention this to young people they think I'm making it up. They cannot conceive of a government so draconian that it would tell you what days of the week you can use your car.

It always amuses me when our opponents trot out images of a command economy and references to Polish shipyards whenever we propose progressive policy solutions – given that it was their party in charge at the time.

By 1983, double-digit inflation had been running for a decade. Wages had failed to keep pace. In response, the government of the day brought down a wage and price freeze.

It failed.

The economy stalled and the Government's financial position was in free fall. There was a run on our currency. Interest rates for home loans hit 20 per cent by the mid-1980s.

The efforts of the Reserve Bank to rein in inflation were formalised by the late 1980s. By then New Zealand had been suffering from high and erratic inflation averaging between 10 and 15 per cent for close to two decades.

The Reserve Bank was given independence by the Labour Government and the mandate to pursue price stability to preserve New Zealanders' purchasing power. Its obligation to protect the stability of our financial sector was retained.

The pursuit of lower inflation was not without cost, but by the early 1990s low inflation had been achieved. As the Reserve Bank observes, "*it has since become a well-entrenched feature of the economic landscape*".

The importance of controlling inflation is a lesson of history well understood. We remain committed to an independent full service Reserve Bank.

After all, we established it.

I mention this history to remind us all that a high and volatile exchange rate is not the only economic setting that hurts the tradeable export sector.

High inflation, especially in the absence of any capital gains tax, encourages speculative investments in property to the detriment of investment flows into capital equipment – and into structured savings.

The high interest rates associated with high inflation also increase the cost of investing in the capital plant which we all know is needed to improve productivity and maintain export competitiveness.

The crippling effect of high and volatile inflation is uncontested.

But it is at the very least arguable that the New Zealand prescription of monetary policy was applied in too draconian a fashion in terms of how high interest rates were pushed, and in too lax a fashion in terms of credit flows into New Zealand.

We do have a tendency for policy extremes in New Zealand.

Other countries achieved control of inflation without interest rates staying higher than international averages over time. The international trend was for lower inflation over this period anyway, and some inflationary pressures would have abated even without the Reserve Bank Act.

So while the success of the Reserve Bank Act is reasonably clear - low and stable inflation - it is important that we are not blind to the limits and side effects of monetary policy and reflect on ways we could do better.

Nor should it blind us to ways to rationally deal with our world-leading external deficit.

The other major issue the 1980s through to the 2000s left us with was an infrastructure deficit – we fell behind on infrastructure investment.

Governments faced with the enormous mess left by Muldoon had to restore the government balance sheet and deal to the crippling level of government debt. One dollar in five of taxes was being spent on interest, and this was compounding. The huge government deficit had to be curbed.

Nurses, teachers and police still had to be paid, as did unemployment benefits and pensions. Government capital investment was one area of spending that could be cut and delayed. And it was.

It took two decades to restore the government books. By then there was a substantial infrastructure deficit.

Infrastructure is fundamentally important because it is an enabler of the economy. Its importance extends beyond the cost of the asset. Without adequate roads, rail, electricity generation, transmission, telecommunication, schools or hospitals the economy as a whole cannot prosper.

A decade ago our serious infrastructure deficit threatened our efficiency and prosperity.

But now we have largely caught up.

The last government – and to be fair to them, this one too – has invested heavily in capital expenditure on infrastructure.

Central government capital expenditure has risen to amongst the highest in the OECD. We have made enormous progress.

However the question now to be asked is – where best to direct the substantial government contribution to our country's capital expenditure?

In my view it is time for government to focus more on stimulating industrial capital expenditure, following a period of necessary – and expensive – catch up capital expenditure on infrastructure.

This is not to deny the need for continued infrastructure spending. There will always be more that needs to be done. The Auckland City rail link is a prominent new example. The need to continue with the UFB roll out another.

Continued investment in all the other areas of infrastructure will always be required. But the overall balance of capital expenditure stimulated by government can now shift towards industry.

It is clear that we must pay our way in the world by being a highly successful trading nation. Our ambition must extend beyond commodities and include more high value exports in manufacturing in and beyond the primary sector.

Our proposed policy mix is intended to drive our economy towards productive investment and growth – policies that drive our productive economy.

We need to deepen capital markets, and reduce our dependence on imported capital, through making KiwiSaver universal. Too many opt out or are on contribution holidays.

We need pro-growth tax reform to ensure capital is invested on the basis of the profitability of enterprise.

We have proposed a capital gains tax excluding the family home. Currently, speculative over investment in property is rife. A substantial driver is the tax bias which favours investment in land and buildings over investment in productive businesses. This is a serious problem.

