

# All change. Destination 2020s

Colin James to Deer Industry Conference, Wellington, 16 May 2019

## 1. A decade of change ahead

- Global politics, trade and economics are in flux. Digital technology is coming of age and bringing societal change. These trends destabilised the 2010s and will intensify in the first half of the 2020s.
- This disorder poses a major challenge to New Zealand and its government led by younger-generation ministers. Are they up to it?

## 2. Global reordering and instability

- The world is in a period of substantial change, economically, politically and technologically. This is more likely to accelerate than decelerate during the 2020s.
- **Globalisation** is in a new phase. Global trade in merchandise products which for some decades expanded faster than global GDP stalled for a while after 2008 and has picked up only to the same expansion as global GDP. Three main reasons: (1) China is consuming more of its own manufactured good as it enriches; (2) advanced economies have been "re-shoring" production by using automation, including robotics, which can match the production costs of long, complex global value chains and respond more quickly and with more precision (customisation) to consumers' wants and needs; and (3) a rise of protectionism and decline of the World Trade Organisation's influence and capacity to resolve disputes.

At the same time, *digital services* continue to globalise because such services can be done by anybody with the requisite skills anywhere. This activity operates through networks rather than global value chains.

These services form part of the processing of manufactured products and software is an increasing element of manufactured products.

*Global finance* continues to integrate and increase its share of the global economy. This leaves individual economies more vulnerable to changes in the currents of global finance and to future shocks of the sort experienced in 2008.

Another globalisation over the past three decades has been of people: *mass migration*, some of it forced by war. Around 250 million people live outside the country they were born in.

- The **global economy continues to rebalance** as China and other mid-level economies enrich and expand. China's One Belt One Road aims to extend China's reach across and influence in central Asia to Europe, the Middle East and Africa and down through south-east Asia – and, eventually, beyond. China is massively investing, and lending for investment, in infrastructure in central Asia, Pakistan, Africa and the South Pacific.

This is generating tension with the established liberal-capitalist economies of the post-1945 era, notably the United States and Europe – but also, with respect to South Pacific island countries, Australia and New Zealand.

It is also a potential source of geopolitical instability as China's loans to poor countries from Belt and Road and other infrastructure increasingly become unrepayable. Analysts estimate Djibouti, Kyrgyzstan, Laos, Maldives, Mongolia, Montenegro, Pakistan and Takistan are in or near default. Add to that list two Pacific states, Tonga and Vanuatu.

- Within **developed economies** there has been over the past 35 or so years a **widening of wealth (and income) disparities**. The top decile has a far greater share of national wealth than from 1945 to 1985. Real wages for the "middle" have stalled or grown very slowly, reducing wages'/salaries' share of total income.

Very loose monetary policy has fed this disparity by **expanding credit**, much (most?) of which has not gone into productive investment but has accumulated in the hands of the better-off and best-off. One result has been that **financial and housing** asset prices have risen far faster than median incomes. Overall global debt more than doubled from 2007 to 2017 to be 236% of global GDP.

- The **political response** in developed economies has been voters' desertion from the established centre-left and centre-right parties which had governed since 1945. Even where the old parties may seem still be running the show, as in Britain and the United States, they are seriously splintered.

Many people have backed various forms of **populism**, mixes of nativism, nationalism and nostalgia. This has grown out of **resentment** at self-perpetuating **privileged elites** who benefit from the new order and are seen as self-interested and out of touch with "real" people, who are, or see themselves as, disempowered and/or disoriented and/or see themselves as foreigners in their own land threatened by immigration the elites have allowed or encouraged.

The most extreme forms have been United States President Donald Trump's erratic personalised rule and Britain's Brexit mess. The previous global trend towards liberal democracy has reversed. Autocracy has gained ground in the likes of Hungary, Poland and Turkey. China and Russia are in effect fascist.

One **alternative to populism** has been attachment to **macro-personalities** who transcend traditional politics and divert resentment. Examples: Justin Trudeau in Canada and Emmanuel Macron in France – and Jacinda Ardern here. Trudeau and Macron have both run into trouble.

