

The New Zealand Institute of Economic Research

Its Role in Achieving Asia-Pacific Partnerships

By Gary Hawke

Leading Role in Public Discussion on New Zealand's 1st FTA

New Zealand has been active in trade agreements for nearly 50 years, much longer than they have been fashionable in international economic diplomacy generally. Free Trade Agreements (FTA) have grown astronomically since the 1980s with few countries now not involved in their proliferation. Previously they were unusual, but New Zealand has used them as a tool of economic strategy since the 1960s. The New Zealand Institute of Economic Research (NZIER) was founded in 1958, in time to play a leading role in public discussion before New Zealand's first modern FTA with Australia.

New Zealand was one of the economies that W. W. Rostow, in his *The Stages of Economic Growth: A Non-communist Manifesto* (CUP, 1960), termed "born free" economies, namely those which became developed without being industrialized. Its exports were predominantly agricultural and although the population was mostly (small-town) urban since agricultural exports required processing and much support from services, the basic political economy was taxing agriculture to support other activities. In the 19th century, New Zealanders sought "development" in the sense of building the range of activities of a modern society and economy while maintaining average living standards above those of the United Kingdom. Modest protection was one of the tools used to facilitate establishment and expansion of a range of urban employment opportunities. In response to the Great Depression of the 1930s, further "insulation" was sought from fluctuating international markets, and a welfare state was instituted. Import licensing and exchange controls were used to protect local industry which was substantially concerned with using imported capital equipment to process imported inputs. The exchange rate was maintained at a level which had the effect of moving resources from agriculture to the rest of the economy.

After World War II, this pattern was assimilated into international thinking about import-substitution industrialization, but the essential policy really remained shifting resources from agriculture so as to provide employment opportunities for New Zealanders whatever their interests and aptitudes.

In the 1950s, New Zealand was not an enthusiastic participant in moves towards liberalization. Imports remained subject to quantitative licensing to protect local processing. The early GATT rounds were criticized because they did little or nothing to promote markets for agricultural exporters.



Author Gary Hawke

New Zealand's rate of economic growth was slow in the 1950s, and while this was largely attributed to discrimination against agricultural exports in international markets, it was realised that the world was not going to change to accommodate New Zealand's interests. The policy response was to seek faster growth by diversifying export composition and markets. New markets were sought outside the slow-growing UK, the agricultural products exported became more varied, and new exports were added, the so-called "non-traditional exports". Forest products were prominent, the result of a great deal of forestry plantations created from the 1930s, but various manufactured products were also included. A good deal of diversification of export products and markets was achieved, although the rate of economic growth remained modest.

NZIER was founded in 1958 in an endeavor to promote well-founded public discussion of economic developments. It was supported by public sector funding but was independent and relied on private sector subscriptions and eventually consulting income. Among its earliest publications was a discussion of the merits of freer trade with Australia (*Should We Have Free Trade between Australia and New Zealand?* F. W. Holmes, NZIER Discussion Paper No. 1, 1961). NZIER economists contributed significantly to public debate over the balance which would result between gains from better resource allocation from free trade and the costs imposed by adjustment of New Zealand industries to competition from Australia, especially the social changes involved in abandoning the historic "development model" of taxing agriculture to support other avenues for employment. NZIER was especially prominent in seeking to relate the pace of liberalization to increased ability for New Zealand manufacturers to compete with Australian firms.

A limited FTA was signed with Australia and came into force in 1965; the New Zealand Australia Free Trade Agreement was generally known as NAFTA, it being some years earlier than the North American Free Trade Agreement which adopted the same acronym. It was largely driven by the need of both Australian and New Zealand pulp and paper firms to rationalize their assets and production on both sides of the Tasman Sea, and although it reduced some other tariffs, many were close to zero anyway. It also included a specific provision whereby licenses for imports to New Zealand were linked



A selection of NZIER publications

to exports of industrial but not necessarily closely-related products to Australia. Officially Article 3.7, this was familiarly known as the “panty-hose for Holden” clause, Holden being a marque of the Australian motor industry and the New Zealand clothing industry still trying to sell a full-product range. The provision was an interesting and worthy attempt to establish an adjustment path which permitted economies to move closer to an optimal resource allocation while moderating the impact on manufacturing employment, and NZIER can be proud of its role in its development even though what was enacted was a pale shadow of what was proposed. In practice, it was impossible to distinguish a development tool from a mere modification of traditional protection. Its effect was small and probably counterproductive, being more protective than adjustment-facilitating, and it was eventually abandoned.