That tax bias on property speculation also contributes to our underinvestment in bank deposits, retirement savings and in productive plant and manufacturing equipment.

The absence of a Capital Gains Tax also pushes up house prices beyond the reach of many, and enables some of New Zealand's wealthiest people to pay lower rates of tax than less wealthy New Zealanders, which is plainly unfair.

It is worth noting that a reputable public opinion poll out a couple of weeks ago shows a majority of people now in favour of the introduction of a capital gains tax.

We need research and development tax credits – the second leg of our pro-growth tax reform – that will encourage innovation and push our product mix towards higher value goods and services.

We need changes to monetary policy to enable more attention to be paid to our overvalued and volatile currency, which currently hinders exporters and import substitution.

The current Reserve Bank Act is 25 years old. It forces the Reserve Bank to give primacy to inflation targeting ahead of the exchange rate and external balance. We believe its objective should be broadened.

I am committed to a prosperous balanced economy that fairly delivers for everyday New Zealanders through decent jobs that sustain good wages. Currently not enough people are on good middle incomes.

People on good middle incomes tend to save, pay taxes, and contribute to strong societies.

The policy challenge, for me, is how we achieve this step change towards higher valued output sustaining higher incomes. Achieving this will deliver social well-being and maintain New Zealand's control of our own destiny.

Growing working New Zealand in this way will take improvements in productivity in the tradeable export sector.

This change in viewpoint has come about in no small part because the Global Financial Crisis laid bare the frailties in economies which pushed financialisation of the economy too far. Inadequate investment in the productive economy left excessive reliance on the service sectors.

Pouring more coffees, tucking-in more tourists or selling more raw commodities doesn't add enough to our productivity or sustain enough well-paid jobs in other parts of the economy.

We need to transform more of our products, and create additional value. The rest of the world sees this too, and competition will always be tough.

Our exports haven't grown as a proportion of GDP. Our share of world trade has been dropping, and all the talk of added value over the last 30 years hasn't grown middle New Zealand.

The globalisation of world trade accelerated exponentially since the 1980s.

We should have encouraged investment in the sophisticated plant and innovation needed to improve labour productivity and sustain high wages.

In New Zealand savings were low, monetary policy jacked up our exchange rate and deterred productive investment, incentives for research and development went out the window, and tax policy advantaged speculation for capital gain.

The labour market remained slanted towards lower skill jobs, where working people on low wages substituted for capital investment.

Improvements in tertiary education, important though they are, are no substitute for capital.

Even with low wages we could not compete against developing countries when producing lower-value high-labour content manufactured goods.

Our failure to save and invest sufficient new capital compounded. We didn't raise productivity, and so we fell further behind productivity improvements in other countries.

As a consequence, while there are exceptions, our productive and export base has narrowed and we have hollowed out well-paid jobs.

Imbalances in the economy remain, and need to be fixed.

And they will never be fixed if we restrict the debate to doctrinaire slogans and mindless adherence to economic dogmas whose time has passed.

Which brings me to savings.

Labour approach to retirement savings and sustainable superannuation is based on our history and values tempered by the economic circumstances we would be likely to face as an incoming Government.

We have a proud history in retirement incomes policy and an enviable track record – most notably KiwiSaver and the NZ Super Fund – the Cullen Fund.

We will build on this legacy as a means to not only improve the incomes of future New Zealand retirees but also as a way to help build a stronger and fairer economy.

Our opponents tend to give in to short-term political expediency.

They killed the Kirk scheme, they railed against and voted against KiwiSaver – they opposed and called the Cullen Fund a “dog”. To compound the felony, they stopped contributions to the Cullen Fund, and wound-back contributions to KiwiSaver, at the first opportunity.

This short-term expediency has already had a large cost. .

As fund managers told me at the time, after the biggest cleanout in a generation is a good time to invest, not stop investing – particularly with zero net government debt thanks to our nine years of surpluses, and with the Crown cost of funds at a historic low.

The cost of this folly will continue to grow, unless you believe that future returns from investment in the private sector will be lower than the crown’s cost of funds. And if you believe that, then most of you should quit, because you would already be telling your investors to pull out of capital markets and stick their money in government stock instead.

Failing to contribute to the Cullen fund also assists the government to understate the true challenge of funding future superannuation to our aging population.

This was a big wrong call by the current government.

Next year marks the 40th anniversary of the commencement of the Kirk scheme. Our first retirees would have soon been drawing down their annuities, from the fund calculated by your industry to be worth in the region of a quarter trillion, maybe more, today.

We were actually 20 years ahead of our Aussie cousins, in this regard. Killing off the Kirk scheme was another big call by our political opponents that was wrong.

