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# New Zealand number one

by Kenneth Simmonds

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***A national strategy may not be simple to specify nor easy to implement, but a sustained search for it will change the inward-looking focus to questions of how, where and why to gain advantages over other countries.***

In 1873, New Zealand's gross domestic product per capita surpassed Australia's and Britain's to make it world leader for the first time.<sup>1</sup> While it was number one for only 14 years, New Zealand stayed close to the top for nearly a century. It last held the number one position in 1938 and until 1967 never ranked lower than number eight. From 1967, however, New Zealand's ranking began a long slide until it reached number 36 in 2000. Hopefully, it will never go much lower. Only persistent pursuit of a losing strategy at government level could prevent New

Zealand's natural resource endowment from producing a middle ranking GDP per capita with relative ease. As so colourfully pointed out by John Gunther in 1972:

*"To this country, grass, turned into wool, lamb, and mutton by that four-footed factory, the sheep, or into milk, butter, cheese, and powdered milk by that equally industrious animal, the cow, is like oil to Kuwait. Beautifully, simply and endlessly, the soil has poured out the wealth that let New Zealand live its easy, cushioned life."*<sup>2</sup>

But there is an important difference between oil and soil. Oil extraction in Kuwait depletes its resources and reduces the present value of its per capita wealth. New Zealand's agricultural production, in comparison, makes no perceptible dent in the present value of its wealth.

This value would even increase were

New Zealand to do nothing except expand its population more slowly than the rest of the world. And China's growing demand for food will be enough on its own to ensure that prices for New Zealand's agricultural output grow faster than the prices New Zealand pays for imports of manufactured products. After all, China has less



Patrick Lundberg, Untitled (Corner Composition) [Detail], 2004, acrylic on board.

than 10% of the world's arable land and more than 20% of the world's population. As if that were not enough reward for strategic ineffectiveness, the tourism value of New Zealand's under-populated scenic areas will also increase as such areas vanish elsewhere.

If New Zealand is to raise its GDP per capita back to the levels of leading countries, however, New Zealand residents must do more than husband the non-depleting natural resources they have inherited. New Zealand must become a source from which non-resident firms and individuals obtain services that provide the best value to them that they can find worldwide, while the prices they pay for those services leave a high return to New Zealanders for their input. The higher the present value of this return, the higher will be New Zealand's GDP per capita ranking.

A higher ranking for New Zealand will not be achieved without opposition from other countries as they strive to gain more for their own residents. New Zealanders' choices of what they offer to the rest of the world and of the terms on which they are prepared to deal across their borders, amount in effect to a New Zealand strategy.<sup>3</sup> Whether or not New Zealand receives a higher share of global income will depend on the strength of this New Zealand strategy relative to the strategies of competing countries.

In a competitive world, where one country's loss may be another's gain, the best way for New Zealand to avoid any repeat slippage in its GDP ranking is to aim again for the top position – to be number one. A number one strategy may not be simple to specify nor easy to implement, but a sustained search for it will change the national focus. It will change from an inward-looking concern for stimulating the New Zealand economy to questions of how, where and why it might be possible to gain significant strategic advantage over other countries.

### **Picturing New Zealand's business future**

Some have argued that the seeds of the future are already planted.<sup>4</sup> Their approach would be to identify these seeds and forecast the future that these imply. But there is more to international performance than forecasting. Performance depends upon the stream of strategic actions and reactions taken by many countries. Performance is not a foregone conclusion stemming only from paths already chosen. With wise actions a country can be turned around in a short number of years, just as a firm can be turned around. There is ample evidence of countries whose strategies have led to major changes in GDP per capita in a very short period of years. Over eleven years, Hong Kong rose from 35<sup>th</sup> place in 1982 to 3<sup>rd</sup> in 1993. Singapore rose from 37<sup>th</sup> place in 1982 to 4<sup>th</sup> in 2000, passing Hong Kong which had fallen back to 10<sup>th</sup> place by that year. Japan also recorded rapid gains and rapid falls, rising from 32<sup>nd</sup> place in 1976 to 3<sup>rd</sup> in 1991, only to fall to 13<sup>th</sup> place in 2001.