A **second alternative** is the demand by growing numbers of **under-30s** in developed economies for **radical reforms** to reduce inequalities of wealth and opportunity. They see established centre-left parties as ineffective/out-of-touch.

Add to them older folk who yearn to return to the 1960s and have turned to **old-left** politicians such as Jeremy Corbyn in Britain (who might be the next Prime Minister) and Bernie Sanders in the United States. There are similar currents in some European countries.

(There is a parallel in China where some young people protest that Xi Jinping, by allowing big inequalities of power, privilege and wealth, is debasing "Marxist thought" which he has proclaimed to be the guiding philosophy.)

- Accompanying these disturbances has been a **first-principles search** by commentators, academics and some politicians and officials for **different policy settings**. International commentary in serious media such as the *Financial Times* has increasingly featured this commentary.

This commentary is *challenging the economic orthodoxies* of the past four decades, notably:

- the tight focus on gross domestic product (GDP) growth as the primary indicator of how well a country is doing; the challengers insist the state of the environment, social cohesion and personal development and satisfaction are also important indicators; viz the New Zealand government's exploration, led by the Treasury, of "wellbeing economics";
- central banks' obsessive focus on inflation (which digital technology may be making less reliable as a measure of costs of living) and the resultant massive rise in global debt and asset prices;
- how and what globalisation now is (*see above*);
- the purpose and conduct of corporations, the shareholders of which are now mainly investment banks and hedge funds which have a narrow, short-term focus on what constitutes success;
- the role and relevance of economics and economists and the need for injection into economics of other disciplines; and
- regulators' capability to respond to new technologies quickly and relevantly.

A major problem for reformers: there is *no ready-made alternative* sitting on the shelf, as Milton Friedman and other free-market economists had ready for adoption when the Keynesian model came under stress in the 1970s. In that absence, some reach back to earlier times for "solutions" which don't work now.

Moreover, this lack of clear direction comes at a time when countries that are not liberal democracies are pushing different theories, for example, China.

- Add to this global turbulence the risk of a **disjunctive shock**, heightened by the political turbulence and rebalancing. Past such shocks include the first world war, the 1929 stock market crash and the 2008 global financial crisis.

There is increasing commentary in serious media worrying about another *financial system shock*, which could be much worse than the 2008 one because of the huge rise in global company, personal and government debt since 2008.

Other potential shocks are *environmental*: water shortages, crop failures because of extreme weather events and the impact of climate change.

At the extreme end, these could provoke *violence* and wars, both within countries and between them.

- **IMPLICATION FOR NEW ZEALAND**: Big countries can tough out international disorder. Small countries have to rely on skilful navigation or attachment to a big player. New Zealand's economic over-dependence on China but values-alignment with Europe and north America poses a difficult choice if one has to be made.

At home, if there are serious economic impacts, populist reactions could upset our politics and generate ad hoc, reactive policies.

The experiment with "wellbeing economics" offers a way of anticipating and responding to the challenges and even possibly softening the impact.

### 3. Technology change in the 2020s

- **Digital technology** is now coming of age. Artificial intelligence (AI), including robotics, will have a major impact of many agricultural and manufacturing processes and on ways of living, from medical diagnoses drawing on all known diseases and conditions to driverless vehicles to more efficient harvesting of fruit.

This is likely to have a major effect on "work".

It is also destroying privacy, at the hands of corporations and governments (note particularly China's social profiling). Public reaction, including to the mega-corporations such as Google and Facebook, will intensify in the 2020s.

- **Artificial** (plant-based and animal-cell-based) **protein** is in its early stages. Assessments of where it will take us in the 2020s vary from not far to major changes in diets and supplies of food. In any case the impact on animal-based protein will be limited in the first half of the 2020s.
- **Gene editing** is also in its early stages. It has large potential: for good, for example, in anticipating, preventing and dealing with medical conditions (not least, through precise targeting of cancer cells and new bacteria and virus strains) and development of new plant and animal strains; and for bad, for example misuse against dissidents by autocratic governments.
- **IMPLICATION FOR NEW ZEALAND:** Through the 2020s AI etc will pose opportunities and threats and drive social change, likely sharpening the divide of attitudes and values between younger generations and older generations. Alternative sources of protein and gene editing are likely by the end of the 2020s to be affecting agriculture, horticulture and aquaculture. If so, having a top national brand may become more important.

