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The New Zealand Model of Economic Reform: A Review

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Brian Silverstone, Alan Bollard and Ralph Lattimore (eds), ***A Study of Economic Reform: The Case of New Zealand****, North-Holland, Amsterdam, 1996*

Lewis Evans, Arthur Grimes and Bryce Wilkinson with David Teece, 'Economic Reform in New Zealand 1984-95: The Pursuit of Efficiency', ***Journal of Economic Literature****, Volume 34 (December 1996), pp. 1856-1902*

THE recent flurry of publications by New Zealand economists about the recent economic reforms in that country is presumably a response to strong international interest. As David Henderson, formerly Head of the Economics and Statistics Department of the OECD, has pointed out, the New Zealand reforms undertaken since 1984 have amounted to 'one of the most notable episodes of liberalisation that economic history has to offer' (Henderson, 1995:13). He has since elaborated as follows: 'In no other OECD country has there been so systematic an attempt at the same time (1) to redefine and limit the role of government, and (2) to make public agencies and their operations more effective, more transparent, and more accountable' (Henderson, 1996:13). Yet the attention these reforms have attracted outside New Zealand has not all been favourable. A common view in Australia is that the New Zealand reforms 'exceeded the speed limits'. For example, Fred Argy (1996:93) claims that 'the short-term social costs of the New Zealand reform program have been so great that the overall welfare effects of the program are at best ambiguous and at worst negative'.

The publications under review make reliable information about the New Zealand reforms more readily accessible. The book edited by Silverstone, Bollard and Lattimore incorporates contributions from 19 economists from universities, research institutes and financial institutions. The editors aimed to produce a set of integrated chapters, covering economic outcomes, sectors and policies. Contributors were requested to use appropriate theory, policy and evidence to analyse the reforms and to draw lessons from the experience. They were asked specifically to link experience during the reform period with the experience in the pre-reform period.

The article by Evans, Grimes, Wilkinson and Teece represents an attempt to review the main features of the reforms and to comment selectively on aspects

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which the authors consider are likely to be of international interest. A more detailed account of the material covered in the article has since been published as a monograph (Evans et al., 1996).[1]

Characteristics of the New Zealand Model of Reform

The authors do not define precisely what they mean by 'economic reform'. Silverstone et al. identify what they describe as a 'reformist agenda' that has spread quickly from one country to another from 'liberalisation experiments' that 'began in the early 1970s in Chile and, subsequently, in the United Kingdom and the United States' (p. 6). Evans et al. list 33 different reforms covering a wide range of areas, including the change to a proportional representation system of voting and cuts to government expenditure.

In his contribution to Silverstone et al. (p. 136), Brian Easton questions whether the 'reforms' should be viewed as consisting solely of market liberalisation or whether they also include macroeconomic stabilisation policies. In my view, the approach to macroeconomic policy adopted from the mid-1980s did involve a substantial departure from previous policies adopted. Among other things, macroeconomic stabilisation in New Zealand involved substantial changes in formal institutions, including changes to the Reserve Bank Act that were directed toward enhancing the credibility of anti-inflation policies. Indeed, one of the important characteristics of the New Zealand reforms is the extent to which they have involved changes in rules made by the governments that influence incentives faced by individuals.[2] But important changes of approach also occurred that did not require changes in formal rules, such as, for example, governments generally refraining from attempting to use fiscal policy for short-term demand management since 1984.

Evans et al. and Silverstone et al. agree that the reforms were characterised by the application of new conceptual frameworks incorporating advances in microeconomic theory (contestability, principal-agency and public choice) and the new classical macroeconomics (rational expectations, transparency, credibility and an expectations-augmented Phillips curve). Evans et al. (p. 1862) suggest that the reforms 'might be characterised as the pursuit of: coherent policies on a broad front; credibility and time consistency; a comparative institutional approach; and efficient contracting arrangements'. Silverstone et al. (p. 11) describe the approach adopted as 'classic "big bang" reform' involving rapid implementation over a wide area of policy, with little consultation, limited concern for the transitional period and typically little compensation for the losers from the changes.

