The Political Philosophy of the New Zealand Treasury

An analysis of Treasury's briefing papers to the incoming governments, 1984 to 1993

A thesis

submitted in fulfilment

of the requirements for the Degree

of

Master of Arts in Political Science

in the

University of Canterbury

by

Sarah Jane Merl Miskin

University of Canterbury

1997

For Ben, first and always

and in memory of my father,

William James Sands
(2/2/1941 to 22/4/1981)

Contents

Abstract

This thesis explores the political philosophy of the New Zealand Treasury by analysing the briefing papers it prepared for the incoming governments of 1984, 1987, 1990 and 1993. The underlying premise is that Treasury has been inextricably linked to the economic, administrative and social reforms of this period, which transformed New Zealand from a model of Keynesian state intervention to a bastion of free market economics. Such reforms can be seen as consistent with neo-liberalism in which the state's role is minimised, being limited to setting and enforcing the rules by which the free market operates. The intention of the thesis is to investigate whether the political philosophy underlying Treasury's economic policy framework, as put forward in the briefing papers, can be said to be neo-liberal. In doing so, it will first offer a brief overview of the New Zealand economy before presenting Treasury's model, which compares the abilities of the state and the market to achieve New Zealand's social goals. It will demonstrate that Treasury argues in favour of a neo-liberal policy framework on the grounds that the state can never produce better results for New Zealanders than the market, so it should leave the achievement of social well-being to the private sector. The thesis will then examine the claims that economic policy is essentially scientific and value-free -- in other words, politically neutral -- demonstrating that the "scientific facts" on which some of Treasury's assumptions are based are flawed. It will then discuss what happens to the social policy areas of health and education when the market model is applied, given its underlying weaknesses. The conclusion of the thesis focuses on the implications for the political community of the pursuit of neo-liberal policies, arguing that Treasury's neo-liberal prescriptions for social policy are unlikely to produce the "fair and thriving" society of the kind envisaged by New Zealanders, but are more likely to undermine the collective values on which New Zealand society has been built.

Acknowledgements

Two people deserve my thanks above all others for their help in producing this thesis:

First, Ben Miskin, whose numerous contributions ranged from doing my cooking and laundry to proof-reading and laboriously checking all my footnotes -- all this despite disagreeing with all my arguments and conclusions. Without his love and support throughout my time at university, I would not have been able to juggle both career and study, and this thesis is as much a reflection of his effort as it is mine.

Second, Dr Joanna Goven, who is valued as a friend as well as a helpful and tolerant supervisor. I appreciate her patience as she read several early drafts, and I am especially grateful for her valuable suggestions on areas that could be expanded. Her encouragement and attention to detail have made me a better student and potential academic.

My love and gratitude go to my sister, Briony Sands, who knew when to rescue me with coffee and muffins, and always said "uh-huh" at the right time when I was expounding the merits of my argument. I want her to know that when she writes her law thesis, I'll buy her lots of muffins too.

I owe special thanks to Associate Professor Mark Francis for his cheerful and friendly advice to me while I have been a student at the University of Canterbury. His contributions to my intellectual development have been too many to note, but I owe him a great deal.

Finally, thanks to the members of my family, especially Andrew Sands and Rowan Sands, and my friends at *The Press* -- Dorothy Parker, Mark Wilson, Laura Keddell, Glenn Inwood, Sally Mekalik and Liz Bluck -- who have all showed tremendous tolerance in enduring my enthusiasm for my subject matter. Their patience and friendship is appreciated.

Sarah Miskin
April 1997

INTRODUCTION

New Zealand's first MMP election in November 1996 brought to an end of the most turbulent periods in New Zealand's history. Over a 12-year period, successive Labour then National governments attacked the foundations of the Keynesian welfare state, replacing it with a new faith in the free market as a means of achieving prosperity for New Zealanders. While these reforms have been named after the ministers of finance behind their implementation -- Rogernomics (Labour's Roger Douglas) and Ruthanasia (National's Ruth Richardson) -- they have also become synonymous with Treasury, the department responsible for providing economic and financial advice to government. Treasury has become inextricably linked to the economic, administrative, and social reforms, being widely identified as their "leading advocate and prime architect".[1] The problem, however, is that while Treasury has borne much of the criticism over the reforms, as former Reserve Bank economist Len Bayliss observes, "comments on Treasury's role and performance are often strong on emotion and weak on facts".[2] The department's reputation has not been helped, however, by publicity on some of its more bizarre policy ideas, the most recent of which brought public ridicule when it was reported that Treasury had argued against employing more police officers because justice system costs would rise as the enlarged police force caught more criminals. One newspaper report quotes both opposition and government politicians calling Treasury's arguments in the 1994 report "totally stupid" and "silly".[3]

Undoubtedly Treasury took part in the "radical, often controversial", reforms of 1984 to 1996. The department's statutory defined role is not only to provide economic, financial and commercial advice and information to the government, but also to implement specific economic and financial policies.

---

1 Jonathan Boston, "The Treasury: Its Role, Philosophy and Influence", in Hyam Gold, ed., *New Zealand Politics in Perspective* (Auckland: Longman Paul, third Edition, 1992), p. 195.

2 Len Bayliss, *Prosperity Mislaid* (Wellington: GP Publications, 1994), p. 75.

3 Diane Keenan, "Plan aims for lift in police strength", *The Press* April 11, 1997, p. 3.

Accordingly, this thesis is not interested in examining how closely Treasury's policy prescriptions match those of the reforms implemented by the Labour and National governments. The focus of this thesis is on whether Treasury's underlying political philosophy matched the neo-liberal philosophy of the parties implementing reform. The reason for this is two-fold: first, it could be expected that as a state agency, providing advice to governments of all political hues, that Treasury would be neutral in its advice, presenting a range of options from which the ruling party could choose. Second, neo-liberalism has important implications for the relations between state and society, the most important of which is that it eliminates any notions of collective interest, instead focusing on individualism and the superiority of the unfettered free market in allowing individuals to pursue -- and attain -- their own interests. It is the second of these reasons that is the main focus for this thesis. Since the 1930s and the introduction of the Keynesian welfare state, New Zealanders have become accustomed to living in a particular type of community. Under both Labour and National governments, New Zealand progressively developed "a comprehensive range of social services characterised by underlying notions of egalitarianism, humanitarianism, and a conviction that the state has a responsibility for the health, education and welfare of its citizens".[4] Neo-liberal prescriptions that limit the role of the state are likely to eliminate these notions, which may not be what New Zealanders want. It is important to know whether Treasury is reflecting the views of the public, given that as a state agency its role is to present policy that helps the state to achieve society's goals.

Writing soon after the 1996 election, National member of Parliament Simon Upton linked Treasury to the neo-liberal philosophy he said had driven politics for the past 12 years.[5] He claimed that from 1984 to 1996 New Zealand had been ruled by a single government that "masqueraded under two different political banners". Both Labour and National had recognised the importance of implementing change in the New Zealand economy, and both parties "drank at the neo-liberal well

---

4 Task Force on Economic and Social Planning, *New Zealand at the Turning Point* (Wellington: Government Printing Office, 1976), p. 97.

5 Simon Upton, "Without a crisis looming, reform in New Zealand is going to be much harder", *The Press* November 5, 1996, p. 11.

because the old one had quite simply dried up". Upton wrote that the coalition governments that were part of the new MMP environment would bring politics, or a plurality of political ideas and options, back to the centre stage, "and there's nothing in Treasury's tool kit about how to deal with it". With this statement, Upton is claiming that for the past 12 years Treasury had -- like the "single" government -- "imbibed a particular economic logic", and eliminated alternative policy options.

It is not clear that Treasury would accept this neo-liberal tag; in fact, it has repeatedly claimed that it provides "independent economic and financial advice and information to the government".[6] This is based on its assumption that it is possible to split the economic and political spheres, and that economic theory is not a political, but a technical, scientific matter. Economics is value-free and politically neutral because economics is devoid of value judgments and focuses only on the methods (means) to achieve society's goals (ends). Based on these views, the department can claim that its advice to the government reflects the apolitical nature of economics, and the policy framework it offered was not political, but simply reflected the only method by which the government could reverse New Zealand's economic decline and achieve the economic growth necessary for New Zealand's future prosperity. In this sense, Ann Mari May's comment on economic theory is particularly apt to Treasury: "Perhaps because of the adamant claims that economics is scientific and, hence, apolitical, economic theory is all the more effective in mystifying the political nature of its inquiry."[7]

Although Treasury has been the focus of much attention during the reform period, little has been written on its political philosophy. Most of the scrutiny of the department's policy has been confined to analyses of the economics of its economic policy stance and recommendations, which are issues outside the scope of this thesis. While texts on New Zealand politics recognise the importance of

---

6 New Zealand Treasury, *The Treasury: A Profile* (Wellington: Government Printer, 1992), p. 2., quoted in Shaun Goldfinch and Brian Roper, "Treasury's Role in State Policy Formulation during the Post-War Era" in Brian Roper and Chris Rudd, eds., *State and Economy in New Zealand* (Auckland: Oxford University Press, 1993), p. 64.

7 Ann Mari May, "The Challenge of Feminist Economics", in Charles J. Whalen, ed., *Political Economy for the 21st Century* (Armonk, New York: M.E. Sharpe, 1996), p. 74.