### 4. Planetary limits and social change

- **Water** is becoming scarce in some major economies, not least India and China. New technologies and better management can make supplies go further. But there are limits to those and climate-change disruption of monsoon seasons doesn't help.
- **Pollution** of air, sea and land is worsening, damaging and in some cases destroying ecosystems. Again, science and better management can offset these effects but again there is a limit.
- **Climate change** is speeding up, evidence suggests. One impact is disruption to weather patterns plus extreme weather events, affecting crops. Another is sea level rise, threatening coastal cities, which house a rising proportion of the population.
- **Pandemics** are possible – some say likely – sometime in the 2020s, driven by antibiotic-resistant bacteria or new viruses.
- **Generational change** is under way. The post-1945-born generation, which dominated liberal democracies – and through them much of the world – up to around 2000 is being replaced in power by those born in the 1970s and 1980s. The next generation, now in its 20s or younger, are growing up in a different world, with different threats and opportunities and during the 2020s will increasingly make themselves felt, even by 2025.

- That generation will have to come to terms with **planetary limits** to human production and consumption. This coming to terms could be done well but is more likely to involve conflict, potentially very destructive, if past eras of human existence are a guide. This coming to terms may, however, be after the 2020s.
- **IMPLICATIONS FOR NEW ZEALAND:** We trade on clean/green but don't carry it through in practice. That will generate challenges for the 2020s which growing numbers here recognise and are anticipating with action. As a lightly populated place, New Zealand is likely to become increasingly attractive to people in Asia. How we, as a small, defenceless country, will deal with that demand will likely become a significant issue in the 2020s.

## 5. The good news is...

- ...that we humans have half a decade or so to begin adjusting to the new global environment and its threats and opportunities. New Zealand's distance (not as distant as it was, thanks to global connectedness) might make it an ideal place to work out those responses.

And we have time. The first half of the 2020s may not be too much different from the last half of the 2010s.

## 6. The Ardern government

- Compared with other liberal democracies, **New Zealand has been in a bubble**, first under the Key-English government and now under Jacinda Ardern's. Winston Peters has been soaking up what populist reaction there is and he is not the firebrand he once paraded as. This bubble has been nurtured by a reasonable-to-good economy.

In this bubble the centre-left (Labour) and centre-right (National) continue to dominate Parliament – unlike in other liberal democracies (*see above, p2*).

But bubbles are not hermetically sealed. A pinprick can let out the air. Labour is not the force it was and probably would have ended up in 2017 in the low-20s (like other social democratic parties in proportional systems) if Ardern had not flashed on the scene.

Ardern is a **macro-personality**. Her handling of the Christchurch shooting has added lustre. She connects, she is empathetic, people feel comfortable with her and she is different from what went before.

- Ardern bills herself as "youth-adjacent". That is appropriate because the 2017 election marked a **generational change in Parliament**. As a result of the 2017 election the number of MPs under 40 rose from 13 just before the election to 25, one-fifth of Parliament. Add in 40-45s and the total was 37%. In 2018 two more were added: Nicola Willis (35 in 2017) replaced retiring Bill English and Agnes Loheni (45 in 2017) replaced retiring Steven Joyce.

The 2020 election will take that cohort comfortably over 40% of Parliament and by 2023 it may well be a majority.

The cabinet's key ministers are predominantly people clear of the baby-boom generation and its long shadow. (Winston Peters, 74, is a standout exception.)

The rising cohort has had markedly different life experiences, including the impact of digital technology and wealth inequalities, and so thinks differently from those who have dominated governments since 1984.

- **Ardern is not stardust.** She is intelligent – not super-intelligent but well up to handling the complexities of her role. She has a good intellect, fully capable of mastering foreign and domestic affairs. She is tough and firm, with a solid moral base. A telling off from her hits its mark – and she does that without being nasty.

That adds up to **substance**. She is not Prime Minister by mistake or chance. She can do the job. She has authority. An early example was her firm stance at the first cabinet that the Trans-Pacific Partnership deal had to be done, if possible.