This description is, I think, only partly correct. By OECD standards, many of the reforms occurred quickly. But trade liberalisation has occurred gradually and predictably. The major reforms in the labour market did not begin until 1991. Reforms in the social welfare area began even later and were quite moderate: they did

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[1] Subsequent references to Evans et al. refer to the article under review rather than the monograph.

[2] To use the terminology of the new institutional economics, many of the reforms involve changes in 'formal institutions'. See for example North (1990) and Alston et al. (1996).

not even wind back the expansion of the welfare state that occurred during the 1970s. Reforms in many areas were preceded by publication of reports that provided opportunities for public comment.

In my view, the reforms are more accurately characterised by their emphasis on the need for credible commitment by government than by a 'big bang' approach. The principles of economic reform espoused by Sir Roger Douglas, the minister most responsible for initiating the reforms, certainly emphasise the desirability of quantum leaps, large packages, speed and maintaining momentum; but they also stress the need to maintain public confidence through credibility and consistency of approach, to provide advance notice to encourage adjustment and to keep the electorate informed (Douglas, 1993:220-3). The heavy emphasis on policy transparency is evident in the ease with which the contributors to these publications are able to identify aspects of economic theory that were influencing policy-makers in introducing the reforms.

Was There an Alternative to Reform?

Is it realistic to view the reforms as an experiment by a prosperous and stable welfare state to sacrifice some equity in the hope of achieving greater efficiency? Alternatively, was the New Zealand welfare state of the 1970s a 'fools paradise' that was becoming increasingly difficult to sustain?

Information provided in some of the contributions to Silverstone et al. goes a fair way toward providing answers.

- New Zealand recorded one of the worst real GDP and per capita growth rate performances of any OECD country in the post-war period (chapter by Viv Hall).

- Trade protection levels remained high over the period 1970-85, isolating New Zealand from the potential for cost reductions in manufacturing and contributing to a decline in export competitiveness in international markets — which occurred despite increasing export assistance and agricultural subsidies (chapter by Ralph Lattimore and Paul Wooding).

- State enterprises had come to account for 20 per cent of gross investment by the early 1980s and were characterised by poor returns on capital, high costs and a high level of political involvement in decision-making (chapter by Ian Duncan).

- New Zealand's inflation rate was on an almost unbroken upward trend between 1970 and 1982, and considerably higher than that of its main trading partners (chapter by Arthur Grimes).

- Income support payments grew rapidly during the 1970s and 1980s as a result of increased unemployment and an expansion in the entitlements of aged persons and single parents (chapter by Graeme Wells).

- The ratio of net public debt to GDP rose from 5 per cent to 32 per cent of GDP in the decade to 1984 and peaked at 52 per cent in 1991-92 (chapter by Graeme Wells).

Evans et al. present a similar picture of declining economic performance in the decade preceding the reforms.

One factor relevant to consideration of the sustainability of previous policies, which does not receive much attention in these publications, was the net migration of people from New Zealand to seek employment in Australia from the mid-1970s to the late 1980s. Losses due to net migration varied from year to year, apparently reflecting labour market conditions relative to Australia's, but amounted to more than 1 per cent of population in some years.

Policies implemented in the late 1970s and early 1980s were starting to show signs of desperation. For example, stringent controls were applied to the amount of money that people were permitted to spend on overseas visits. Growing amounts of industry assistance were provided to the export sector in a futile attempt to compensate for effects of import barriers in taxing exports.[3] A 'think big' development program was implemented in the early 1980s to reduce dependence on imported liquid fuels and to boost exports from energy intensive industries. Extensive wage and price controls were introduced in 1982.

The foreign exchange and constitutional crises that accompanied and followed the general election of June 1984 probably strengthened the hands of reformers by making the electorate more receptive to the substantial reforms that followed (Dalziel & Lattimore, 1996:21-3). But radical reform was not the only alternative available to the new Labour government. For example, the government could have made the minimum changes needed to cope with immediate problems and continued with previous policies until the next crisis arose. Progressive deterioration in performance could have continued until reforms were imposed externally as a condition for obtaining assistance from the IMF.