Treasury, the writing tends to focus on the mechanics of the department's role as an economic and financial adviser, or on the economic policy recommendations themselves.[8] Jonathan Boston, perhaps the most widely published commentator on Treasury, wrote in 1989 that by the 1980s, Treasury had adopted a monetarist perspective, but this says little about its underlying political philosophy.[9] Brian Easton looked briefly at the political philosophy of the second briefing paper being examined in this thesis, *Government Management* (1987), and published a seven-page article in *Political Science*, but it is not detailed, and does not entail a comparison to Treasury's other briefing papers to see whether its stance is consistent.[10]

A major difficulty with discovering Treasury's political philosophy is deciding which policy documents to analyse, given that Treasury can claim the stance of many of its policy papers simply reflects that of the current government. For example, in an attack on Paul Dalziel's criticism of the "rhetoric" of the 1990 briefing paper, Treasury employees Peter Gorringe and Peter Bushnell point out that policy papers are influenced by the government of the day.[11] The minister of finance exercises control over the detail of the areas in which Treasury gives policy advice, and "Treasury continually applies its resources to tasks set by the ministers of finance".[12] An examination of the briefing papers prepared for incoming governments after elections resolves this problem, however, because the papers are prepared for ministers of either party.[13] As Gorringe and Bushnell themselves

---

8 Boston's chapter in Gold, for example, has only four pages on "The Treasury Line", in which he focuses on the shift in Treasury's thinking from Keynesianism to monetarism. He does, however, comment that the theories employed by Treasury "have a tendency to generate relatively conservative or right-wing policy conclusions". Boston in Gold, *op. cit.*, pp. 200-204.

9 Jonathan Boston, "The Treasury and the Organisation of Economic Advice: Some International Comparisons", in Brian Easton, ed., *The Making of Rogernomics* (Auckland: Auckland University Press, 1989), p. 76.

10 Brian Easton, "*Government Management*; A Review of its Political Content", *Political Science* vol. 42 no. 2 (December 1990), pp. 35-42.

11 Peter Gorringe and Peter Bushnell, "The Rhetoric of 'The Rhetoric of Treasury'" *New Zealand Economic Papers* vol. 26 no. 1 (1992), p. 134.

12 *Ibid.*, p. 134.

13 Bayliss says that any "thorough" analysis of Treasury's performance would require full access to all the major economic policy papers written in the past 20 years or so. "However, a fairly accurate picture of Treasury's thinking can be gained from public documents such as those prepared for the post-election government and supporting papers for the budget". Bayliss, *op. cit.*, p. 75.

observe, a briefing paper presents to a new minister an overview of the main issues facing the economy, introduces Treasury's key concerns, and highlights the areas where -- in the department's view -- policy change is "considered appropriate".[14] Referring to the 1990 paper, Gorringe and Bushnell say:

> Since it was completed before the polls closed, it had to be suitable for an initial briefing to a new Minister. Its length and degree of detail took into account that the first requirement of a Minister would be for an overview of the key issues. ... It started with the assumption that Governments of either party would have as their primary economic goals the achievement of faster economic growth and fuller employment.[15]

Such a description is accurate for the other papers examined in this thesis, and also highlights that the term "briefing" is somewhat of a misnomer. As will be touched on in chapter two, the first three briefing papers could not be described as "brief" in either their length or detail.

An analysis of Treasury's briefing papers for the reform period reveals that it proffered a policy direction that sits comfortably within neo-liberal ideology. The briefing papers of 1984, 1987, 1990 and 1993 did not offer a middle-of-the-road policy or suggest a range of programme options from which ministers could choose after considering the needs and wants of the electorate. Instead, Treasury consistently argued for one option to "rescue" the New Zealand economy -- that of less state intervention and more reliance on the mechanisms of the free market. Such a stance conforms to neo-liberal precepts that limit the role of the state to setting and enforcing rules to allow "free and voluntary" exchange in the market. In arguing for these policies, Treasury shifted into the market or private sector a wide range of decisions previously seen as the realm of the public sector and politicians. While Treasury claimed its framework was apolitical, reflecting its role as a "non-political", "rigorously neutral" and "independent" adviser to the government, the economic policies it advocated were not apolitical.[16] In introducing the market to all levels of policy, Treasury's plan to solve New Zealand's economic crisis centred on a switch from the prevailing social democratic philosophy of the Keynesian welfare state and

---

14 Gorringe and Bushnell, *op. cit.*, p. 128.

15 *Ibid.*, p. 128.

16 Goldfinch and Roper, *op. cit.*, p. 51.

its associated intervention to a neo-liberal philosophy of minimum state, maximum market.

Before outlining how this thesis will present its arguments, it is necessary to set the parameters of the analysis and outline what will not be covered. While it argues that Treasury's briefing papers reveal the department has a neo-liberal political philosophy, it will not discuss the individuals employed by Treasury or their personal views and motivations. For this reason, this thesis does not include interviews with any Treasury personnel, but focuses solely on the briefing papers. This thesis will not examine Treasury's links to, or influence over, politicians from any political party either in government or in opposition, as this is not relevant to the argument.[17] Nor will it examine Treasury's fiscal and monetary stance, or -- as discussed in the opening paragraphs -- whether its policy framework was implemented. It will not offer a detailed discussion of Treasury's functions and role, nor whether it fulfilled its task in offering a single policy framework, beyond some brief concluding comments on the expected role of a state agency.

This thesis will not analyse the briefing papers in terms of an international perspective on the need for economic rationalism. Undoubtedly, as Barry Hindess points out, globalisation has changed how governments perceive the problem of national economic management, because "national economies are no longer the relatively self-contained unities of earlier liberal conceptualisations".[18] Hindess argues that much of what passes for neo-liberalism is responding to the emergence of a new problem of economic security in an international sense, and his argument has some validity when considering Treasury's stance. Treasury acknowledges that New Zealand's economy has to be able to compete with others in the global economy, and that there are internal as well as external reasons why this

---

17 This issue has been covered elsewhere, especially in W. Hugh Oliver, "The Labour Caucus and Economic Policy Formation, 1981 to 1984", in Easton, *op. cit.*, pp. 11-52., and Andrew W. Mansfield, *The Power Elite: the Treasury and N.Z. Business Roundtable's Power in the Formation of the Privatisation Programme 1984-1987 - A Theoretical Analysis*. (Canterbury: University of Canterbury, M.A. Thesis, 1990).

18 Barry Hindess, "Neo-liberalism and the National Economy", in M. Dean and B. Hindess, eds., *Governing Australia* (Cambridge: Cambridge University Press, 1997), pp. 3, 6.

might not be achieved, but Treasury's main focus is on domestic issues for domestic outcomes. That is, economic growth is to be pursued, not only so that New Zealand is internationally competitive, but because it increases incomes and opportunities for citizens. In this sense, while it is true that areas of community life outside the economy are "increasingly perceived in terms of their contributions to economic performance", in its briefing papers at least, Treasury still treats the performance or growth in the national economy as a resource contributing to the well-being of the community.[19]

In offering criticisms of some of the assumptions and outcomes of neo-liberal ideology, this thesis will not try to offer an alternative position. Nor is this thesis trying to diminish economic theory. As May aptly says:

> Despite what we have been told, recognition of the political nature of economic inquiry will not diminish, taint or lessen our understanding of economic matters. Such recognition offers, instead, the hope of having an honest intelligent conversation about material reproduction.[20]

In short, this thesis is interested only in Treasury's underlying political philosophy as revealed in the briefing papers to the incoming governments of 1984, 1987, 1990 and 1993; a criticism of some of the weaknesses of the neo-liberal model and how these affect anticipated outcomes in the social policy areas of health and education; and the possible effects of neo-liberalism on the political community. It claims only that as Treasury is a body "central to machinery of government", it is important to understand the political philosophy underpinning Treasury's economic theory because of the consequences for New Zealanders and the type of community in which they live should the policy framework be implemented. This thesis acknowledges, as Treasury employees Peter Gorringe and Peter Bushnell point out, that Treasury is not the government's only source of economic and financial advice.[21] However, it would be naive to believe that the government does not regard its own Treasury as a

---

19 *Ibid.*, p. 19.

20 May, *op. cit.*, p. 75.

21 Gorringe and Bushnell, *op. cit.*, p. 134. "Many people and groups are willing to offer, or sell, advice -- business people, trade unions, other special interest groups, Ministers' own staffs, the Government Caucus, the political parties, the Opposition, the media, independent economic commentators, constituents and so on. Ministers actively seek and listen to advice from all these quarters. Ministers and others in Government also have their own beliefs, objectives, personal values, and views of what is good for the country." While the point is noted, it is questionable whether a government would listen to some of these groups more than -- or even as much as -- its own Treasury.

important source of economic advice, given that this is one of its main functions. Using Treasury's own arguments, it could be seen as an inefficient use of public resources if Treasury was funded to provide advice that the government then consistently ignored.

Chapter one provides a context for the briefing papers, giving a brief overview of the structure of the New Zealand economy and highlighting the role of state intervention in its development.[22] It examines the shift in paradigms from Keynesianism and an emphasis on the welfare state to monetarism and the new focus on the mechanisms of the free market as the best means of achieving a better life for all New Zealanders. This chapter discusses the political consensus over the direction of economic reform, and raises the claim that the reforms were apolitical in that "politicians were prepared to step aside from politics for a while", in order to achieve gains in economic welfare. It also briefly outlines the functions of Treasury, and its change from a Keynesian to monetarist policy framework. It concludes with a brief discussions of how Treasury's economic philosophy is based on the idea that economics can be split from politics, and that economics is value-free and simply a means to achieve society's ends.

