BUILDING NEW ZEALAND’S COMPETITIVENESS

Vague plans are not enough

Tony Caughey

— Central government should learn from Auckland’s economic development goals.

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AUCKLAND’S Economic Development Strategy was launched in September, 2012. It is a ten-year plan that supports the 30-year Auckland Plan approved by Auckland Council the previous March. Now, for the first time, a Supercity organisation exists with a timeframe, legislated by central government, that is well beyond the three year election cycle; an organisation that has formulated a unique economic development strategy for Auckland, based around its specific strengths.

Central government should learn from Auckland’s economic development goals.
This time horizon is particularly important given the now-accepted need for economic growth to be developed from the bottom up, rather than from the top down. We must get our cities and regions working better. Our cities rank highly on quality of life dimensions, but not on economic competitiveness measures.

The Auckland Plan set some explicit and ambitious goals—increasing GDP annually by a minimum of five per cent, regional exports by six per cent per year, and productivity by two per cent per year. The Economic Development Strategy (EDS) addresses how these increases are to be achieved.

There is much that central government could learn from Auckland about writing an economic development plan. Auckland’s EDS is a long way ahead of the Government’s Business Growth Agenda (BGA) on many fronts.

The first thing a plan needs is a goal against which progress can be measured. Auckland’s goals, as outlined above, are specific. By contrast, government has four broad priorities:

- Responsibly managing government finances
- Building a more productive and competitive economy
- Delivering better public services within tight financial constraints
- Rebuilding Christchurch

The priority of most interest to me is number two—“building a more productive and competitive economy”. While the concept is sound, the obvious question is: how will government know if it is has been successful in achieving these twin priorities? Productivity is relatively easy to measure, but by how much do we want to improve it? Auckland has a target of increasing productivity by at least two per cent a year. Is government’s goal to achieve anything better than zero, and if so, will it be enough? Where is the debate about this?

Competitiveness is a much more difficult concept. There is no attempt within the BGA to define what it means to build a “more competitive economy”, so how will government know whether it has achieved this priority?

One way would be to track New Zealand’s progress on a variety of international indices that measure competitiveness. These include the World Economic Forum’s Global Competitiveness Report, the IMD World Competitiveness Yearbook, the report released by the Chinese Academy of Social Sciences, and that of the Economist Intelligence Unit.

One might think that if government was interested in increasing New Zealand’s rankings in these surveys it would have programmes to address the variables that the surveys measure—especially the important ones where New Zealand is ranked poorly. However, I can find no evidence of systematic government thinking that addresses the areas where New Zealand is underperforming.

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The export goal sounds attractive, but why would you want to do this if you don’t know what you wish to achieve by it?

In the early 1990s I was part of a group that used a model developed by economic research company BERL to determine that if New Zealand wanted annual GDP growth of four per cent, then one way to achieve it, given certain other assumptions, was to grow exports by nine per cent a year—in other
words, to double exports in eight years. So, the export goal in the BGA sounds about right, but creating an objective in a vacuum, without a broader, quantifiable goal, makes no sense.

Having said that, there is much to applaud in this export goal. It is the first time in 30 years that the government has acknowledged a basic fact—that we are a small island economy at the bottom of the world which depends for its prosperity on exporting to a world that does not owe us a living. Treasury thinking since export incentives were abolished in the early 1980s has been dominated by the theory that a dollar earned in New Zealand is as good as one earned overseas—with the inevitable and unsurprising result that our exports have stagnated. At last we have a signal from government that exporting is a good thing. It is tantalising to speculate on what strategies government will put in place to achieve this goal, as we have seen almost nothing to date.

Such a goal will go some way to reaching the definition of competitiveness espoused by Michael Porter and others. They declare that a region is “a competitive location to the extent that companies operating in it are able to compete successfully in the global economy while supporting high and rising living standards for the average person in [that region]”. A competitive location produces prosperity for both companies and citizens.

Regrettably, the BGA hasn’t yet got a definition of competitiveness. It is a complex subject. In their research paper “The Determinants of National Competitiveness”, Mercedes Delgado, Christian Ketels, Michael Porter and Scott Stern say: “Competitiveness has for the last few decades been a central feature of the economic policy debate. But the debate, both in policy and academia, remains mired in confusion about what the term competitiveness actually entails”.

Government’s business growth agenda is nowhere near world’s best practice. Its language is far removed from that used by Harvard Business Review in its March 2012 special issue on US Competitiveness, which noted that: “Although the US retains profound competitive strengths—for instance, in higher education and entrepreneurship—those strengths are increasingly threatened by weaknesses in areas such as the tax code, basic education, macroeconomic policies, and regulation. Steps to reverse the loss will require a new focus by government and business leaders”.