Doing the job includes managing the **first genuine three-way government** under MMP. She has insisted all matters have to be cleared with the partners. New Zealand First works off a 300-page summary of its pre-election policies to position itself and negotiate. The Greens have pent-up ambitions far in excess of their numbers. These three factors have (a) slowed a lot of decision-making, (b) narrowed options and (c) killed off some grander ambitions and/or postponed them till after the 2020 election. One minister puts it this way: no more "new" initiatives this term beyond work in progress.

Coalition management is complicated by the **fiscal responsibility rule** agreed with the Greens before the 2017 election. Ardern calls sticking to that rule "earning a licence to govern". That has shaved social policy ambitions.

Ardern has proved **capable of intervening** in ministers' portfolios, not least in foreign affairs where she doused Winston Peters' enthusiasm for a free trade agreement with Russia, his musing in Washington about a free trade agreement with Donald Trump (which, as MFAT would tell you, is a matter of being careful what you ask for, given that Trump's idea of a deal is that he has to win) and in mollifying China, including supporting the Belt and Road initiative.

- **Grant Robertson** (long-term colleague and personal friend of Ardern) is the **effective No 2**. He has grown into the job, Treasury says.
- There is to be a **cabinet reshuffle in June**. It is badly needed. David Parker (trade, environment, economic development, Attorney-General and associate finance) and Chris Hipkins (education, state services, ministerial services, leader of the House of Representatives) have impossible workloads.

Problem: Who can take on some of that work? The middle-ranking ministers are not star potential. Phil Twyford's outsized transport and housing ambitions have had to be scaled back to reality. David Clark is struggling to assert authority in health to match his high intelligence. Megan Woods has yet to match potential with results, though does have the complication in energy of dealing with Greens who have very different ideas. Carmel Sepuloni is a plodder in social welfare. Kelvin Davis: ho hum – but he is said to go well on marae.

Two Labour ministers who have clearly measured up are Andrew Little and Kris Faafoi. Nanaia Mahuta is a quiet achiever.

The top-performing **New Zealand First** minister is the low-profile Tracey Martin who gets inside her children and seniors portfolios and has a clear idea of where to go. Shane Jones is a real risk to the government in the way he handles his regional slush fund (though there are some positive stories) and his rash

comments. Winston Peters has MFAT's respect, for example, backing the important South Pacific reset, and still can make personal connections but is not the man he was when Foreign Minister with Helen Clark.

**James Shaw** was slow to get real progress on climate change but that is because he insisted (so did Ardern) on getting New Zealand First aligned with the net zero carbon legislation and on trying to get National less resistant. Shaw could personally quite easily work with National but that would mean leaving his party which won't have a bar of National. **Julie-Anne Genter** is having real influence in transport, bringing urban form issues to the portfolio. **Eugenie Sage** is periodically cited as intransigent by Labour ministers.

Whom might Ardern bring into the cabinet and ministry to fill the two spots left by Clare Curran and Meka Whaitiri? There is reason to give Whaitiri another go, having done her penance, and Ardern sort-of hinted at her press conference on 6 May that might be possible. For real ability Ardern would have to reach down to new MPs (Michael Wood? Deborah Russell? Ginny Andersen?) but that would be unusual. The good news for Ardern for the *second term* is that those three and others (Jamie Strange, Kieran McAnulty, Jan Tinetti among them) could grow into ministerial, then cabinet roles.

## 7. The policy direction and ambition

- There are **four policy dimensions** to the Ardern government's **first term**.

**One dimension** is to **fix up what it considers is wrong or has been neglected in health, housing, education, social assistance and workplace relations** and plug some other gaps, including in the arts and **regional development**. This is traditional-Labour and becoming-traditional-Green stuff. Much of it also fits New Zealand First inclinations.

So far there is little to indicate the social policy adjustments will meet the different needs of the 2020s. For example, the 19 education working groups, committees etc listed by the Ministry of Education focus essentially on fixing what Labour and various interest groups think has got out of kilter in the 2010s **education** system. The initial response to the **welfare** working group on 3 May was modest, again more geared to alleviating stress than genuine, deep reform. And because welfare is inextricably tied up with tax, separating the two leaves the government stuck with piecemeal policy, not real reform.