Chapter two will examine Treasury's arguments in favour of a much narrower role for the state, focusing in particular on the state versus market model presented in *Government Management* (1987). According to this model, the state can never produce better results for New Zealanders than the market, because it faces more pitfalls than the private sector when seeking solutions to social problems. Treasury also advocates a greater role for the market because market mechanisms promote more efficient use of resources and decreased dependence on the state, which will promote the economic growth needed to resolve the economic crisis. In setting out Treasury's arguments, this chapter raises many of the issues that will be

---

22 New Zealand Treasury, *Economic Management* (Wellington: Government Printer, 1984); New Zealand Treasury, *Government Management* (Wellington: Government Printer, 1987); New Zealand Treasury, *Briefing to the Incoming Government 1990* (Wellington: GP Print Ltd, 1990); and New Zealand Treasury, *Briefing to the Incoming Government 1993* (Wellington: GP Print Ltd, 1993). After the first mention in each chapter the references to the Treasury briefing papers will be abbreviated to: *Economic Management; Government Management; Briefing 1990;* and *Briefing 1993.*

discussed later in the thesis. An important section of the chapter shows that Treasury's argument is constructed in a vocabulary that neutralises the political elements of its suggestions, presenting its arguments as logical and common sense. It also highlights the difficulties in Treasury's use of language, that is, the department's arguments are often circular and confusing, partly because it does not define some of the terms that it uses, and it uses them in ways that are different from their generally accepted meanings.[23] Treasury's use of the term "rights", for example, and its inclusion of efficiency as a defining characteristic of rights, does not seem to fit with generally understood notions of rights. Also, Treasury does not define what it means by the terms "government" or "state", and uses the terms in several different ways. As Easton observes:

> The term [government] is used with different meanings in different places ranging from the Executive Council, to the Cabinet and Caucus, to the policy making bodies including the advice agencies, to all the political and public agencies. [*Government Management*] suggests "we think of the Government as 'the political executive in action'", but it does not stick with such a definition.[24]

It is not clear whether or not Treasury includes itself in the term "government". Because of this difficulty, this thesis has adopted the practice of using the term "state" when referring to both the ruling party and its agencies, and "government" when referring to a specific governing administration. It retains Treasury's original use when quoting from the briefing papers.

Chapter three moves from the details of briefing papers to examine Treasury's claims to political neutrality. This chapter argues that the "science" behind Treasury's model, that economics is a technical matter following immutable scientific laws and is therefore neutral between values, does not hold up to scrutiny. It raises three areas where the assumptions are weak: that markets find their way back to equilibrium through the supply and demand mechanisms; that people can be reduced to rational, self-interested maximisers, and that markets allow the maximisation of choice. It will argue that markets may not perform as expected; that individuals are

---

[23] An example of Treasury's circular argument comes when it defines social policy as: "For the purposes of the post-election briefing, and for this annex, no strict definition is attempted; social policy is simply that list of activities that are normally understood to be social policy." *Government Management, ibid.*, pp. 394, 125. Further examples to justify the claims of this thesis will be presented in chapter two.

[24] Easton, "*Government Management*; A Review of its Political Content", *op. cit.*, pp. 35, 36.

not necessarily solely self-interested and may not respond to monetary incentives as envisaged; and that the choice maximised in the free market is simple freedom from coercion, which does not give people freedom to pursue their opportunities. This chapter will show that once the "science" is eliminated from the free-market model, what remains is a neo-liberal political philosophy, which justifies the free market and the minimum state.

Chapter four will examine what happens in the social policy areas of health and education when the model is applied, given the weaknesses outlined in chapter three. An important issue raised at the beginning of this chapter is Treasury's view of social policy and social well-being, which it sees as essentially a private matter, that is, private in the sense of being specific to the individual. In this way, it is able to argue that individual well-being is best fulfilled by individuals being free from state intervention to pursue their own notions of well-being in the market. However, this view ignores that society may have collective goals, such as ensuring that all of its members are provided with quality health and education. This chapter concludes that society may not want the market model applied to health and education because these areas have community values beyond that of simple supply and demand.

Chapter five draws the arguments of the thesis together to look at the implications of neo-liberalism on the political community, and what happens to collective interests and common goals. Neo-liberalism wants life in the community to be built on individual freedom and initiative, which means reducing the role of the state to setting and enforcing the rules that protect life, liberty and estate. Individual liberty is thus perceived as a primary goal of the state, and collective good, or the over-all good of society, is achieved when all individuals are left free to pursue their own notions of well-being. This means that neo-liberalism does not accept either collective interests or social justice, both of which are seen as coercive, a disincentive for individuals to look after themselves, and stultifying of the economy. Treasury's use of the market model changes the relations between citizens and the state to mirror those of parties in the private sector, with the result that social service provision is stripped of its human factors and commodified (given a monetary value), and is thus reduced to purely economic or market relations. This new state-society relationship limits the ability of citizens to exert control over the types and amount of goods and services the state supplies to meet their needs and wants. The state's role is diminished from facilitating the achievement of the community's collective goals to setting the rules of the market within which individuals act to achieve their individual goals. In concluding, this thesis will argue that New Zealanders have strong notions of their democracy, what they are entitled to as citizens, and what the state should provide. These notions contradict those of Treasury's neo-liberal framework. This suggests that if the government accepts Treasury's policy direction there is a risk of sacrificing the type of community in which New Zealanders want to live.

CHAPTER ONE
Putting Treasury's briefing papers in context

Introduction

New Zealand's transformation in the 1980s from a model of state intervention to a bastion of the free market has been the subject of much analysis and discussion from academic institutions and the media to pubs and community halls across the country. By now the story is a familiar one: in response to the economic crisis of the 1970s and early 1980s, the new Labour government in 1984 turned from the Keynesian economic consensus and its associated commitment to the welfare state, to monetarism and its commitment to market forces, a shift that has continued through the change to a National government into the 1990s. The mechanics and resulting outcomes of this fundamental alteration in the underlying analytical framework for policy-making have been well detailed in the literature on New Zealand politics. Since 1984, there has been a major change in the structure of the economy and the direction of economic policy to a focus on the mechanisms of the free market and its alleged ability to promote both equity and efficiency in the use of the nation's resources. Throughout the 1980s and early 1990s, political and bureaucratic elites have reviewed what the state should try to do in the economic and social fields, and concluded that the best policy instruments to achieve the objectives of the state are those that set the rules for the operation of a free market. As a result, changes were introduced in both the direct activities of the public sector, and the legislative and regulative environment within which the private sector operates.

Although these changes were focused on the economy, they also reflected a change in the political philosophy underlying the actions of the state, with serious repercussions on the social policies pursued by the Labour and National governments. This chapter sets the scene for an analysis of the political implications of the policy framework promoted by Treasury in its briefing papers. It will give a brief overview of the structure of the New Zealand economy and how state intervention helped shape its development in line with the egalitarian notions of the Keynesian welfare state, according to which the state should have an active and major role in the nation's economic affairs to alleviate the failings of the market, promote social justice, and generally achieve the betterment of the human condition. This chapter will then examine the shift in paradigms to monetarism and a focus on the free market as a means of fulfilling the welfare aims of the state, and the consensus that arose between the Labour and National parties that major economic reform would improve New Zealand's economic performance and thereby enhance the lives of New Zealanders. It will conclude with a discussion of Treasury's function as the state's main source of economic advice, and the department's role in the transition to a new faith in the free market as the solution to all of the country's problems.[1]

The New Zealand economy in perspective

The structure of the New Zealand economy can be traced to the middle of the nineteenth century when New Zealand was annexed by Britain and incorporated into the world of international trade.[2] New Zealand prospered as an off-shore farm for its colonial master, exporting wool, dairy products, and sheep-meat, which financed a wide range of imports allowing New Zealanders to enjoy the same high standard of living available in the industrialised countries of Europe and North America.[3] In a world in which 75% of trade was in agricultural products, New Zealand enjoyed remarkable success and prosperity, but its small size left it vulnerable to fluctuations in the global economy. World market prices for New

---

1 The argument about the international effect on national economies will not be covered in this thesis. Undoubtedly, as Hindess points out, globalisation has changed "*governmental perceptions* of the problem of national economic management", and "national economies are no longer the relatively self-contained unities of earlier liberal conceptualisations". Author's emphasis. Barry Hindess, "Neo-liberalism and the National Economy", in M. Dean and B. Hindess, eds., *Governing Australia* (Cambridge: Cambridge University Press, 1997), pp. 3, 6. Treasury's economic prescriptions acknowledge that New Zealand has to be able to compete with other economies, but the briefing papers focus on domestic reasons for poor economic performance, domestic solutions, and the domestic consequences of improved economic growth (that is, increased income and opportunities for New Zealanders). That such a narrow focus is simplistic in a world of increasing global interdependence is not in dispute.

2 Paul Wooding, "New Zealand in the International Economy", in Brian Roper and Chris Rudd, eds., *State and Economy in New Zealand* (Auckland: Oxford University Press, 1993), p. 92.

3 Wooding, *ibid.*, p. 93., and Statistics New Zealand, *New Zealand Official Yearbook 1996* (Wellington: Statistics New Zealand, 1996), p. 343.

Zealand agricultural exports were volatile because its traded volumes were only a small proportion of total output, and small movements on either the supply or demand side translated into large movements on price. Export income fluctuated, falling during world recessions such as the Great Depression in the 1930s, and rising during commodity booms such as those during the Korean War of 1950-51 and the commodity shortage of 1972-73.[4] The political response to such vulnerability was the elaboration of a continually interventionist state.[5]

The state intervened in the economy from the beginning: it was responsible for building and operating infrastructure such as railways, and when gaps in the institutions available were not otherwise filled, as with insurance companies and some forms of financial institutions, a state agency was created.[6] Until the 1930s the state's role was largely supplementary to the private sector rather than seeking to control it. During the Great Depression, however, the state's responsibilities increased as it struggled to deal with rising unemployment and falling export prices. In attempts to bring some stability to the vulnerable economy, the state began introducing regulations aimed at rectifying the "market failures" exacerbated by the Depression in the 1930s and war-time conditions in the 1940s. Licensing, tariffs, exchange and currency controls, and standards regulations were used to help protect the balance of payments, as well as to ensure a stable market for industry, utilise domestic resources to the fullest extent, and encourage investment and productivity. Import substitution policies, where incentives and subsidies were paid to domestic firms to produce equivalents to imported products, aimed both to ensure local jobs and to reduce the demand for imports, thus improving the balance of payments. Throughout the 1950s and 1960s, the basic structure of the economy came to depend on these regulations. New Zealand domestic manufacturers were protected from international competition by wide-ranging controls and an elaborate system of import-substitution programmes and practices subsequently overlaid by an expanding

---

4 Wooding, *ibid.*, p. 93.

5 Nick Perry, "Upside Down or Downside Up? Sectoral Interests, Structural Change, and Public Policy", in John Deeks and Nick Perry, eds., *Controlling Interests: Business, the State and Society in New Zealand* (Auckland: Auckland University Press, 1992), p. 41.