Significant changes in any country's ranking from year to

year are usually due to relatively recent action by the country or its competitors, and there is no reason to believe New Zealand should be an exception. Any explanation of the slide in New Zealand's performance since 1966 will lie more in the actions the country chose to take over the past thirty years than in its earlier history. Looking ahead, changes in New Zealand's GDP per capita ranking will be determined by what its residents choose to do from now on.

This paper contributes to the search for a number one strategy using a form of reverse deduction. New Zealand is assumed to have once more achieved the number one ranking by 2025. A set of propositions is then advanced as to the characteristics of surviving and newly emerged New Zealand businesses that this leadership position will have entailed. They are likely, though not individually necessary, characteristics of the businesses of a number one economy, though not exhaustive in the sense that they provide a complete description of the entire economy. Nor do they indicate the alternative paths that might be taken to build these characteristics, or the problems that different paths would encounter. The overall picture conveyed, however, is rather more than just a wishful scenario of the future.<sup>5</sup> The opportunities for New Zealand to excel in the relatively short period of 20 years are quite constrained, and significant advancement towards each of the ten characteristics would almost certainly be necessary for the country to reach a number one ranking by 2025. For each of the ten characteristics, a sketch is provided suggesting how New Zealand business might be described in more depth, given that the characteristic advanced has emerged strongly.

Depiction of the characteristics of business in a number one economy has another advantage. Without such a picture, those wanting to improve a country's performance seem inevitably to couch their proposals in the terms used to describe aggregate economic performance – mainly national accounting terms, but sometimes the economics of industries. They invariably use terms such as foreign investment, productivity, investment levels, savings ratios, overseas borrowing, home ownership percentages, and so on, all of which describe the aggregate economy. Even when they look at business they tend to refer to industries in general terms, such as dairy, timber or services, and to generalise about the need for more innovation, better education, human-resource development and better access to capital. They certainly do not focus on decision making at the business level and what would make it attractive for firms to locate in New Zealand rather than in other countries. Moreover, the motivations of business decision makers resident outside the country who will inevitably play a significant role in determining New Zealand's performance as a country, are usually omitted entirely.

With a description of the characteristics of the businesses that will be carried on in a number one economy, it becomes much easier to discuss what might be done to help businesses

to achieve these characteristics, and to discuss it using business-oriented language. A more direct focus on business, particularly foreign domiciled business, should also help to overcome the tendency for so many New Zealand politicians to sound like talking textbooks in economic and social theory. Even Roger Douglas, in his action-oriented ABC “There’s Got To Be A Better Way!”,<sup>6</sup> used predominantly macro-economic variables and mentioned foreign businesses only once or twice. Much the same can be said of the Porter project on New Zealand which couched most of its analysis and recommendations in macro-economic terminology and the questionable micro-economics of the Porter approach, while at the same time recommending that government should move beyond economic policy.<sup>7</sup>

## **Characteristics of business in a New Zealand ranked number one in 2025**

### ***1. Surviving products and services are justified by global demand***

Except for those carrying out New Zealand services that cannot be operated from abroad, New Zealand firms and their employees are almost all competing in a global marketplace with worldwide customers. Products or services justified solely by New Zealand demand contribute very little to its high GDP per capita. Market segments within New Zealand have proven to be so small that they do not justify separate attention. Products designed for New Zealand alone have been found to be both too costly for New Zealand and sub-optimal for any global segment. Even when not sub-optimal for a global segment, sales outside New Zealand have not grown. Firms producing elsewhere to meet global demand have gained economies from their global coverage and seem predestined to replace New Zealand production entirely.