HBR goes on to describe 17 essential elements of the national business environment:

**Macro Elements**
- Macroeconomic policy: soundness of government budgetary, interest rate, and monetary policies
- Effectiveness of the political system: the ability of government to pass effective laws
- Efficiency of the legal framework: modest legal costs, swift adjudication
- Complexity of the national tax code
- K-12 education system: universal access to high-quality education; curricula that prepare students for productive work
- Innovation infrastructure: high-quality scientific research institutions; availability of scientists and engineers
- Regulation: effective and predictable regulations without unnecessary burden on firms
- Strength of clusters: geographic concentrations of related firms, suppliers, service providers, and supporting institutions with effective collaboration
- Quality of capital markets: ease of firm access to appropriate capital; capital allocated to most profitable investments
- Sophistication of firm management and operations: use of sophisticated strategies, operating practices, management structures, and analytical techniques

**Micro Elements**
- Logistics infrastructure: high-quality highways, railroads, ports, and air transport
- Communications infrastructure: high-quality and widely available telephony, Internet, and data access
- High-quality universities with strong linkages to the private sector
- Context for entrepreneurship: availability of capital for high quality ideas; ease of setting up new businesses; lack of stigma for failure
- Availability of skilled labor
- Flexibility in hiring and firing of workers

Again, I find the reference to clusters of interest. Likewise, the concept of promoting entrepreneurship, which is entirely missing from the BGA, as I have previously noted.

**Clusters**

THEN WE have the Economist Intelligence Unit’s report at the end of 2011 on “Fostering Innovation-Led Clusters”. That report began by stating that: “There are few economic development policies as popular as clusters. It is hard today to find a country, region, or even city that is not trying to develop a network of complementary and competitive firms.”

Actually, it is not hard. You just have to look at New Zealand. Cluster development strategies are yet to feature in the Business Growth Agenda. Why? I contend that the main reason is a lack of understanding of active cluster development programmes in our Wellington institutions. On a scale of one to 10, I would rate the level of understanding somewhere between zero and one. In a straw poll I did of my assessment, I was told by one official that I was being too harsh. But a world leader in cluster development suggested that such a score was generous. There are a handful of officials with some experience of cluster development, most of it relating back to the Joint Action Group (JAG) initiatives of New Zealand Trade and Enterprise some 15 years ago. These people do not seem to be prominent in the writing of the BGA.

There are glimmers of hope that the understanding of cluster development programmes in government institutions in Wellington is about to improve. But
more on that later.

The big picture is that New Zealand is underachieving economically. This was alluded to by the Organisation for Economic Cooperation and Development almost 10 years ago. In the OECD’s 2003 economic survey of New Zealand, it said:

“The mystery is why a country that seems so close to best practice in most of the policies that are regarded as the key drivers of growth is nevertheless just an average performer.”

Academic Phillip McCann later called this New Zealand’s “Productivity Paradox”. Such terminology was adopted by the late Sir Paul Callaghan, who used evidence-based research to enter the economic debate. He argued for a greater emphasis on education, innovation and the development of the high-tech manufacturing sector. This was all in the context, as he put it, that “we seem to have the market fundamentals right, but we still haven’t got the productivity we are looking for”.

So the problem is not new, and it has been well described. The question is, what do we do about it? Self-evidently, we need to do something different from what is embedded in the Business Growth Agenda. The implementation of this agenda would simply allow us to restate the Productivity Paradox year after year while remaining a merely average performer.

The Auckland Strategy provides answers on how we can break free of this paradox. Its five priorities are not dissimilar to the government’s business growth agenda: developing into the innovation hub of the Pacific Rim, becoming internationally connected and export driven, becoming business friendly and functioning effectively, growing skills and the local workforce, and developing into a vibrant and creative international city. In addition it has four cross-cutting themes: a sustainable eco-economy, an iwi/Maori economic powerhouse, an innovative rural and maritime economy and a diverse ethnic economy.

More importantly, the Auckland EDS has explicit goals, as outlined earlier. It also has plans to develop specific industry clusters, and in this it has benefitted from a submission by the global conference of The Competitiveness Institute (TCI), held in Auckland in 2011. This Barcelona-based institute is a network of 9,000 professionals from more than 100 countries who are the world’s leading practitioners in the economic development of cities, regions and countries. I was privileged to chair the steering committee for the 2011 conference.

In October 2012, I attended the TCI’s conference in the Basque Country in Spain, in company with 450 delegates from more than 50 countries. The Basque Country was quick to embrace many of the ideas of Michael Porter 20 years ago and is reaping the rewards of its cluster development programmes. Bilbao is an example of how a decaying industrial city can be transformed into a modern vibrant one, with some of the best infrastructure in Europe, and with no debt. Universities in the region have embraced the subject of competitiveness in both teaching and research.