6 Statistics New Zealand, *op. cit.*, p. 343.

range of export incentives.[7] In such an environment, domestic investors could be confident of their markets and the businesses they funded kept the rate of unemployment low by ensuring demand for labour was high.[8]

In the 1960s, exporters began to have problems finding markets for their products. Britain, which had taken about 90% of New Zealand's exports until the 1950s, became saturated with primary products, and surpluses generated by the Common Agricultural Policy of the European Economic Community frustrated attempts to redirect exports to other countries.[9] From 1962, in an attempt to expand the export base in order to pay for increasing imports, incentives were provided to exporters of non-traditional export goods. When Britain joined the EEC in 1973, New Zealand faced limitations on its previously guaranteed access to what was still a major purchaser in a world where agricultural products now accounted for only 9% of world trade. In 1978 supplementary minimum prices were introduced in a further bid to help struggling farmers. In terms of New Zealand's prosperity, the 1970s was the decade that highlighted "the end of the golden weather", marking the descent into "an epoch of stagnation, declining incomes, and rising unemployment".[10] In the world recession sparked by the 1973 OPEC oil shock, New Zealand suffered the most severe fall in per capita real income of any OECD country, with a decline between 1973 and 1977 of 11.5%.[11] The National government of prime minister Robert Muldoon responded with growth or "think big" projects -- huge state-funded ventures aimed at developing New Zealand's hydrocarbon resources, which had become more valuable in line with the world price of oil.[12] As the economy suffered under adverse changes in New Zealand's terms of trade, persistent low growth, high inflation, and mounting structural problems, the National government responded with comprehensive wage and price controls, a highly regulated capital market, tight exchange rate controls, high import tariffs and import licensing constraints, as well as

---

7 Perry, *op. cit.*, p. 38.
8 Statistics New Zealand, *op. cit.*, p. 345.
9 Wooding, *op. cit.*, p. 93.
10 Brian Roper, "The End of the Golden Weather: New Zealand's Economic Crisis", in Roper and Rudd , *op. cit.*, p. 1.
11 Perry, *op. cit.*, p. 38.
12 Statistics New Zealand, *op. cit.*, p. 346.

subsidies and direct government investment programmes. By the 1980s, "Fortress New Zealand" had adopted a stance of "domestic defence" in which it maintained high protective barriers against foreign manufactured goods and a dependence on the export of primary products to a narrow range of markets.[13]

Keynesian intervention

Underlying the interventionist economic policies was a political commitment to the state having an active and major role in the nation's economic affairs, in the promotion of social justice, and in the betterment of the human condition.[14] Keynesian economics, the dominant framework of the inter-war and post-war period, was formed in response to the failings of private enterprise and the free market during the Great Depression of the 1930s. Keynesians argued that the idealised free market economy of an "automatic, spontaneous, and harmonious tendency" towards a market-clearing general equilibrium in which all resources were fully employed, was not realistic in a world of monopolistic firms and strong trade unions, where the efficiency properties of the market were inevitably compromised.[15] The free-market economy was, in fact, inherently unstable, and when major disturbances occurred, the price signals from the marketplace could be confused or misleading rather than leading the way back to equilibrium.[16] Keynesians said the state, therefore, had a role to play in managing aggregate demand to maintain full employment, provide social welfare, enforce contracts in the labour market, undertake public works to develop the infrastructure of the economy, provide public housing, and so on.[17] Accordingly, the Keynesian welfare state was "an inherently politicised vision of the economy revolving around sustained growth within a mixed economic system, where continued private production and market dynamics could be

---

13 Ian McAllister and Frank Vowles, "The Rise of New Politics and Market Liberalism in Australia and New Zealand", *British Journal of Political Science* vol. 24 (1994), p. 387.

14 Jonathan Boston and Martin Holland, "The Fourth Labour Government: Transforming the Political Agenda", in Jonathan Boston and Martin Holland, eds., *The Fourth Labour Government: Radical Politics in New Zealand* (Auckland: Oxford University Press, 1987), p. 3.

15 Robert Scollay, Susan St John, and John Horsman, *Macroeconomics and the New Zealand Economy* (Auckland: Longman Paul, 1989), p. 152; and Shaun Goldfinch and Brian Roper, "Treasury's Role in State Policy Formulation during the Post-War Era", in Roper and Rudd, *op. cit.*, p. 54.

16 Scollay et al, *ibid.*, p. 152.

17 Goldfinch and Roper, *op. cit.*, p. 54.

sufficiently harnessed by a redistributive state to meet the needs of the broader, co-operative working population".[18] The first Labour Government of 1935-1949 pursued this vision: it introduced benefits for the unemployed, increased pensions, restored cut wages (1936), established a minimum basic wage, gave dairy farmers guaranteed prices, reintroduced compulsory arbitration (1937), and started a series of public works on roads, railways, and hydro-electric power stations. The core elements of the welfare state -- public spending, taxes and public employment -- gave the state greater leverage in its control of the economy.

As in other western democracies, policies based on Keynesian economics introduced in the 1930s under social-democratic and socialist governments were accepted by conservative parties in the 1950s and 1960s, with most governments endorsing the welfare state and a degree of income redistribution.[19] The role of the market as an allocative mechanism was diminished and the legitimacy of market outcomes questioned, leading to a highly interventionist mode of economic management that aimed to benefit all citizens. In New Zealand the aim was to "ensure that economic change was planned and gradual, that the economy was shielded as much as possible from the negative consequences of destabilising events abroad, that the costs of economic adjustment were evenly spread throughout the community, and that full employment was maintained -- even at the price of substantial foreign borrowing."[20] By 1984, New Zealand's welfare state, and the general commitment to it by whichever party was in power, were well-established. This is not to argue that National governments, particularly the third National government led by Robert Muldoon from 1975-1984, were "paragon[s] of Keynesian virtue".[21] While accepting some intervention in the economy, National was also committed to "emphasise in all policies the freedom and independence of the individual and the promotion of individual effort, initiative and opportunity

---

18 David Denemark, "Social Democracy and the Politics of Crisis in New Zealand, Britain, and Sweden", in Martin Holland and Jonathan Boston, eds., *The Fourth Labour Government: Politics and Policy in New Zealand* (Auckland: Oxford University Press, Second Edition, 1990), p. 270.

19 Jonathan Boston, "Thatcherism and Rogernomics: Changing the Rules of the Game -- Comparisons and Contrasts", *Political Science* vol. 39 no. 2 (1987), p. 129.

20 Jonathan Boston and Martin Holland, "The Fourth Labour Government: Transforming the Political Agenda", in Boston and Holland, *op. cit.*, p. 3.

21 Roper, "The End of the Golden Weather", *op. cit.*, p. 9.

coupled with responsibility" and "to encourage sound economic growth through competition and the promotion of individual ownership and private enterprise".[22] However, certain values, including egalitarian notions based on state provision and funding of education, health, justice and social welfare had become entrenched, and state expenditure was critical to activities "seen by many as essential to the social life of New Zealand".[23]

Shifting paradigms

When the Labour Party came to power in 1984, it assumed control of a major economic crisis that many claimed was a direct result of decades of protectionism introduced by successive governments to insulate the New Zealand economy from the international marketplace.[24] The myriad of protections and regulations covering the economy had not resolved a growing economic crisis. As early as 1962, a report pointed to the problems within the New Zealand economy, saying that between 1949 and 1960 it had the unfortunate distinction of one of the slowest annual rates of growth of productivity among advanced countries.[25] From 1960 to 1984, the rate fell even further to an average of 1.2%, lower than any other OECD country. A 1989 OECD report claimed that by 1984, New Zealand was one of the most highly regulated of its member economies.[26] New Zealand manufacturers were deemed costly and inefficient compared to their international competitors, and the terms of trade were worsening as New Zealand remained dependent on exports of low-profit primary-based products while importing high-cost raw materials and processed products.

---

22 New Zealand National Party, *Constitution and Rules of the New Zealand National Party,* (Wellington: New Zealand National Party, 1986) cited in Boston and Holland, *op. cit.,* p. 38. Roper also points out that Keynes's support for the welfare state did not back Muldoon's subsidies for agricultural production (which inhibited the diversification of New Zealand's export base) or the "think big" projects. Nor did Keynes mean the "*ad hoc* and inconsistent nature of Muldoon's economic management". Roper, *ibid.,* p. 9.

23 Statistics New Zealand, *op. cit.*, p. 347.

24 Catriona McLennan, "Trade Policy for the 1990s", *The Press* May 24, 1993.

25 Monetary and Economic Council Report 1962 quoted in Roger Douglas, *Unfinished Business* (Auckland: Random House, 1993), p. 14. This is not, however, universally accepted. Brian Easton says that real GDP was "going at about the same rate as the rest of the OECD up to the time of the reforms [1984 onwards]". Easton, "Ignoring the Critics", *The Listener* February 15, 1997, p. 60.

26 OECD, *Economic Survey New Zealand* (Paris: OECD, 1989), quoted in Chris Rudd, "Politics and Markets: The Role of the State in the New Zealand Economy", in Holland and Boston, *op. cit.*, p. 89.