### ***2. Skills are advanced and expensive to emulate***

Services to residents of other countries use advanced skills and knowledge that bring high incomes to their New Zealand suppliers. Even with these high incomes, the cost of replicating the services outside New Zealand would be greater than the prices at which they are now supplied. Products and services for overseas markets that are based on unskilled or semi-skilled labour have provided very little opportunity for significant incomes to New Zealand suppliers and have largely vanished from the New Zealand supply scene. Anything New Zealanders still produce for export that requires more than a small percentage of unskilled or semi-skilled input, has to be sold at a price that leaves such a low “national profit” that it reduces New Zealand’s GDP per capita when the man hours involved are taken into account. This applies even to products using New Zealand sourced materials, whether animal, vegetable or mineral. Even greenstone koru are cheaply produced in China, and only greenstone products with high individual design bring reasonable incomes to the New Zealand artisans still working in greenstone.

### ***3. Imports of materials and unfinished products have almost vanished***

The only physical production left in New Zealand using foreign materials is that for which the inward transport costs of materials or components are minimal. Where foreign materials of any significant weight are needed, the cost of inward and outward shipping required for domination of a global segment put New Zealand producers at a significant disadvantage to producers in countries located closer to the supply of the materials and to bigger markets of final users. The production of jewellery and furnishings using New Zealand designers and very expensive materials, however, has flourished, particularly for the world tourism market where customer spending regularly exceeds their spending in their home markets.

### ***4. Highly specified brands have replaced bulk primary produce***

Marketing successes from precise brand positioning of products with an agricultural base such as wines, juices, honeys, lavenders and olives led to an advanced New Zealand expertise in brand marketing which has extended to encompass everything extracted from natural resources. Creativity in designing and branding products so that they can command premium prices has percolated even to outputs which for centuries were sold at auction as bulk commodities. Greasy wool is one example - now an input into very advanced products and no longer a bulk export. The world’s finest yarn mixtures, turned into cloth for exclusive named-brand suit lines have recorded the highest prices for any cloth worldwide, while still leaving high profits for the overseas producers of the clothing brands.

A marked feature of New Zealand’s exports is the way in which brand owners almost without exception now retain title until the products reach retail or an industrial user. New Zealand producers know their ultimate customers and control the complete batch of services that the customers see themselves as buying when they purchase the products. In so doing, they avoid transferring monopoly profits to foreign middlemen, and services best acquired outside New Zealand are purchased through competitive tender. By retaining title, New Zealand suppliers no longer compete among themselves to lower their prices to foreign buyers who had found it more profitable not to compete with each other for the New Zealand supply.

### ***5. Firms are treated as international allies***

Global firms are now recognised as the prime intermediaries switching resources and services between New Zealand and other countries, and New Zealand treats them as allies, no matter where they are domiciled and what their actions. New Zealand has introduced low flat tax rates on corporate profits taken in New Zealand and on incomes of those involved in services carried out here. Only a few small tax haven states, such as Bermuda, remain below New Zealand in the rates they

impose. As tax rates have been lowered, more multinational service functions have been moved into the hands of New Zealand specialists while global firms take more profits in New Zealand and invest more heavily. The re-nationalisation of digital telecommunication services and its free provision to users have given service firms located here a tremendous advantage, and made New Zealand the envy of the world as a communication paradise.

On the other hand, global firms have shown themselves always ready to switch physical production out of New Zealand, in their search for the highest corporate value. Those who did not do so have been beaten by other global firms and their values have declined. Even firms domiciled within New Zealand have found that they have had to relocate functions overseas when they can gain competitive advantage or remove disadvantage by so doing.

### ***6. Services to multinationals are predominantly multinational services***

Apart from direct production input, many opportunities have emerged for providing high profit yet competitive input to multinationals, and services of a specifically multinational nature have grown astronomically. Multinationals have avidly purchased multinational knowledge. They have found it more economic to obtain knowledge services from service firms able to spread the cost over numerous clients, than to attempt building it slowly and expensively themselves from multiple national sources. One multinational has needed advice only once about the interaction of United States, Bermudan and Chinese law relative to a supply investment in China. A New Zealand law firm with highly trained bi-lingual Chinese legal staff, offering its service to multinationals worldwide, was its sole source for this advice.