The Transitional Costs of Reform

Poverty and inequality. Despite efforts to protect low-income earners, some reforms probably did result in hardship for some people, at least in the short run. Since economic reforms typically involve the removal of interventions that shield incumbents in particular industries, firms, public-sector organisations, unions, and so on, from competition, it is almost inevitable that those made worse off in the short run by any reform will include some low-income earners. At the same time, and as acknowledged by Brian Easton in the chapter on income distribution in Sil-

[3] My view that this compensatory assistance was futile is based on the fact that the cutting edge of protection from import competition was provided by means of import licences which were administered with a view to avoiding a substantial transfer of resources out of protected industries. The provision of compensatory assistance can be successful only if it results in a reallocation of resources favouring lightly assisted industries at the expense of heavily assisted industries (Syntec, 1984).

verstone et al., 'these microeconomic changes need not accumulate to a macroeconomic change of the aggregate distributions' (p. 133). Under a broadly based reform program such as that undertaken in New Zealand, people who are disadvantaged by one policy change are likely to be among the beneficiaries of other policy changes.

Easton suggests that the economic reforms of the 1980s and 1990s did result in some increase in economic inequality, but this conclusion appears to be quite sensitive to the time period considered and the way poverty is measured. The results of one analysis quoted by Easton suggest that the proportion of income going to the bottom four deciles of households rose in the period 1981/82–1987/88. As might be expected, the cuts in welfare support of 1990 and 1991, combined with the sharp recession at that time, resulted in an increase in the proportion of households falling below various poverty lines. Evidence provided in the Treasury's (1996) briefing to the incoming government suggests, however, that the proportion of the population in hardship, relative to fixed real-income levels, has declined in recent years. This is in line with the growth of the economy and the decline in unemployment rate from 10.9 per cent in September quarter 1991 to 5.9 per cent in December quarter 1996.[4]

Some commentators argue that transitional costs could have been reduced if reforms had been pursued differently. Fred Argy's comment to the effect that the overall welfare effects of the New Zealand reforms may be negative was based on his view that some of the New Zealand reforms, particularly those of the labour market, 'have probably contributed only little to its strong economic performance and yet entailed a high social cost' (Argy, 1996:90-1). However, Argy's representation of the New Zealand labour market reforms is at variance with the facts as presented in the publications under review as well as with accounts provided by Wolfgang Kasper (1996) and the OECD (1994). Argy refers to a 'sharp lowering in minimum wages and conditions' and a 'weakening of the arbitral and grievance redress machinery' (1996:91). In fact, the Employment Contracts Act (ECA) left in place statutory minimum wages; and, rather than being weakened, the ECA's grievance redress machinery has placed great emphasis on procedural correctness in dismissals and on 'fairness' even when dismissed workers have been manifestly negligent or incompetent (Evans et al., p. 1880).

Unemployment. Employment opportunities were obviously scarce during much of the period over which the reforms were taking place. The unemployment rate more than doubled during 1987-91. But can this be attributed to the reforms? It is easy to see why many New Zealanders think so. The total combined jobs lost in corporatised and privatised government departments between 1987 and 1994 is

[4] The evidence that recent economic growth in New Zealand is expanding the opportunities available to the poorest members of the community is consistent with the international evidence of an association between growth in average incomes and the opportunities available to the poor to improve their lot in an absolute sense (Bates, 1996).

equivalent to nearly half of the rise in total unemployment (Silverstone et al., p. 156). However, this comparison looks at only one side of the picture: it overlooks the indirect effects of the reforms in increasing private sector employment opportunities by reducing business costs and taxes.

Tests of the hypothesis that increased unemployment was attributable to structural change, reported in the chapter on unemployment in Silverstone et al. by Simon Chapple, Richard Harris and Brian Silverstone, do not support the popular view. If structural changes were an important source of rising unemployment, they could be expected to be associated with a major increase in occupational and regional mismatches. In fact, increased occupational and regional mismatches accounted for only a minor part of the overall increase in unemployment. The authors' econometric results suggest that the increase in unemployment during the reform period was attributable to 'shocks from aggregate demand' (p. 168).