We have already stated that we see universal KiwiSaver as the means to help many more New Zealanders achieve a comfortable retirement, and to grow depth in our own capital base.

Frankly, that we are still debating this issue 40 years on beggars belief.

Our election policy won't be announced till next year but the main principles are clear.

Once universal KiwiSaver is put in place there is merit in stepping up contributions split between the employee and their employer over several years to reach a level sufficient to fund an adequate income in retirement. 9 % was our target at the last election.

Obviously, we wouldn't want to put New Zealand families under financial pressure. We would want contributions to increase as incomes recover as we lift out of this period of lower growth. We suggested 1% pa at the last election. To assist the lowest paid, we will increase the minimum wage.

We see a need to reconsider the investment profile of the default funds in relation to the age of the saver.

Despite cogent and detailed advice from the sector, the current government has decided the default option should be into conservative funds, irrespective of age of saver.

We all know that on average that means our savers and our country will be significantly poorer as a result.

Younger savers should be in balanced growth funds. We accept that advice from the industry bc it is so patently clear. Another big decision on savings they got wrong.

According to ANZ, an average 25 year old will miss out on $72,000 over their lifetime by staying on the conservative default option rather a 'lifecycle' plan.

I acknowledge the work you are doing around some form of limited guarantee against risk of loss of capital shortly before retirement. We are cautious about this, especially if, as the OECD speaker suggested at your recent conference, this comes with restrictions on being able to switch providers.

We are interested in the work, but will take some convincing.

We have noted your proposals to offset the over-taxation of long term retirement savings to make the tax playing field with rental property more even. We note our capital gains tax and ring fencing of tax losses from property investment already push in this direction more than our political competitors, but we recognise more needs to be done.

The option of extending KiwiSaver to include a basic level of life and income protection insurance, as exists in Australian group superannuation schemes, is again something worthy of further discussion as policy develops over coming months.

You raise an interesting idea in relation to the gap in our income support systems where many families are required to adjust to significantly lower household incomes due to prolonged periods off work due to a serious illness.

I am interested to hear more from you about this proposal and see your research.

Although we do see merit in trying to achieve the cross party consensus you desire on long term policies like retirement income policy, we recognise the severe challenges to achieving that in an MMP environment if one or more parties are committed to gainsaying policy for a 'quick buck' in electoral terms.

The regrettable track-record of policies in this area is testimony to the inherent frailty of a consensus. If you think I am being too tough in that regard, then I would remind you that our opponents:

- Killed the Kirk work based savings scheme
- Opposed the Cullen fund at inception
- Stopped contributions at the wrong time
- Won't restart even when we get back to surplus (now want net debt to be under 20%).
- Opposed the creation of KiwiSaver
- Undermined KiwiSaver through fiddling with contribution rates
- Have no vision to lift either the contribution rate or coverage
- Made the wrong decision of default schemes
- Refusal to address tax biases which are unfair to savers and distort the economy towards speculation and consumption
- Are bloody minded in their refusal to lift the age of eligibility for universal government superannuation

That is quite a list of what I believe were big wrong calls, but good luck on consensus.

So to conclude.

Exports are largely stagnant overall. They are still dropping in manufacturing outside the primary sector.

Headlines based on the terms of trade at a 40-year high miss the point.

We remain over-reliant on consumption and overseas debt, instead of elaborately transformed exports and productivity growth.

We need a breakthrough in our economy to give hope and opportunity, by growing the value of our productive economy. To achieve this we must increase our capital intensity.

Governments cannot, and should not, do everything. Priorities have to be chosen wisely.

As a country we need to move the focus towards industrial capital expenditure, after some years focus on public infrastructure.

The next government must actually deliver the genuine step-change we need – a step-change that takes us from volume to value.

It has been talked about for years.

However, in order to maintain and grow our prosperity and meet the challenges of tomorrow we need a government prepared to place genuinely transforming the economy at the centre of its agenda.

Moreover, we do not hold to the now quaint notion that the fundamental role of government is to provide a benign environment for market competition.

It is much more complicated than that – modern economies need to be much more sophisticated to prosper and so does their government.

We are heading back to surplus and the growth numbers are as I would expect coming out of a prolonged recession and with the $40 billion Christchurch rebuild finally gearing up.

We will build on the sound foundations we laid when last in government – KiwiSaver – the Cullen Fund.

We will tackle the profoundly distorting taxation arrangements for investment and savings.

As I said earlier, being fiscally responsible is a given. We know we cannot write cheques we cannot cash.

We know what needs to be done, and we have the vision and the determination to see it through.

Thank you and enjoy the rest of your day.

ENDS