Similar multinational services have emerged for functions as varied as planning global marketing strategies, developing global advertising, global public relations, product design, international financial reporting, recruitment and logistics. And New Zealand service firms have discovered that the more they offer these services, the more their knowledge accumulates and the more difficult it has become for others to unseat them from their global leadership. License income to New Zealand inventors and developers has grown to very high levels as the number of patents registered to New Zealand residents has increased and inventors have discovered it more lucrative to license foreign producers and marketers than to enter as competitors on their own account.

### ***7. Services to non-resident individuals are predominantly for cross-nationals***

New Zealand service firms that have tried to offer services globally to private customers have found it difficult to expand from a New Zealand base because extensive and expensive “on the ground” representation is generally required in the countries where the customers reside. When the customers themselves are cross-national individuals, however, services

offered from New Zealand have been more successful. The customers themselves cross national borders in order to seek the service from New Zealand. They are invariably among the more wealthy individuals in their countries with a motivation to maximise net wealth and minimise risk. Cheaper health and education services, higher investment returns, greater security, and lower taxation have all attracted such individuals to seek services in New Zealand rather than from “service providers” in their own or other countries.

The value of New Zealand’s educational and cultural heritage as a supply of international value has resulted in significant inflows of foreign residents coming to New Zealand for educational purposes. Foreign residents long ago became the majority within New Zealand’s education system. The value from creating a leading multinational university country as never before achieved has also carried across to many other areas of New Zealand performance. New Zealand resident students themselves have become more capable of dealing with multinational issues as curricula have become more multinational in their orientation.

Services appealing to the worldwide propensity to travel to centres of excellence for medical advice and surgery also proliferate in New Zealand, with major impact on the design of hospitals and associated accommodation facilities for those who accompany patients. Incomes of medical staff have risen significantly and New Zealand has become the preferred destination for many seeking careers as leaders in medicine.

With a population that has the highest number of qualified accountants per capita, stable legislation, clear tax rules and an established culture of fair treatment, New Zealand has also become a leading country in the provision of services for formation of companies and trusts, and in investment and estate management.

### ***8. International financial services have flourished***

New Zealand long ago merged its stock exchange with Australia’s and adopted the Australian dollar as its currency and makes no pretence of being a financial centre. But it has become a centre for international financial services. Without its own currency it has been able to grow at a much faster rate and allow its prices and incomes to rise faster whilst avoiding devaluation the moment that local inflation occurs.

It was New Zealand’s time zone location that supported its first flush of international financial services designed to continue the operations of European and North American financial markets while they slept. Advanced models for financial intervention are now as likely to be developed and utilised from New Zealand as they are from the Northern hemisphere. This expertise has led to the expansion of New Zealand domiciled funds and other financial investment vehicles – all reinforced by a favourable taxation environment and the multinational knowledge that has accumulated in the country.

Specialist New Zealand financial expertise has begun

to erode the business of foreign financial institutions that tried to replicate and monopolise conventional single-country financial services on a global scale. The market for identification and evaluation of merger and acquisition possibilities worldwide has been stolen from merchant and investment banks that could not provide multinational risk and taxation assessments. New Zealand now harbours many advanced specialists who can provide penetrating reports and valuations faster than any other source worldwide. New Zealand has even led the way in creatively tapping sources of finance in developing countries appropriate for global firms wanting to tie funding to their operations in such countries.

### **9. New Zealand's professional qualifications are multinational**

New Zealand professions first offered courses overseas as education for their qualifications shortly after the turn of the millennium. Year by year, they extended their examinations to include more and more knowledge of foreign conditions and legal requirements, established their own foreign branches, and licensed foreign institutions to carry out education on their behalf. Of all the countries whose professional institutions began to extend overseas, New Zealand was the first to see the advantage of offering multiple country and cross-country qualifications, and residents of less-developed countries in particular flocked to gain the accreditation offered by the New Zealand societies – whether they were in law, medicine, accounting, surveying or a dozen other professions. The worldwide diaspora of New Zealand professionals gave an impetus to local recognition in a hundred cities and it now has local accreditation, local branches and local visibility second to none. Four of New Zealand's chartered bodies are the world's leaders in their fields both by size and reputation.