Increasingly, influential members of New Zealand's economic and political elites were convinced that the economic problems were structural in origin. Many began to argue for a new order based on the fundamental reversal of values and priorities, saying over-protection of the economy had led to a misallocation of resources away from internationally competitive export-oriented sectors. While intervention had resulted in development in secondary industries producing for a domestic market, it had also brought "poor quality and high prices, a cost-plus mentality in industry, a focus on political strategy rather than business strategy, and continued failure to gain a close understanding of foreign markets."[27] Protection had also led to unintended outcomes, with some industries receiving high levels of protection while others faced high costs because they had to buy products from sheltered industries. Those who wanted to escape the small New Zealand market and export to the world found that their high costs rendered them uncompetitive.[28] Pressure to deregulate the economy began to increase as many began to feel that the maintenance of high level protection without dramatic restructuring had merely delayed the inevitable crisis. By 1984, it was argued that New Zealand's worsening economic situation was calling for a reversal of strategy; a more "efficient" New Zealand economy was needed.[29]

Taking power at the moment that New Zealand was plunged into an exchange rate crisis, Labour moved rapidly to assert the new direction for the economy in what one economist described as a "sea-change" in New Zealand macroeconomic policy.[30] "The defeat of the Muldoon government, and the appointment of Roger Douglas to be the new Minister of Finance, ushered in an era of sweeping deregulation and faith in market forces to solve the problems of the New

---

27 Graham T. Crocombe, Michael J. Enright, and Michael E. Porter, *Upgrading New Zealand's Competitive Advantage* (Auckland: Oxford University Press, 1991), p. 151. The book is a report of the "Porter Project" in which Harvard Business School lecturers Porter and Enright, in the words of project director Crocombe, "agreed to donate their time to an independent study of the New Zealand economy", p. 10. In the foreword to the book, Porter says the project result "highlights how New Zealand's institutions and policies have retarded the progress of the economy", and the group argues along similar lines to Treasury for a decreased role for the state and an increased role for the market.

28 Wooding, *op. cit.*, p. 106.

29 *Ibid.*, p. 106.

30 Geoff Bertram, "Keynesianism, Neo-classicism and the State", Roper and Rudd, *op. cit.*, p.26.

Zealand economy."[31] The policy regime switched from Muldoon's interventionism and corporatism, where the state formed close alliances with industry and the unions, to Douglas's anti-statist and anti-corporatist crusade.[32] Labour's rationale was that regulation, while it might be advantageous for particular industries in the short-run, had led to the stifling of the market and poor economic performance. To improve the general performance of the business sector, regulating constraints had to be minimised or abandoned.[33] Labour embarked on a massive programme of reform: economic policy was reoriented from a decades-old trend towards protection, regulation, intervention, and state ownership to liberalisation, deregulation, and privatisation. The state's trading activities were commercialised and privatised, and the public sector reformed, shifting emphasis from the state funding all programmes to the purchase by ministers of defined services from the different government departments. Few sectors of the economy were left untouched as New Zealand was transformed into one of the least-regulated OECD economies, "practising what market-oriented reformers in other countries preach".[34]

The new policy-making framework was monetarism, according to which the economy would spontaneously generate non-inflationary economic growth and lower unemployment if the state balanced the budget, reduced taxation, slashed social spending, and liberalised regulatory control over markets.[35] Such an approach responded to what monetarists saw as the failure of Keynesian stabilisation policies to cope with unemployment and rising prices. It targeted key areas of a disappointing economic performance, including "poor, inconsistent macroeconomic management,

---

31 *Ibid.*, p. 26.

32 Oliver offers a useful definition of corporatism as "the formulation and implementation of government policies through the mechanisms of a negotiated and consensual alliance of labour, capital, and the state". W. Hugh Oliver, "The Labour Caucus and Economic Policy Formation, 1981 to 1984", in Brian Easton, ed., *The Making of Rogernomics* (Auckland: Auckland University Press, 1989), p. 11. Oliver's chapter discusses how the Labour Party came to abandon corporatism.

33 John Deeks, "Introduction: Business, Government and Pressure Group Politics", in Deeks and Perry, *op. cit.*, p. 9.

34 Steve Hoadley, *The New Zealand Foreign Affairs Handbook* (Auckland: Oxford University Press, with the Institute of International Affairs, Wellington, 1992), p. 70.

35 Roper, *op. cit.*, p. 11. Donald Rutherford's *Dictionary of Economics* says monetarism is "popularly thought of as a tough fiscal stance and careful attention to monetary variables when targeting the economy". Donald Rutherford, *Dictionary of Economics* (London and New York: Routledge, 1992), p. 10.

too much bureaucratic regulation of the economy, an excessively large state sector, poor industrial relations, an inflexible labour market, over-generous and inappropriately targeted welfare assistance, a decline in entrepreneurial initiative, and a rigid social system."[36] It also targeted what was seen as a growing "dependence" on welfare, which was based on the allegation that New Zealanders had become accustomed to turning to the state first to meet their needs rather than relying on their own initiative.[37] Cutting welfare benefits was seen as a way of reducing state expenditure and encouraging people to be more self-reliant and productive, all of which would have the result of aiding economic growth. From 1984 to 1996, successive governments followed monetarist prescriptions: first Labour then National implemented legislation and reforms to liberalise the economy, privatise state assets, cut social spending, and reduce the power of the labour movement.

A consensus in favour of change

In a 1993 referendum on New Zealand's future electoral system, voters overwhelmingly supported a radical change to a system that electoral reformists said was increasingly unrepresentative. This was a result of their outrage in 1990 when, after ousting the Labour government over the radical economic, administrative, and social reforms of the previous six years, they found the reforms not only continued, but enhanced by the replacement National government.[38] The result of the ill-feeling against National was that it became, "according to public opinion polls, even more unpopular than the Labour government it had replaced".[39] Cynics remarked that there was so little difference between the parties that whichever the voters chose, they got the same policies. What New Zealanders faced was a political consensus between

---

36 Jonathan Boston, "Thatcherism and Rogernomics", *op. cit.*, p. 134.

37 Former National government finance minister Ruth Richardson told the BBC in 1995 that a major problem for New Zealand was that it had developed a "dependency culture" after fifty years of the welfare state. "The system had no integrity; it didn't give people in real need the help that they required or indeed the choice of how they would access that assistance, and we were breeding a dependency mentality." Richardson speaking to Ngaire Woods, "Analysis: Shrinking the State", BBC News and Current Affairs Department; broadcast on July 13, 1995.

38 For a discussion on the opinions of voters at this time, and the reasons for these feelings, see Colin James and Alan McRobie, *Turning Point* (Wellington: Bridget Williams Books, 1993), especially chapters eight and nine.

39 John Henderson, "Government: Representation and Trust", in David Novitz and Bill Willmott, eds., *New Zealand in Crisis* (Wellington: GP Publications Ltd, 1992), p. 56. Admittedly, National still won the 1993 election, despite its unpopularity, but its majority fell.

the two: National spent most of the years under the Labour Government in "political impotence" because "in the economic area, it could not outflank on the Right the formerly Left-wing party now in government".[40] Labour had taken National's economic position in what Roger Douglas described as a shift in the political landscape that rendered the old politics of "so-called economic Right and Left" meaningless.[41]

In rejecting Labour in 1990, voters believed they were also rejecting Rogernomics, but they got a more extreme form of the same policies, "Ruthanasia", named after National's Finance Minister, Ruth Richardson.[42] The reform process continued on the basis that no matter how much it might hurt, reduced state spending, deregulation and the removal of protections was the only route to economic salvation. As Labour in the 1980s had attacked the groups National could not -- farmers and manufacturers -- so National in the 1990s attacked the groups Labour could not -- the workers. Reflecting on the reforms, National Party member of Parliament Simon Upton said that Labour in 1984 "took on constituencies that it never had a chance of winning in any case. It really hit rural and provincial New Zealand very hard. ... (In 1990) the National Party hit sections of the welfare state that would have been almost impossible for Labour to hit and, of course, (National's) labour market reforms would never have been possible for a trade union-based party."[43] He says both parties were able to do this because all New Zealanders recognised and accepted the need for reform. "What was different about New Zealand (at this time) is that all of those constituencies, at least to some extent, said: 'look, we know there's a crisis; we know we've got to take something on the chin'."[44] Rod Deane, former manager director of Telecom (the deregulated and privatised telephone corporation), supports this view,

---

40 Stephen Franks, "The New Zealand Experience", *Columbia Journal of World Business,* Spring, 1993, p. 86.

41 Douglas, *op. cit.,* p. 11. The confusion over Left and Right had been building since 1975 when the supposedly Right-wing, 'free-enterprise' National government under Muldoon introduced extreme controls on the New Zealand economy. From 1984 to 1990, a supposedly Left-wing Labour government began unravelling the welfare state, a main achievement of earlier Labour governments, in favour of a free-market economy. Henderson , *op. cit.,* p. 57.

42 Henderson, *ibid.,* p. 58. Other sources refer to the policies as "Ruthonomics", but the more commonly used term is "Ruthanasia".

43 Upton on BBC broadcast, "Analysis: Shrinking the State", *op. cit.*

44 *Ibid.*

although he gives most credit to the "courage" of the politicians. "We had a period where politicians were prepared in a way to step aside from politics for a while and to say, 'what will really lead to gains in economic welfare', and then the courage to override their political reservations and say, 'let's do it'."[45]

The consensus also overrode any alternative focus to the economic paradigm being implemented by both governments. Ruth Richardson says there was no valid argument against reform, because had there been one, "it would have been given the hearing to which it was entitled".[46] However, Roger Douglas admits that the success of such a wide-ranging reform programme, despite adverse implications for many, lay in the speed with which it was introduced in many sectors simultaneously. "I always said you want to ... to move fast, because if you're moving fast and doing a series of reforms, the fire of your opponent is a lot less accurate ... it's much harder to hit a moving target, and by the time they got [sic] themselves organised to respond to your first policy, you're on to the next one so that never gets settled."[47] The rapid realignment of political forces left groups opposed to reforms, especially the workers, fragmented and weak. The unions were less and less able to resist the attempts by employers and the state to undermine their organisational strength and bargaining power. This was due, in part, to rising unemployment caused by a decline in the sectors of the economy in which the more militant unions have traditionally been based (transport and distribution, meat freezing, mining, manufacturing), and later, under National, the introduction of the Employment Contracts Act.[48]

While the business elite in the form of the Business Roundtable were decidedly in favour of the new economic direction, the less powerful businesses were

---

45 Roderick Deane on BBC broadcast, "Analysis: Shrinking the State", *ibid.*

46 Richardson on BBC broadcast, "Analysis: Shrinking the State", *ibid.*

47 Douglas on BBC broadcast, "Analysis: Shrinking the State", *ibid.* See also Douglas, *Unfinished Business, op. cit.*, pp. 220-227.