This seems to put the blame for increased unemployment squarely in the court of the monetary policies that were used to wind back inflation from 13 per cent in 1985 to 1 per cent in 1993. Yet even this conclusion is simplistic. Viv Hall's analysis in Silverstone et al. suggests that New Zealand's sacrifice ratio (a measure of the output forgone to reduce inflation by 1 percentage point) was higher than Australia's. His simulation analysis suggests that it would have been substantially smaller if New Zealand's wage setting institutions had been more flexible in 1985: that is to say, if labour market reforms had been introduced sooner. Real wages rose substantially after the end of the pre-reform wage and price freeze (nominal wage rates rose by 22 per cent during the year to December 1996, resulting in a 14 per cent rise in real wages relative to producer prices for outputs); and this was unwound only partially in subsequent years despite rising unemployment (Evans et al., pp. 1870, 1880).

Arthur Grimes's discussion of monetary policy suggests that economic adjustments to policy tightening during the 1980s were delayed because the Reserve Bank 'had no established anti-inflationary credentials' (Silverstone et al., p. 256). During the disinflation period, actual inflation was typically half expected levels, reflecting a widespread view that the Reserve Bank, given the multiple objectives that it had before 1989, was likely to revert to a more expansionary stance once unemployment levels started to rise.

An appropriate conclusion to draw is that high unemployment during the reform period was a hangover from pre-reform labour market and monetary policies rather than a consequence of the reforms themselves.

Sequencing of reforms. Evans et al. make a case, in terms of theoretical principles of sequencing, that the costs of reform could have been reduced if the labour market and fiscal reforms had taken place at an earlier stage in the reform process. They argue that this could have 'induced lower real interest and exchange rates and lower real wages through the reform period' (p. 1871). Silverstone et al. have some sympathy for this view. They argue that 'the importance of political support in in-

fluencing the sequence of reforms in New Zealand may have added to the transition costs in terms of lower growth and higher unemployment' (p. 22).

The response that Sir Roger Douglas has given, as a practitioner of reform, to the question of optimal sequencing is worth noting in this context:

> I find the question fundamentally irrelevant. Before you can plan your perfect move in the perfect way at the perfect time, the situation has already changed. Instead of a perfect result you end up with a missed opportunity... If there is an opportunity to implement a reform that makes sense in the medium term, grab it before the moment passes. When an economy is stalling and failing, what matters is to get it moving toward a better future as soon as possible. (Douglas, 1993:224)

Could the costs of reform in New Zealand have been reduced if a more gradual and tentative approach to labour market reform had been adopted, as in Australia? A comparison of Australian and New Zealand unemployment rates since 1970 shows that only during 1989-91 were unemployment rates in New Zealand higher than in Australia. In those three years, the difference in favour of Australia was substantially smaller than the difference in favour of New Zealand has been in subsequent years (Silverstone et al., p. 206). Evidence presented by Tim Maloney and John Savage suggests that New Zealand's labour market reforms are at least partly responsible for the strong employment growth in that country in recent years (Silverstone et al., pp. 210-11).

The counterfactual. What would have happened if New Zealand had not reformed during the 1980s? The publications under review do not address this question, but Grant Scobie and John Janssen, among others, have argued that 'it is altogether too naive to assume that the old order would have simply continued' in the absence of reform (1993:6). A strong case can be made that the most likely outcome would have been a continued deterioration in economic performance, with more painful reforms being required at a later stage.

Anyone with a genuine interest in the well-being of low-income earners in New Zealand should be pleased that a substantial change in policy direction occurred without major social trauma. The recent history of the former centrally planned economies, as well as of some economies in Latin America, shows that social safety nets constructed by governments provide little protection to the poor when unsustainable economic policies are followed to the point where a collapse in economic activity becomes unavoidable (World Bank, 1995:103-8).

How Much Has Economic Performance Improved?

Real GDP growth in New Zealand averaged 3.8 per cent a year over the four years to 1996. In its briefing to the incoming government elected in 1996, the Treasury forecast that, on current policy settings, growth would average 3.2 per cent a year over the four years to 2000 (Treasury, 1996).