However, there is an attempt to ensure a "**just transition**" to a lower-carbon economy: jobs and business opportunities to replace those in the petroleum industry. (*See below for whether it might be taken further.*)

A **second dimension** is to reshape **Maori-Crown** relations, with less deference to iwi leaders and more attention to flaxroots leaders of urban marae, iwi not-for-profits and other pan-Maori or whanau groupings, which is in keeping with Labour's focus on lower socioeconomic strata. Kelvin Davis is setting up a new Maori-Crown agency with a government-wide brief but it is too soon to get a clear idea of how it will operate differently from existing agencies. Ardern has a disproportionate number of Maori in her ministry, even after Meka Whaitiri's sacking. She doesn't want to leave room for a new Maori party.

A **third dimension** is **reform of the public service** to operate more flexibly and

more cooperatively across agencies – and to be more proactive, freer with advice and more open. This is critical to the success of "wellbeing economics" (*see below*).

The *fourth dimension* is its **three big ambitions**: tax reform, climate change and "wellbeing economics".

- (1) Ardern **backed off serious tax reform** during the election campaign in 2017 and again in April, responding to the tax working group's final report. She ruled out taxing income from *capital gain* on the basis that there is no mandate but she made clear she would *not try to create a mandate* even when free of New Zealand First's blocking in the current coalition. This has upset many on the left and those who think the tax system should be genuinely broad-based (and, if so, income tax rates could be reduced). Likewise, the government's response to recommendations to introduce **environment taxes** got "consider for inclusion in work programme" responses. This tentativeness on tax might help tip some votes to the Greens or Opportunities party or some other left grouping in the 2020 election. Again, environment taxes could be offset by lower income tax rates or lower GST (also ruled out in the current term).

There remains, however, a possibility a *second-term government*, if there is a Labour-Green majority, could opt for environmental taxes, not least to help make progress towards the climate change objective.

- (2) **Climate change**, Ardern said in the 2017 campaign is her generation's "nuclear moment". That refers to the Lange Labour government's nuclear ban – but whereas Lange acted quickly and decisively and built a mandate, Ardern took her time in line with her insistence on full coalition agreement on all measures. The resultant legislation provides a framework rather than a certain pathway, leaving the Climate Change Commission (which National backs) advisory only and relying heavily on trees and still to some extent on foreign emissions reduction units. Also only modest steps have so far been taken on complementary measures, such as electric vehicles, industrial heat and heating office blocks and other large buildings.

However (a) *more* is to come *this term*, for example in renewable energy and (b) in a *second term* Ardern might become more assertive, especially if she has a majority with just the Greens. One factor some ministers push is protection of the national "brand". They say that brand could fray if New Zealand falls behind the play on climate change and affect tourism and primary products positioning at the high end of the market.

A **subsidiary element** is the potential for the "**just transition**" (developing new businesses and jobs as fossil fuels are wound down) to be extended into a more general transition as artificial intelligence and robotics change the nature of "work" in the 2020s – the "gig" economy and so on. Certainly, Ardern sees it that way and Grant Robertson led a two-year commission looking at "the future of work" while in opposition.

- (3) "**Wellbeing economics**" has the potential to change the way the government develops future policy initiatives. It was developed by the Treasury from mid-2015 and Ardern and Robertson gradually came to realise it could fit Labour's hope for policy renewal. The thrust of "wellbeing economics" is to

assess economic success (and fiscal success) not just on whether financial and physical capital is rising or falling but whether natural, social and human capital are rising and falling.

The *2019 budget* is the "wellbeing budget" but it will be a long way short of genuine "wellbeing economics". Much of the problem is to get reliable numbers against which to judge whether those other capitals are rising or falling. This will take well into a second term and maybe need a third term if it is to survive a future National-led government.

Why National might go along with it is that it ties in with the *social investment* approach developed by Bill English. That envisaged much *better cross-portfolio cooperation by government agencies*. The wellbeing approach can only work if there is such seamless cooperation. The public service is a long way short of working out how to do that successfully.