48 Brian Roper and Chris Rudd, "New Zealand's Political Economy", in Roper and Rudd, *op. cit.*, p. xi. For a discussion on divisions among the groups opposed to the reforms, see Brian Roper, "A Level Playing Field? Business Political Activism and State Policy Formulation", in Roper and Rudd, *op. cit.*, pp. 147-171.; Franks, *op. cit.*, pp. 86, 90.; and Bertram, *op. cit.*, pp. 37-47.

divided.[49] New Zealand manufacturers, for example, became a much less unified group as protections were removed. The reforms caused animosity between those industries who had traditionally received high levels of protection and wanted it to stay, and those who attacked protectionism because they bought products from the sheltered industries, adding to their costs and making them uncompetitive.[50] The farming sector was similarly divided, with the biggest farmers' interest group, Federated Farmers, in favour of the reforms because, according to Roger Douglas, the grand scale of what Labour was doing "convinced them we meant business in keeping their costs down as well as removing the subsidies".[51] Farmers were pitted against workers in other sectors as "long-hated (worker) feather-bedding in transport and other protected industries in the state sector were being addressed by the government at the same time".[52]

Treasury

New Zealand's senior bureaucrats added their weight to the political consensus, with those in Treasury playing a major role in the shift from Keynesianism to monetarism. The department used its position as the state's main source of economic advice to advocate a programme of monetarist economic reforms that had wide-reaching consequences. Treasury's official function is to manage the Crown's finances and "provide the government with economic and financial advice

---

49 This thesis will not discuss the influence of New Zealand's business leaders on policy formulation. For a discussion on such influence, see Brian Roper, "A Level Playing Field? Business Political Activism and State Policy Formulation", in Roper and Rudd, *op. cit.*, pp. 147-171; Brian Roper, "Business Political Activism and the Emergence of the New Right in New Zealand 1975 to 1987", *Political Science* vol. 44 no. 2 December (1992); Paul Dalziel, "The Economic Summit: What People Were Thinking", in Easton, *The Making of Rogernomics*, *op. cit.*, pp. 56-58.; and Andrew W. Mansfield, *The Power Elite: The Treasury and N.Z. Business Roundtable's Power in the Formation of the Privatisation Programme 1984 to 1987 - A Theoretical Analysis* (Canterbury: University of Canterbury, M.A. Thesis, 1990).

50 Wooding, *op. cit.*, p. 106.

51 Douglas, *Unfinished Business*, *op. cit.*, p. 226. For a discussion on farmers and the reforms see Robert Bremer, "Federated Farmers and the State", in Roper and Rudd, *op. cit.*, pp. 108-127. Bremer says that in the early 1980s, the Federated Farmers' economic policy returned "to the full-blown economic liberalism which had been the Federation's official philosophy prior to the 1970s". p. 125. Although farmers suffered hardship under the reforms, they wanted them to continue in other sectors that impacted on agriculture.

52 Franks, *op. cit.*, p. 90. "Organised attempts [among farmers] to disrupt the economy and reverse government policies gained only patchy support because at the same time farmers could see reductions in tariffs on their inputs and similar hardships pending for other formerly politically privileged groups."

from a broad perspective".[53] Statistics New Zealand, in its annual *Official Yearbook*, explains the roles of the various government departments and says Treasury's roles include:

> providing economic, financial and commercial advice and information; implementing specific economic and financial policies; providing financial information on the operation of government; accounting for the revenue and expenses of the Crown; managing the Crown's public debt and Treasury-managed financial assets; contributing to public understanding of economic and financial matters in a manner consistent with current constitutional conventions; and performing an actuarial role in regulating and providing to the government actuarial advice on life insurance, superannuation, and related industries.[54]

While Treasury is not the only source of economic and financial advice to the government, "it is undoubtedly the most important".[55] Its main bureaucratic rival, the Reserve Bank, is not only more limited in scope, but has been described as "Treasury's natural ally on most issues".[56] Treasury's policy influence is enhanced by strong support in Cabinet, with the Minister of Finance being one of the most senior members of Cabinet.[57] The department employs most of the state's public sector economists, which has helped create a reputation of expertise and intellectual strength such that "even its adversaries express admiration for its [Treasury's] competence, discipline, persistence, and political skill".[58] Other sources of advice, including economists working in other ministries and government agencies, are smaller and less cohesive than Treasury, which in 1990 employed 361 staff, of whom 150 were economic or financial analysts.[59] From this basis it can be argued that Treasury is the most powerful government department because "as controller of finances, it is at the centre of the administration, and its financial decisions and recommendations pervade every aspect of government activity".[60] Treasury's

---

53 Statistics New Zealand, *op. cit.*, p. 45.

54 *Ibid.*, p. 45.

55 Jonathan Boston, "The Treasury and the Organisation of Economic Advice: Some International Comparisons", in Easton, *op. cit.*, p. 70. Treasury describes itself as "the government's advisor on economic and financial matters". New Zealand Treasury, *Economic Management* (Wellington: Government Printer, 1984), p. 122.

56 Goldfinch and Roper, *op. cit.*, p. 52.

57 Boston in Easton, *op. cit.*, p. 77.

58 Jack H. Nagel, *Market Liberalisation in New Zealand* (Paper for delivery at 1994 annual meeting of the American Political Science Association), p. 19. See also Goldfinch and Roper, *op. cit.*, p. 52., and Alan Bollard, *The Political Economy of Liberalisation in New Zealand* (Wellington: N.Z. Institute of Economic Research), working paper 93/2 (1993), p. 22.

59 Jonathan Boston, "The Treasury: Its Role, Philosophy and Experience", in Hyam Gold, ed., *New Zealand Politics in Perspective* (Auckland: Longman Paul, 1992), p. 197.

60 Goldfinch and Roper, *op. cit.*, p. 51.

influence extends over the whole state apparatus and touches on every important area of public policy from macroeconomic (monetary, fiscal, incomes, and exchange rate policies) to regulatory, administrative, environmental, and social policy issues.[61] In this sense it is unchallenged because no other department has a mandate to cover so many areas.

Treasury's statutory obligation to monitor other departments adds to its power; it is formally required to comment on all department submissions to the Cabinet that have economic implications, which means about 75% of submissions to Cabinet are first looked at by Treasury.[62] Since 1973 Treasury's reports have been distributed to all Cabinet ministers, which creates two significant advantages for the department's views. First, it gives other ministers an opportunity to consider Treasury's views, and second, "because Treasury's reports are generally cogently argued and are often shorter than the departmental submissions ... [g]iven the work pressures faced by most Ministers, there is a natural tendency for them to read the Treasury report but to give only cursory attention to the original departmental submission".[63] This is not to say, however, that Treasury's advice is always taken, but its capacity to influence the broad philosophical and conceptual framework within which most policy debates are conducted gives it tremendous influence.[64] Jonathan Boston, who has written widely on Treasury and the organisation of economic advice to the government, says Treasury has tended to adopt a particular theoretical stance, which it then applies "as consistently as possible to the issues of the day".[65] The framework "profoundly influences the kind of questions that are asked, the way problems are defined, and the policy options that are considered relevant", which has an obvious implication, as Boston succinctly points out: "If one can determine the

---

61 *Ibid.*, p. 51., and Boston in Easton, *op cit.*, p. 71.

62 Boston, *ibid.*, p. 72. "In the words of the *Cabinet Office Manual*: 'A proposal having economic, financial or revenue implications will not be accepted by Cabinet Office unless it has either Treasury's signed endorsement or is accompanied by a separate Treasury report -- except, of course, when the submission is presented by the Minister of Finance (Cabinet Office 1987, E 1.5, d[i]).'"

63 *Ibid.*, p. 72.

64 In fact, under the third National Government of 1975 to 1984, Minister of Finance Robert Muldoon often disagreed with Treasury, introducing policies against Treasury thinking. Boston in Gold, *op cit.*, pp. 207, 208.

65 *Ibid.*, p. 76.

framework which will be used by ministers in their policy deliberations, one can also have a major influence on the policy decisions that are made."[66] From the 1950s to the 1970s, Treasury worked mainly within the prevailing social democratic Keynesian economic consensus, according to which the state had an active interventionist role in managing the economy in order to maintain full employment and stimulate economic growth. By the early 1980s, however, Treasury had changed towards a monetarist perspective, adopting "a conceptual framework for analysing policy issues based on a mixture of agency theory, a transactions-costs perspective, and a concern with the specification of property rights".[67] According to this framework, the emphasis shifted from intervention to a continuing assessment of the costs to the state of doing so.[68]

Treasury's policy prescriptions

Key members of Treasury had been won over to monetarism in the 1970s, and their views consolidated in favour of economic deregulation, exchange-rate flexibility, and a move to monetary policy modelled on Thatcherism in the United Kingdom in the late 1970s and early 1980s.[69] Treasury produced several reports that were widely circulated among economists and business groups, and the fall of the Muldoon Administration in July 1984 provided the opportunity for the new pro-market, anti-Keynesian generation of officials to "dislodge the remaining defenders of the older tradition of New Zealand policy-making".[70] This new group has been described as "largely free of party political loyalties and unconcerned with the manifesto commitments and policy principles with which Labour had won the

---

66 *Ibid.*, p. 76.