Although Silverstone et al. are cautiously optimistic, they suggest that it is 'too early to conclude firmly whether New Zealand's improved economic performance is sustainable' (p. 21). Their caution is based partly on the difficulty, discussed particularly in Viv Hall's chapter, of distinguishing between cyclical and structural components in the strong economic growth experienced in recent years. Evans et al. acknowledge that there is still room for debate about the degree to which the recovery is structural rather than cyclical, but conclude more positively that 'New Zealand appears to be on a trajectory to maintain its economy as a consistent high performer among the OECD' (pp. 1893-5).

On balance, I think that the contributions to Silverstone et al. would have supported a less equivocal conclusion along the lines of that reached by Evans et al..

- The growth of recent years has been occurring in a context of a sound fiscal situation (generation of budget surpluses) and low inflation (chapters by Graeme Wells and Arthur Grimes).

- There is evidence that the reforms have had a positive effect on the rate of growth in total factor productivity (TFP). The results reported in the chapter by Rolf Fare, Shawna Grosskopf and Dimitri Margaritis indicate that TFP growth rose from 0.7 per cent a year during 1973-84 to 2.4 per cent during 1984-1994. Qualifications always attach to measurement of TFP growth, but this appears to represent a substantial improvement, particularly in view of the fact that some important reforms were initiated only toward the end of this period. The authors also suggest that their methodology may tend to underestimate productivity growth because the capital stock series they use (calculated using the perpetual inventory method) tends to overstate capital stocks during a period of economic reform.

- The analysis of international trade by Ralph Lattimore and Paul Wooding suggests that policy change has resulted in a more rapid expansion of trade, particularly since 1988. Agricultural exports have been reoriented following the removal of discriminatory subsidies, and smaller manufacturing firms in food processing, metal fabrication and textiles have been oriented increasingly toward exports.

- Tim Hazledine and Andrew Murphy, in their chapter on manufacturing industry, find a modest improvement in an indicator of allocative efficiency for the manufacturing sector as a whole during 1984-92, but these gains occurred largely in two major primary processing industries. The apparent lack of evidence of widespread efficiency gains may be attributable to the fact that the indicator of allocative efficiency used in this study does not reflect efficiency of resource use in production and to the study's data cut-off point in 1992, which is at the start of the recovery period.

- The corporatisation of public enterprises generated major gains in productive efficiency through large-scale job-shedding, and business and household consumers benefited directly from improved services (chapter by Ian Duncan).

- Labour market reforms appear to have contributed significantly to the growth in employment since 1992, although the expected positive effect of these reforms on average labour productivity is not yet evident in the aggregate statistics (chapter by Tim Maloney and John Savage).

Although there has been some dispute over the question of how rapidly labour productivity has been rising since the ECA came into effect (Evans et al., p. 1881), the more important question is what has been happening to TFP. Viv Hall suggests that, while there is as yet no clear evidence that TFP growth rates have been higher recently than for periods before the mid-1980s, there is 'a reasonable possibility that full cycle figures for the currently incomplete business cycle could register better news for both TFP and labour input growth' (Silverstone et al., p. 65).

Business surveys provide some supporting evidence of an improvement in productivity performance of the New Zealand economy in recent years. Evans et al. summarise results of a business survey by John Savage and David Cooling, which suggest that, following the introduction of the ECA, employment contract negotiations have included a strong emphasis on productivity improvement. The survey responses indicate the use of more flexible work practices, reduced demarcation disputes, increased multi-skilling, greater use of performance-based pay and increases in ordinary-time pay rates, in addition to cost-reducing measures such as reducing overtime rates of pay (Evans et al., p. 1883).

John Yeabsley and John Savage (1996) have pointed to strong supporting evidence provided by the quarterly survey of business opinion undertaken by the New Zealand Institute of Economic Research. The proportion of survey firms reporting higher productivity has been substantially greater since 1991 than in earlier sub-periods. For example, in the expansion phase from June quarter 1991 to March quarter 1996 an average of 30.2 per cent of firms reported higher productivity, compared with only 14.2 per cent in the expansion phase from June quarter 1978 to Septemer quarter 1986.

New Zealand's Prospects

Are the reforms likely to enable New Zealand to become a 'growth success story'? The New Zealand Business Roundtable (1996:3) has argued that 'the New Zealand economy is capable of moving into the "fast lane" provided the momentum is maintained'. The Business Roundtable suggests, however, that to maintain momentum 'New Zealand will need to embrace continuing change' (1996:1).