From NAFTA to CER

NAFTA provided for annual ministerial consultations, which added a few minor products to its coverage, but generated a great deal of dissatisfaction. By the late 1970s, Australian ministers especially were unwilling to devote time to a largely fruitless ritual. NAFTA had either to be modernized or abandoned. After a good deal of hesitation by politicians, who were still apprehensive about possible consequences for employment and who were worried about the political impact of removing protection from their supporters in organizations like the Manufacturers’ Federation, NAFTA was replaced by the 1983 Australia and New Zealand Closer Economic Relations Trade Agreement, ANZCERTA or CER.

CER was a much more thoroughgoing FTA than NAFTA had been. It covered virtually all trade in goods, and looked forward to covering trade in services as well. In 1983, a timetable was provided for eliminating tariffs (and quantitative restrictions) and for extending coverage to most services, and when the timetable was reviewed in 1987, liberalization was accelerated. CER was treated in New Zealand as much more than a trade agreement. Although the terminology of a “comprehensive economic partnership” had not been invented, CER anticipated its conception and dealt with issues like mutual recognition. Over time it became sensible to think in terms of a “single economic market” although with each liberalization step there were new boundaries to be discussed in an effort to determine what were justified differences between the economies and societies, and what were unnecessary barriers to trans-Tasman integration.

The relationship between New Zealand and Australia was unusual. They shared a great deal of history and many interests although they grew apart after a number of Australian colonies joined in the federal Commonwealth of Australia in 1901 while New Zealand stood aside and the relationship often had a prickly element of fraternal rivalry. The common history, however, left a legacy of free movement of people between the two countries so that economic integration had an unusually congenial context. CER attracted interest because much orthodox belief in the 1980s was that FTAs worked best between complementary economies whereas Australia and New Zealand were more competitive than complementary. Orthodoxy was also dominated by belief in an orderly progress from FTA to customs

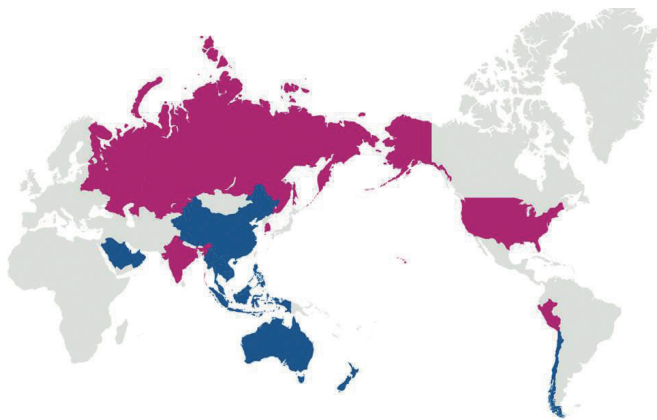
union (through a common external tariff) towards an economic union (through a single market) to political union. Australia and New Zealand did not develop a common external tariff, although unilateral reductions in tariff levels generally had some of the same effect. Ideas of a single economic market became influential, but influential work was focused on removing barriers to trans-Tasman cooperation and rationalization rather than the building of a common code with supranational institutions.

The process resulted from trial and error rather than deliberation; CER did not include an explicit disputes resolution system since ordinary processes of political and business discussion could (mostly) be relied on. It was relatively simple to provide for Australian legal processes to take place in New Zealand and *vice versa*, and the building of explicit trans-Tasman institutions could be chosen from a complete range of possible means of collaboration, ranging from informal discussion through negotiation to absorption. Ironically, before “the ASEAN way” became well-known in New Zealand, its precepts were practised in relations with Australia. The emphasis was on consensus and commitment, rather than on appearances. What was important to New Zealand was that the CER changed attitudes towards economic policy and it was relatively easy for New Zealanders to adapt to a thoroughgoing process of structural reform from the 1980s instead of being fixated on tariff levels and a discrete trade policy. Furthermore, it made New Zealand much more outward-looking.

Intellectual Contributions to FTAs

NZIER participated in debates about CER as it was formulated, and was even more prominent in discussion of its implementation and extension. By the late 1980s, public debate focused on liberalization more generally, including a possible free trade agreement with Canada, the United States, and more generally in East Asia. By 1993, when the Ministry of Foreign Affairs and Trade issued a formal statement of New Zealand’s trade policy, free trade areas were welcome. New Zealand’s top priority remained the multilateral trading system: the Uruguay Round had changed the situation in which GATT did not engage in a major way with agricultural trade. But New Zealand trade policy included a willingness to contemplate a free trade area with anybody who was willing to conclude an agreement which was compatible with WTO requirements, and in particular was “comprehensive” – i.e. did not have unreasonable exclusions or special provisions relating to agriculture.