The good news for New Zealand is that largely as a result of the TCI conference in Auckland last year, The University of Auckland Business School has announced that it will join the University of Otago and more than 100 leading universities around the world in teaching Porter’s “Microeconomics of Competitiveness” course. This is a welcome development and will help raise the level of understanding among young people of these vitally important concepts. Over
tivities in addition to that move towards internationalisation through electronic means.

ME: Absolutely. There is a need for connectivity throughout New Zealand so that people anywhere in the country can connect to each other and also connect to the rest of the world. It is one of the ways in the modern world to try to overcome the disadvantage of distance and small domestic population. But at the same time, cities are also important. They are basically where the work of globalisation gets done. They are the places that connect one country to another, that connect one population to another. In addition, if you think about it, the process of improving communication and transportation, allows certain activities to be spread over space, but also allows other activities to be concentrated. And what we find is that industries and activities that depend on the creative process, that depend on knowledge that is difficult to write down, difficult to codify, require face-to-face interaction. And exactly the same communications and transport technologies that allow some economic activities to disperse over space actually cause other economic activities to concentrate over space and these tend, in many cases, to concentrate in cities. This will increase the level of knowledge in our institutions that can be harnessed to implement such policies.

The full name of the course is “Microeconomics of Competitiveness: Firms, Clusters, and Economic Development”. The course outline explains that it: “explores the determinants of competitiveness and successful economic development viewed from a bottom-up, microeconomic perspective. While sound macroeconomic policies, stable legal and political institutions, and improving social conditions create the potential for competitiveness, wealth is actually created at the microeconomic level. The sophistication and productivity of firms, the vitality of clusters, and the quality of the business environment in which competition takes place, are the ultimate determinants of a nation’s or region’s productivity.”

The problem that we face is that there are very few people in New Zealand who understand this. Hong Kong-based Michael Enright, of research and strategy consulting firm Enright, Scott and Associates, has undertaken a study of New Zealand’s competitiveness. It builds on research that he started more than 20 years ago when he worked on Upgrading New Zealand’s Competitive Advantage with Michael Porter, Graham Crocombe and others. He is regarded as one of the foremost international academics and advisers on competitiveness and cluster development (see sidebar interview, p13), and his perspective will need to be carefully considered by all those working in this field in New Zealand.

We must also deepen people’s understanding of clusters, because there are many misconceptions. It is very important to realise that a cluster is not a science park, nor a piece of infrastructure—like the Food-bowl—or a precinct. Clusters are also not about “picking winners”. Cluster development programmes, as practised by every government in Europe, are development programmes for industries that are already winners.

There are many definitions of clusters. Porter calls them: “Geographic concentrations of interconnected companies, specialised suppliers, service providers, firms in related industries and associated institutions... in particular fields that compete but also cooperate.”

The problem for us is that many places around the world have benefitted from active cluster development policies that New Zealand officials have not wanted to believe in. The Auckland plan offers some hope that these shortcomings will be overcome.

The final word should go to the 2012 TCI submission on the Auckland Plan—before the Plan’s early drafts made any mention of clusters. TCI said: “Clusters are no silver bullet and they need to be part of a broader competitiveness strategy to reach their full potential. But they are a tool and perspective far too powerful for Auckland to neglect on the ambitious path that the region has embarked on.”

I have just begun a programme driven by Auckland Tourism, Events and Economic Development (ATEED) and the Auckland Council to further develop a food and beverage cluster in South Auckland. I am looking forward to this challenge as part of a wider attempt to enlightened economic development in New Zealand.

In summary, then, the Business Growth Agenda requires a fundamental rethink. It needs goals that can be measured. It needs to recognise what is happening elsewhere in the world. And it needs to reflect that thinking—aided by the experience of business people and people with backgrounds in economic development—in a revised BGA. I find it extraordinary that a set of documents can be produced about New Zealand’s economic future that is completely silent on the twin pillars of cluster development and fostering entrepreneurship. The BGA emphasis on a top-down solution for economic development needs to be modified to deliver a solution which will be from the bottom up.

These three omissions—entrepreneurship, clusters and a bottom-up approach—put us out of step with The Economist (“Fostering Innovation Led Clusters”), Harvard Business Review (on US Competitiveness), the World Bank (elements of a Local Economic Development Programme), the World Economic Forum (The Global Competitiveness Report), The Competitiveness Institute and the world’s most respected academics. Fortunately, the Auckland EDs goes a long way to address these shortcomings in New Zealand’s largest region. With concerted pressure, action can be taken to revise and improve the BGA, break us out of our “productivity paradox”.

KEY TAKE-OUTS

* The government’s Business Growth Agenda is poorly conceived and will not remedy New Zealand’s inadequate economic performance.

* Cluster development strategies—a key component of strong economies around the world—are not well understood in this country.

* Auckland’s new economic strategy suggests a way for New Zealand to break free of its “productivity paradox”.

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