Table 1

Changes in economic freedom and economic growth in selected countries

	Averages for nine high-growth reformers (including Chile)	*Averages for eight low-growth reformers (including NZ)*	*New Zealand*	*Chile*
Change in economic freedom rating: 1975-1990	1.8	1.7	1.7	2.9
Annual % growth of per capita GDP 1985-94	4.6	1.4	0.8	4.8
Per capita GDP in 1980 ($US)	4,458	7,124	10,362	3,892
Average freedom rating 1975-90	5.2	4.5	4.8	4.1
Change in freedom rating during 1985-90 as % of total change in freedom rating from 1975 to 1990	31	64	112	55
Annual % growth of per capita GDP 1970-80	4.1	2.4	0.9	0.2

Note: Freedom ratings are measured on a scale of 0 to 10, with higher numbers denoting greater levels of economic freedom.

Sources: Gwartney et al. (1996); World Bank (1995).

The publications under review contain little discussion of the international evidence relevant to this question. However, Viv Hall quotes the views of David Henderson that economic reforms in OECD countries have prevented a deterioration in performance so 'there is a positive balance [relative to the possible consequences of a 'failure to act'] ... even if some of the main indicators show, for a period at least, little signs of improvement' (Silverstone et al., p. 67). Henderson (1995:79) observes that 'there are few if any OECD economies where it is clear that reforms have already brought, or are in course of bringing, substantial quantifiable

gains across the system as a whole in terms of either productivity growth or levels of unemployment'.

At first sight, Henderson's observation for OECD countries seems to conflict with the evidence for a wider group economies of a strong positive relationship between improvements in economic freedom and improved growth performance. I refer, for example, to the evidence provided by the Fraser Institute's study of the comparative economic freedom of different countries (Gwartney et al., 1996:97-104). The results for individual countries indicate, however, that the high-income countries that undertook substantial reforms during the 1980s (including the United States and United Kingdom as well as New Zealand) were not alone among the reformers to experience low growth during the period 1985-94. Of the 17 economies identified as having the greatest increases in economic freedom during 1975-90, eight had annual per capita growth rates of less than 2.5 per cent during 1985-94; but half of these had per capita incomes less than 25 per cent of the US level in 1980. In addition, some high-income countries that experienced substantial improvements in economic freedom during the 1980s (most notably Singapore and Japan) had higher annual per capita growth rates than 2.5 per cent during 1985-94.

Further examination suggests that the lack of clear evidence of economic benefits in some countries that have undertaken economic reforms in the 1980s can be attributed partly to the time required for new policy directions to become embedded and for adjustment to occur. Some relevant characteristics of reforming countries which experienced high and low growth rates over the period 1985-94 are shown in Table 1. It is apparent that, although the reformers experiencing low growth rates tended to have higher per capita incomes than the high growth reformers, they also tended to have a high proportion of reforms occurring recently, lower average freedom ratings, and a history of low growth rates in the 1970s.

Viv Hall draws attention to the two decades that Chile has taken to move from poor performance to a sustainably higher growth path, and suggests that there are some similarities with the situation in New Zealand:

> Our evidence suggests that, as in Chile from 1981 to 1983, New Zealand has encountered at least one period of major setback (1987-92) and this has contributed to the long transition period. Nevertheless, it is also clear that during the overall period since 1984, sound progress has been made on reducing macroeconomic imbalances, thereby setting up the required macroeconomic platform for efficiency gains and sustained economic growth rates to emerge more strongly. (Silverstone et al., p. 67)

It is not difficult to understand why it may take a decade or more for many countries to complete the transition from poor performance to a sustainable high growth rate. Profound changes in behaviour, including changes in the willingness of individuals to learn new skills and business practices, are required as people respond to the incentives that policy reforms provide. It takes time even for the most innovative firms and individuals to accept that new market incentives are likely to be sus-

tained and to develop and implement new strategies. Widespread adoption requires sufficient time for these new strategies to become demonstrably successful.