67 Boston in Easton, *op. cit.*, p. 76. Agency theory focuses on the contractual relationship between a principal person(s) and others who render services as agents, and transaction costs are the running costs of an economic system, that is, the cost of effecting an exchange or other economic transaction. ("These costs include those of negotiating and drafting contracts, and the subsequent costs of adjusting for misalignments.") Rutherford, *op. cit.*, pp. 10, 467.

68 Treasury defines transactions costs as the "significant costs in social and economic interaction". New Zealand Treasury, *Government Management* (Wellington: Government Printer, 1987), p. 12. It says there is a need to find methods of social organisation that minimise these costs.

69 Bertram, *op. cit.*, p. 43. For a general discussion on the changes in Treasury's thinking, see Goldfinch and Roper, *op. cit.*, Boston in Gold, *op. cit.*, the first three chapters of Easton, *op. cit.*, and Colin James, *New Territory: the Transformation of New Zealand 1984-1992* (Wellington: Bridget Williams Books, 1992).

70 Bertram, *ibid.*, p. 43.

election", and under their control, New Zealand became an extreme case of monetarist and free-market reform.[71] Labour prime minister of the time David Lange later described Treasury as being "almost like a religious cult" when its competence, discipline, and persistence were combined with a "zealous, cohesive commitment" to free-market economic doctrine.[72] There is some argument in the literature over whether Treasury drove Labour Finance Minister Roger Douglas or whether Douglas was committed to free-market ideas first and convinced Treasury he was right.[73] Douglas had been an early convert to the New Right ideology, becoming enamoured of its concepts under the guidance of Treasury adviser Doug Andrew, who was seconded to Douglas's office while the Labour Party was still in opposition. By July 1984, Douglas and his allies had defeated the "corporatist" wing within the Labour Party.[74] Once in power, Douglas's advocacy of market-led reform gave Treasury the political authority it needed to have its ideas transmitted into political action, while Treasury gave Douglas the kind of counsel he wanted to hear.[75]

In 1984, 1987, 1990, and 1993, Treasury supplied briefing papers to the incoming governments outlining the current economic situation and offering policy suggestions.[76] These papers were not unusual in that all government departments prepare briefings for their ministers after each election. The first three papers are similar in style, looking at all facets of policy, including those for purely economic management (monetary and fiscal policy, tax and regulation policies) as well as public sector management, social policy, and the labour market. The 1993

---

71 *Ibid.*, p. 37., and Bruce Jesson "Nationhood: Autonomy and Economic Relations", in Novitz and Willmott, eds., *op. cit.*, p. 44.

72 Nagel, *op. cit.*, p. 19.

73 This argument is well covered in Oliver, *op. cit.*, pp. 11-52., and from a different perspective in Andrew W. Mansfield, *op. cit.*

74 Oliver, *ibid.*, p. 43. "By the time of the 1984 election Douglas and a market liberal economic policy dominated the Labour Party. His was a programme of economic restructuring that required a non-corporatist, and highly elitist, political strategy because of the high social costs involved in its implementation. Economic restructuring could only have been carried out by a government with maximum freedom of action and not one constrained by corporatist institutions and the imperative of maintaining consensus." p. 50.

75 Robert Gregory, "The Reorganisation of the Public Sector: The Quest for Efficiency", in Boston and Holland, *op. cit.*, p. 112.

76 *Economic Management*, *op. cit.*; *Government Management*, *op. cit.*; New Zealand Treasury, *Briefing to the Incoming Government 1990* (Wellington: GP Print Ltd, 1990); and New Zealand Treasury, *Briefing to the Incoming Government 1993* (Wellington: GP Print Ltd, 1993).

paper is less broad, but continues the policy themes of the earlier works. The importance of these documents cannot be underestimated given that the changes parties made to their manifesto promises once they were in power created a situation where "few now believe the main parties' manifestos".[77] Jack Nagel offers a useful summation of the influence of Treasury and the policy framework of the 1984 and 1987 papers:

> "Treasury became the principal initiator and source of purpose; Government became the implementer or on occasion the advisor who counselled that a particular action was not (politically) feasible. *To know what governments would do, one had to read Treasury briefing papers, not party programmes.*"[78]

The influence of the first briefing paper, *Economic Management* (1984), was helped by the fact that when Labour assumed office in July 1984, it faced a financial crisis that demanded immediate action. Treasury's paper offered a blueprint for a plausible course of action, and had an advocate in Douglas.

Economic Management clearly showed Treasury's ideological shift from the Keynesian to the monetarist framework, and that the department was now fundamentally committed to the renewal of unfettered markets and the wholesale dismantling of the collectivist state. The reforms advocated were "profoundly ideological in nature" in that Treasury advised that the Labour government adopt a clear ideology of market-driven growth in which the party's traditional political clienteles were disenfranchised, productivity and flexibility in the workplace were stressed, and dependence on the state deprecated.[79] The "new politics" of free-market values and economic rationalism -- a faith in market forces as an economic panacea -- replaced the "old politics" of collectivism and state intervention.[80] Pro-market

---

77 James, *Turning Point, op. cit.*, p. 114. James says people were, in effect, advised not to believe in the manifestos by then Labour prime minister David Lange who said on Australian television in June 1987: "If anyone judged the incoming government on the basis of a manifesto after three years of office, they'd have to be very silly indeed."

78 Nagel, *op. cit.*, p. 20. My emphasis. Nagel says that in an interview with David Lange, Labour prime minister of the time, Lange "reflected ruefully" on the contrast between Treasury and the government, saying: "I don't *blame* Treasury ... I have more respect for Treasury than I have for the Labour Party, in the sense that they were a consistent, cohesive, intellectually convicted group of people that exercised strength and muscle and an all-pervasive right to go to the prime minister to achieve their end, whereas we in politics were unable to form a coherent base." Author's emphasis.

79 Nigel Haworth, "National Sovereignty, Deregulation and the Multinational: New Zealand in the 1980s", in Deeks and Perry, *op. cit.*, p. 27.

80 McAllister and Vowles, *op. cit.*, p. 382.

ideas were not presented in relation to outcomes or the demonstrable efficiency or inefficiency of the market as a creator of wealth and a regulator of goods and services, "rather they were argued in relation to beliefs, to ideology".[81] The market was given a moral authority; it was *a priori* "good" rather than a good which was a consequence of what it could and did deliver. This view was not confined to New Zealand: many people in western democracies by the 1980s felt that the state had too big a role in the economy.[82] High levels of state spending were said to be taking resources that could be used more productively in the private sector, and high taxes were seen as stifling private enterprise. Increasingly it was felt that the abolition of the complex system of state regulations, interventions, and subsidies would unleash a new wave of private initiative and energy. In the United Kingdom, the United States and West Germany, electorates turned to the political leaders who promised to implement these new policies -- Margaret Thatcher, Ronald Reagan, and Helmut Kohl.

Splitting politics from economics

Treasury's view splits the political and economic spheres, a notion that follows the economic theories of the Austrian, Chicago and Virginian schools from which Treasury gained its ideas. Treasury argued that economics was a technical, not a political issue, in that economics was a technical matter outside the area of political choice. Economic analyses were value-free, excluding moral judgments, and focused on ends rather than means where "the ends of policy are social, and are set by politicians, [while] the means are a technical matter to be settled by experts in terms of efficiency".[83] Treasury's claim that economic growth was the best "means" to achieve the country's "ends" meant the pursuit of growth became the main focus of policy, as all other ends were subsumed into Treasury's strategies to achieve growth.[84]

---

81 Deeks, *op. cit.*, p. 10.

82 David K. H. Begg, Stanley Fischer, and Rudiger Dornbusch, *Economics* (London: McGraw-Hill, Second Edition, 1987), p. 337.

83 James, *New Territory, op. cit.*, p. 90., and Bruce Jesson, "The Libertarian Right", in Bruce Jesson, Allanah Ryan, and Paul Spoonley, *Revival of the Right: New Zealand Politics in the 1980s* (Auckland: Heinemann Reed, 1988), p. 42.

84 "... the most important means of promoting well-being relate not to specific government interventions to deliver particular social services or to correct various inequities. Rather the most important set of policies are those which provide a consistent framework for the growth and

All areas of society were treated as belonging to the economy, but politics was confined to a narrow area of tidying up any malfunctions of the marketplace. Treasury followed the Chicago School claim that it was "a matter of observable fact [that] markets maximised economic welfare and political intervention diminished it".[85] Most public discussion of the new economic direction and the associated reforms was conducted in the language of economics, again allowing it to be argued as a technical matter rather than one of political belief as "[f]or most of the public, and even for most opponents of Rogernomics, ... Rogernomics was based on an incomprehensible body of economic theory that was almost impossible to debate."[86] Adding to the confusion for those wanting to understand Treasury's briefing papers, the way Treasury used certain terms was different to the accepted interpretation of meaning. Economic analyst Brian Easton points to the example of the use of "contestability" for competition, saying that the "introduction of a new piece of jargon may well have had the effect of distancing the analysis from the mainstream as well as misleading as to the intent."[87] A significant effect of the lack of public debate was that economic policies that profoundly challenged the underlying philosophy shaping New Zealanders' values and attitudes were introduced without being discussed and without the implications being fully understood by the public. The reforms and their practical results have been well discussed over the past few years; arguably, their philosophical implications are still not well understood.

Conclusion

Before analysing Treasury's briefing papers, it is useful to have an understanding of the context in which they appeared, that is, a general view of the developments of the New Zealand economy, and the role of Treasury within it. By

---

development of a strong economy. It is the processes of production, distribution and exchange which are the basis of our economic wealth and also central to the quality of our social life." *Government Management, op. cit.*, p. 394

85 James, *New Territory, op. cit.*, p. 89.

86 Jesson, "The Libertarian Right", *op. cit.*, p. 42.

87 Brian Easton, "From Reaganomics to Rogernomics", in Alan Bollard, ed., *The Influence of U.S. Economics on New Zealand* (Wellington: The Fulbright Anniversary Seminars, N.Z.-U.S. Education Foundation, N.Z. Institute of Economic Research, 1988), N.Z.I.E.R. research monograph no. 42, p. 86.