That policy has remained unchanged throughout several different governments. A range of agreements has been completed and added to CER: New Zealand-Singapore Closer Economic Partnership (2001); Trans-Pacific Strategic Economic Partnership (P4 Brunei, Chile, New Zealand, Singapore) (2005); New Zealand-Thailand Closer Economic Partnership (2005); New Zealand-China Free Trade Agreement (2008); ASEAN-Australia-New Zealand Free Trade Agreement (2010); New Zealand-Malaysia Free Trade Agreement (2010); and New Zealand-Hong Kong, China Closer Economic Partnership (2011). Further possible agreements are at various stages with the Gulf Cooperation Council; Russia, Belarus and



FTAs under negotiation
FTAs already signed

Source: New Zealand MFAT

Kazakhstan; India; South Korea; Japan; the Trans-Pacific Strategic Economic Partnership (TPP) which currently involves 11 participants; and RCEP, which involves the 10 members of ASEAN and its six FTA partners. Furthermore, specific extensions are being negotiated, such as a New Zealand-Hong Kong Closer Economic Partnership Investment Protocol.

NZIER continues to participate in trade policy debates. It does so through its consultancy work for both government agencies and the private sector, as well as through self-funded research as part of its Public Good program. Short, non-technical pieces on topical trade and regional integration issues have been published under this program in order to inform the wider public and provide an independent and impartial view to counter some of the rhetoric from more vested interests in the media.

Nature of NZIER's Contributions to Trade Policy

Whereas the earlier contributions were generally discussions of strategy informed by economic reasoning, more recent contributions have tended to be modelling exercise, either computable general equilibrium or gravity models. The earlier form persists, but specific modelling exercises are more common and are often commissioned so that the results are confidential. An early example was a 1994 report on the possibility of an FTA with Chile, while there have been several reports on specific aspects of potential agreements with Japan and with South Korea. Several aspects of the FTA with China were also investigated, as were questions of services trade with, for example, Malaysia. The then director of NZIER was a member of a working party which developed the Closer Economic Partnership for East Asia and NZIER has also investigated aspects of East Asian integration for the Ministry of Foreign Affairs and Trade (MFAT). Like modelling exercises generally, the NZIER reports have found positive benefits for New Zealand, with benefits increasing the wider the proposed coverage and the greater the number of economies involved. Modelling exercises, however, have the merit of taking explicit account of interdependencies which are not obvious and they also make transparent where in the economy adjustment problems

are likely to be encountered.

NZIER is not a participant in negotiating FTAs. The Trade Negotiations Division of MFAT has prime responsibility for negotiations and it is supported most by officials from other sections, especially Trade Analysis and Policy and Economic Divisions (under various names), and from other departments such as Treasury, Health and Customs depending on the issues under debate. NZIER contributes specific knowledge. Making negotiated agreements fruitful, however, depends on an understanding of their potential results, especially but not only in the New Zealand business community. Helping New Zealand firms understand the many, often overlapping FTAs in existence has become an increasingly important part of NZIER's role in the trade policy debate. What was especially notable about the New Zealand-China Agreement was not only its symbolic character as the first between China and a developed economy, or even its strategic significance as part of the re-emergence of China into participation in global leadership, but also the way that New Zealand business became informed about that process. Protectionist attitudes towards China have not been eliminated, but major steps were taken into helping New Zealand business formulate a strategy for participating in global growth rather than sheltering from it. Significant steps were taken toward conceiving rules of origin as instruments for participation rather than as protectionist devices. The impact of CER in shifting understanding from trade barriers to economic strategy was brought up to date in the modern world.

The educational campaigns were led by officials, but NZIER assisted, not only by specific reports and publications but also by the tone and intent of its numerous communications with business, especially but not only its members, as it publicized apparently unrelated publications such as *Quarterly Predictions* and *Quarterly Surveys of Business Opinion*. NZIER's key comparative advantage in the trade policy debate is its independence: it is able to say things publicly that government agencies might want to but cannot due to political constraints, but can also criticize government policy with a view to promoting changes that would improve the business environment, productivity and living standards. This gives its research credibility with both policymakers and the business sector.

Although economic modelling has become much more sophisticated over time, it is still much more able to analyze trade in goods than trade in services and its treatment of deeper aspects of integration remains somewhat simplistic. That is true even of investment let alone such issues as intellectual property regimes, standards conformance and mutual recognition, and nontariff measures which greatly affect the ease of doing business. The future agenda of NZIER remains large.

JS

Gary Hawke is emeritus professor of Victoria University of Wellington and senior fellow of NZIER. He was formerly professor of economic history (1971-2008), director of the university's Institute of Policy Studies (1987-1997) and head of the School of Government at VUW (2003-2008). He is a member of the board of the New Zealand Committee for Pacific Economic Development and a member of the Academic Advisory Council of the Economic Research Institute for ASEAN and East Asia.