## 8. Who governs after the 2020 election?

- **Polling** over the past nine months or so has shown Labour generally competitive with National and Labour+Greens a majority on their own. But there are 16 months still to go, so that could change, possibly even substantially.
- One factor is **National**. So far, with the possible exception of education under Nikki Kaye and a more environment-friendly policy under Scott Simpson, National has scarcely moved from its positioning in the Key-English government, which essentially maintained the 1980s orthodoxies, with adjustments.

Simon Bridges has not (yet?) stamped a "youth-adjacent" change of direction on policy. Whether he leads the party into the 2020 election is unclear. Judith Collins, however, would be a step backwards, not forwards and, though she is trying to be a bit milder, would likely turn some centrist liberals and women over to Labour or Greens (as Don Brash did in 2005).

In addition, National has yet to find a partner which can get 5% or to which it can gift a seat. ACT is a dead man walking, possibly heading ACT for sub-0.4% overhang status reminiscent of Peter Dunne in his last term, or out if Epsom voters decide enough is enough. National has left it too late to woo New Zealand First and in any case Ardern is making sure New Zealand First doesn't have cause to jump ship after the 2020 election. (If it jumped ship during this term it would disappear at the 2020 election because 5 percentage points of its 7% vote in 2017 wanted it to go with Labour.)

But a National government in 2020 cannot be ruled out. (1) It might conceivably entice some New Zealand First MPs across post-election if New Zealand First is the third party and fears having less influence, though this is highly unlikely. (2) If both the Greens and New Zealand First were to fall under 5% (very unlikely) National might govern if it wins more seats than Labour because Labour loses votes to its left and/or if National were boosted by a populist partner to its right that gets 5% or is gifted a seat.

- **The Greens** should clear 5%. They have troops on the ground and money and have not (so far) made any big mistakes. The big sell James Shaw has to do is convince Green-type voters that real politics requires (a) compromises and (b) patience:

steps on the journey, not the whole journey in short order. The Greens are likely to be helped by any disappointment at Labour by its supporters that the government has moved too slowly and/or not far enough on its big ambitions, especially climate change, and/or has not put enough money into social services.

- **New Zealand First** may struggle to clear 5%, not least because only 5% of its support in 2017 wanted Labour. It sees its regional development activity as critical to its vote.
- If there is a Labour-led government, there are **four possible combinations**:
  - Labour+New Zealand First+Greens, with New Zealand First in second place, as now; Winston Peters would stay as Deputy Prime Minister but very unlikely for the whole term;
  - Labour+Greens+New Zealand First, with Greens in second place but all three needed for a majority; Winston Peters might stay Deputy Prime Minister for a while but not the whole term; Sir Winston goes to London or to high office somewhere;
  - Labour+Greens have a majority but Ardern keeps New Zealand First in the tent; again Winston Peters can stay only a short time as Deputy Prime Minister if at all (and Sir Winston gets appointed to high office somewhere); some decisions would be made against New Zealand First opposition but Ardern would likely limit those decisions to a very few;
  - Labour+Greens have a majority and New Zealand First goes out of Parliament. This frees Ardern to be more reforming.

The third and fourth look the most likely 16 months out. That is, there is a real possibility a second-term Ardern government would have **the option to be more reforming**.

- Can Ardern get a **third term**? Short answer: yes. Long answer: it depends on many factors, not least the degree to which National adjusts its policy to 2020s realities.

## 9. Is Ardern heading a "government of transformation" ...

- ...as she claimed in late 2017?
- The *evidence so far is no* – see the comments in 7 above. This is, so far, a reforming government, not (yet?) a transformative one.
- For this term that can be sheeted home to New Zealand First's restraining influence, for example on tax and climate change.
- But are Ardern and her cohort transformation-minded and might we see that in a *second term*? They are significantly and *possibly substantially reforming*, as the shift to "wellbeing economics" and move on climate change indicate. But so far that falls short of transformation, as, for example, was delivered by the Lange government in the 1980s.
- The Ardern-Robertson cohort are **more like a pivot** – *looking back* to the 2000s "third way's" aim for more equitable tax and social policies, adjusted a bit for modern conditions but not for future conditions, and *looking forward* to a different policy environment in its climate change and "wellbeing economics".