These considerations provide grounds for confidence that New Zealand will become a growth success story as the reforms become fully entrenched. How successful will depend, of course, on the future directions of policy, including the extent to which further reforms are undertaken in areas such as education, health and welfare. Robert Stephens concludes his chapter on social services by noting that the welfare state has been more enduring and resilient than many observers thought it would be in 1991 when some reductions in social welfare expenditure occurred (Silverstone et al., p. 490). Evans et al. argue (p. 1894) that the reforms are incomplete and that further action in areas such as education, health and welfare are likely to be necessary if New Zealand is to achieve its potential.

Concluding Remarks

Which of these publications would I recommend? That depends on what readers are looking for. In my view, Evans et al. provide a balanced summary of the reforms. Their analysis of the effects of the reforms is also quite good as far as it goes, but it does seem to skirt around some important issues. For example, although the article is explicitly concerned with efficiency, it could have said more about the distributional effects of the reforms. In addition, while it devotes space to the reforms in the core public service, it does not offer many clues about the extent to which any changes of substance have occurred in relationships between ministers and departments as a result of the adoption of formal contracting processes, or about the implications that such changes might have in the new political environment.

Silverstone et al. give a summary of the reforms in their introductory chapter, but include little discussion of some important aspects, such as the core public sector reforms. As might be expected from the length of this book (518 pages) and the number of contributors, it provides useful in-depth analyses of many aspects of the reforms. The chapter on economic growth is of a particularly high standard. The chapter on productivity growth is also impressive, although the value of the attempt to split TFP into efficiency change and technological change components when the rate of technological change is assumed to be the same in all industries is of doubtful value.[5] Other particularly useful chapters are those on unemployment, labour markets, fiscal policy, monetary policy and international trade.

Although some of the contributors to Silverstone et al. have been hostile to the reforms, they have by and large confined themselves in this volume to objective analytical contributions. One exception is the assertion by Robert Stephens that 'governments have been attempting to curb expenditure growth through a reduction in the quality of education'. This is supported only by the observation: 'In tertiary education, staff/student ratios have risen from 1:12 in 1986 to 1:18 in 1992, and average government funding per student has fallen' (p. 461). It is not obvious why

[5] I am grateful to an anonymous referee for drawing this to my attention.

an increase in the number of students per staff member or a reduction in government funding per student should necessarily be interpreted as reflecting a reduction in quality of education: such changes may reflect increased productivity and increased private funding.

The 'selected bibliography' provided by Silverstone et al. is not very helpful as a guide to further reading. One notable omission is the lack of references to publications by the New Zealand Business Roundtable. This is unfortunate in view of the major contribution that that organisation has made in commissioning high-quality policy analysis of many issues and the impact of this work in raising the standard of public debate over the past decade. It is also odd that the selected bibliography provided by Silverstone et al. does not refer to any publications by Lewis Evans, Arthur Grimes, Bryce Wilkinson or David Teece.

Neither of the publications sheds a great deal of light on the processes of policy development and implementation. Some commentators might argue that to do this would have taken the authors beyond the realm of economics. However, it seems likely that these processes may have been important in influencing expectations about the sustainability of changes in policy directions and hence the willingness of people to respond to changes in the incentive environment. The fact that radical reforms have been sustained in New Zealand must owe a lot to the way policy development has occurred in New Zealand since 1984. Its distinguishing characteristics include:

- a policy agenda which focussed on the 'big issues' rather than on finding short-term 'solutions' to a host of minor problems;

- the attention given by the government to problem definition and 'state-of-the-art' analysis, drawing widely on experiences of other countries but often developing a distinctively New Zealand approach; and

- processes that made the analytical basis for policy change available for public scrutiny and debate.

Finally, it is regrettable that the publications under review do not shed more light on the extent to which the reforms have lifted the productivity performance of the New Zealand economy. This is more a criticism of the current state of applied economics than of the authors; but the shortcomings of our economic measurement techniques become very obvious when we consider that, 13 years after major reforms began, leading New Zealand economists are still unable to provide policy-makers and citizens with reliable measurements of progress toward the goal of lifting the long-term productivity performance of the New Zealand economy. Serious efforts should be made, using firm surveys for example, to develop leading indicators of secular productivity change so that the process of adjustment can be monitored more satisfactorily.

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