### **10. New Zealand has become a life destination**

New Zealand has become an attractive residence for wealth. With education, weather, scenery, space, leisure and a stable low-tax economy, New Zealand has increasingly attracted many of great world wealth. New Zealand has become a life destination. Its distance from highly populated countries and slow immigration led it to preserve its wilderness and seashore better than most countries so that services using New Zealand location have flourished at relatively high prices. Populations worldwide now place New Zealand as their number one destination for long-term tourism. Industries associated with New Zealand's natural beauty have also flourished. Art and cinematography with scenic beauty as a backdrop are a leading source of income and culture.

While New Zealand exported head offices for decades, it has now reversed this flow. Wealthy managers are finding reasons for retaining head offices in New Zealand or moving established firms from abroad to take advantage of the country, its culture and its taxation for those in control positions.

### **The way ahead**

Backwards induction from these ten characteristics of New Zealand as a number one country immediately suggests some actions that would almost certainly go a long way towards achieving them. Other actions are less obvious. For instance, the reduction of direct taxes on the incomes of New Zealand residents and a corresponding increase of indirect taxes in the form of higher product sales taxes, which would largely hit the output of overseas residents, seems a fairly obvious strategy. Less obvious would be the choice of alternatives for creating a globally leading education sector. Should it be achieved through funding the most outstanding foreign postgraduate students to study in New Zealand because a substantial number of those not selected would follow them? Should it be achieved through encouraging universities to set up foreign feeder campuses? Should it be achieved through enrolling disproportionate numbers of postgraduate students, as have Harvard and MIT? Should the universities play a significant role in education for professional qualifications as they are extended internationally? Whatever the paths chosen, however, the over-riding consideration is the ultimate strategic advantage to New Zealand residents in that they will be able to command higher incomes from the services that they provide. Some of these services will be what are offered by those employed in the education sector, others will be offered by graduates and postgraduates of high talent and education who choose to remain in New Zealand.

A coherent national strategy would require every government action, whether it is encouragement, guidance or legislation, to be weighed for its strategic contribution to the interests of New Zealand residents versus those of non-residents. Arguments for government intervention could no longer be couched in terms of internal politics divorced from how they would affect New Zealand's position relative to the rest of the world. Even further, however, government actions would have to be considered as integral parts of a coordinated strategy rather than as individual actions justified in their own right. Both of these requirements would change significantly the way most government actions are today framed and justified. Most are justified individually, and with no mention of their strategic significance vis-à-vis other countries.

The planned changes in tax law that will impose profits tax on the deemed disposals of assets of companies that migrate from New Zealand is an example of a move apparently introduced without strategic consideration.<sup>8</sup> In introducing the proposed legislation, the IRD states that the change is intended to remove incentives for companies to migrate for tax reasons. The law probably will achieve this objective, but it is doubtful whether it will collect significant taxation revenue from any but those who are now caught by the change in law. And the change is very likely to discourage the establishment of New Zealand subsidiaries of foreign firms, to lead foreign firms to invest less in New Zealand, to shorten

the period investment is left here, and to lead residents who might emigrate in the future to set up foreign companies rather than local companies for their New Zealand activity. The new law certainly could not be described as treating foreign firms as allies, nor foreign countries as competitors to be beaten. It decreases rather than improves New Zealand's strategic position.

Finally, there is the issue of the extent to which New Zealanders will be prepared to accept competitive strategy against other countries as the motivation for national actions. Some are unlikely to accept that doing better almost always means taking the revenue that others aspire to – that while the world is not exactly a zero-sum game, any significant change in country GDP ranking will have to be achieved at the expense of residents of other countries. If a country never considers how to gain world leadership, and never grasps the opportunities to do so when they arise, however, it is likely to slip ever lower in the international income ranking – as New Zealand did for the best part of 40 years. The compelling case for a competitive country strategy is that when countries compete, the allocation of the world's output to final consumers reflects more precisely the value to other consumers of what those final consumers have themselves produced. When a country does not strive to compete as well as it might, its residents have little justification for any belief that they have been treated unfairly in the division of the world's output.

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Damien Kurth, Glass, 2004, oil on canvas. Elam School of Fine Arts.