1984 New Zealanders had come to accept, and expect, a large role for the state in the economy. The small size of the country had led to state involvement from the outset, with the state accepting responsibility for the provision of infrastructure and institutions not otherwise provided by the private sector. This role increased over the half century from the 1930s, as the agriculturally based economy was hit in succession by the effects of the Depression in the 1930s, war-time conditions in the 1940s, a decline in the demand for agricultural products in the 1960s and an oil crisis in the 1970s. The state intervened in the economy to protect domestic investors, manufacturers and farmers, and to ensure all New Zealanders had access to the essential needs of life. From the 1930s it followed the prescriptions of Keynesian economics with successive governments introducing and reinforcing elements of the welfare state. When the fourth Labour government was elected in 1984, it took control of "Fortress New Zealand" -- an economy with a myriad of interventions, including restrictive regulations and investment incentives, aimed at domestic protection. It also took control of a welfare state built on "a comprehensive range of social services characterised by underlying notions of egalitarianism, humanitarianism, and a conviction that the state has a responsibility for the health, education and welfare for its citizens".[88]

Treasury is the government's most important and, arguably, most influential source of economic and financial advice. As outlined, Treasury comments on all department submissions to the Cabinet that have economic implications, which makes the philosophical and conceptual framework it uses to assess policy extremely important. Until the 1970s Treasury worked predominantly within the prevailing social democratic Keynesian economic consensus, changing over the 1970s to a monetarist or neo-classical paradigm, according to which it recommended that the state adopt a tough fiscal stance and focus on the money supply. From 1984, Treasury began to offer a monetarist explanation of New Zealand's poor economic performance, acknowledging the decline in the terms of trade and the deterioration of the world's economic performance, but placing most of the blame for New Zealand's

---

88 Task Force on Economic and Social Planning, *New Zealand at the Turning Point: Report of the Task Force on Economic and Social Planning* (Wellington: Government Printer, 1976), p. 97.

economic troubles with the "inadequate policy responses" of the government. It claimed state intervention had caused the economic crisis, with "the sclerosis that has built up through the regulation of many markets of the economy" compounded by the policies of the welfare state, which were seen as providing disincentives for individuals to look after themselves.[89] Treasury's focus on monetary policy as the cause of inflation led it to urge the state to abandon its other interventions aimed at controlling inflation, advice both Labour and National governments chose to follow. As Bertram summarises: "The [monetarist] package gave politicians the chance to abdicate, with a clear conscience, many of the responsibilities which the state had assumed in the preceding decades."[90] Policies of the Keynesian welfare state were abandoned in favour of minimum state intervention and maximum use of the mechanisms of the free market.

Since 1984, New Zealand's economy has been transformed into an almost text-book model of free-market economics. According to a BBC report, Britain's financial press, various British think-tanks and the World Bank are using New Zealand as an example of how to modernise the state and run a successful free-market economy.[91] While the focus has been on the reforms themselves, little attention has been paid to the fact that the shift from a Keynesian to a monetarist paradigm has brought with it a change in the underlying political philosophy of the state. "Value-free" economic policy has moved New Zealand from a social democratic state to a neo-liberal one. Treasury's briefing papers appeared at a time when New Zealand's political and bureaucratic elites agreed that there was a need for a dramatic change in direction in order to rescue the economy and put it on a track to growth and prosperity. The papers offered a blueprint for a new path, one that centred on minimising the state's role in the economy. Many of the policy recommendations were implemented, and the foundations of New Zealand's welfare state were dismantled, concealed behind the need for a "realistic" economic policy.

---

89 *Economic Management, op. cit.*, p. 107

90 Bertram in Roper and Rudd, *op. cit.*, p. 36.

91 Ngaire Woods, "Analysis: Shrinking the State", *op. cit.*

As the next four chapters will show, politicians did not, as Deane claims, stand aside from politics in embracing Treasury's policy framework, because the prescriptions the briefing papers contained were not politically neutral.

CHAPTER TWO

Treasury's "state *versus* market" model

Introduction

Treasury's briefing papers offer ambitious prescriptions for the whole of New Zealand society in what Treasury describes as a framework for an approach to economic management from both an administrative and substantive point of view.[1] The papers offer Treasury's ideas and recommendations on how best to achieve what it says is its central concern: maximising social and economic welfare in the Pareto optimality sense, that is, when no-one can do better to satisfy their interests without someone else doing worse. The papers show that Treasury, in order to achieve its goals, is prepared to sacrifice what had come to be the traditional role of state in New Zealand. As outlined in chapter one, until 1984, governments had followed the principles of the Keynesian welfare state under which the state intervened in the economy to achieve certain goals it felt the free market had failed to meet. Beginning with its 1984 briefing, Treasury advocates a much narrower role for the state on the basis that the state is not the best mechanism to fulfil the needs of New Zealanders. In Treasury's view, the state has failed in its objectives; New Zealand's economic performance was poor with low growth, low incomes, high unemployment and a high dependence on the state, which compounded the economic problems by causing state expenditure to spiral upwards, increasing the need for higher taxes and levies.

Treasury claims the solution to New Zealand's economic problems lies in boosting economic growth, from which other benefits would flow -- a stance that is consistent throughout the four briefing papers. It says growth will solve the economic crisis and give New Zealanders a better life by increasing general welfare

---

1 New Zealand Treasury, *Economic Management* (Wellington: Government Printer, 1984), p. 121. The other papers are New Zealand Treasury, *Government Management* (Wellington: Government Printer, 1987); New Zealand Treasury, *Briefing to the Incoming Government 1990* (Wellington: GP Print Ltd, 1990); and New Zealand Treasury, *Briefing to the Incoming Government 1993* (Wellington: GP Print Ltd, 1993).

-- creating jobs, raising the level of income, reducing the number dependent on the state, and reducing the level of fiscal expenditure and debt.[2] Treasury says the best methods to produce growth are efficiency, that is, the efficient use of resources (both physical and human); increased self-reliance and self-responsibility, which will decrease the debilitating burden on the state; and a positive cost-benefit in policies, or achieving the greatest benefit at the least cost to the state. Treasury examines how these methods can be achieved by comparing the functions and abilities of the state and the market, and concludes that an increased use of market mechanisms is essential. It says state intervention caused the economic crisis, stultifying the economy with rules and regulations that stifled entrepreneurship and decreased the incentives for citizens to use their initiative and take advantage of available opportunities. The free market, on the other hand, allows individuals to trade without interference in voluntary contracts to get the things they need and desire.

This chapter will review the four briefing papers, giving a brief description of each before outlining Treasury's framework for economic management as clearly summarised in its state versus market model in *Government Management* (1987). It will not discuss details of New Zealand's financial situation or particular policies, but will focus on Treasury's attitude to the state and society, and the relations between the two. This chapter will not offer in the body of the text a critical analysis of the contents of the briefing papers beyond some general comments in the section, "Comparing the state and the market", on Treasury's arguing techniques and use of language. This is in order to keep some form of continuity to the exposition of Treasury's model, which will be critiqued in the next three chapters. Footnotes will be used to mark the aspects of Treasury's argument with which issue will be taken, as well as to note areas that could be argued, but are outside the scope of this thesis.

---

2 "A well-functioning growing economy is desirable because it contributes to improved well-being for all New Zealanders. It yields higher incomes which enable consumption of more goods and services; greater scope for quality public services and enhanced environmental quality; [and] wider opportunities for people, including the unemployed, to participate more fully in society." Briefing 1993, *ibid.*, p. 48.

The briefing papers

The first three Treasury papers are the most comprehensive. The 1984 paper, published in book form as *Economic Management*, is 325 pages plus supplements; the 1987 paper, published in book form as *Government Management*, came in two volumes, the first of which was 472 pages and the second, "Education Issues", 295 pages; and the 1990 paper is 181 A4-size pages. The 1993 briefing (a mere 104 A4-size pages with large print and short bold paragraph statements), is less broad in scope, but continues the over-all policy themes of its predecessors. *Economic Management* (1984) set the direction for the later papers, offering an all-encompassing look at the New Zealand economy. As well as six chapters discussing the current economic situation, it has 15 chapters on "Policy and Organisational Issues" including monetary, exchange rate and fiscal polices, taxation, the labour market, social policy, and the public sector. This reflects Treasury's opinion that in order to avoid regarding expenditure as the only means for the government to achieve its objectives, the minister of finance needs to become familiar with policy issues that are the primary responsibility of individual spending ministers.[3] The paper was written in the four weeks between the calling of the 1984 election and the election itself, and was more comprehensive than any of the party manifestos, bringing the comment from Brian Easton: "It is sometimes said, only half humorously, that five parties fought the election, and that the Treasury Party had the largest and most unreadable manifesto."[4]

Government Management (1987) is the most overtly theoretical of the papers, with its discussion of the current economic situation contained in a mere 33 pages in the final, sixth chapter of Volume One.[5] The focus of the briefing is instead on Treasury's theory of state and market relations, which it outlines in chapter one,

---

3 *Economic Management, ibid.*, p. 129. The argument is repeated in *Briefing 1990, ibid.*, p. 80.

4 Brian Easton, "Labour's Economic Strategy", in Jonathan Boston and Martin Holland, *The Fourth Labour Government: Radical Politics in New Zealand* (Auckland: Oxford University Press, 1987), p. 136. Easton is equating Treasury with the four major parties to contest the 1984 election: Labour, National, Social Credit and the New Zealand Party. The comment is valid: Treasury's cohesive and disciplined characteristics could reasonably be compared to those of a political party.

5 This thesis will focus on Volume One of *Government Management*, being concerned with the broad sweep of Treasury's policy prescriptions rather than the details of a specific section, education, offered in Volume Two.

the "Role and Limits of Government". It then applies this framework in the next three chapters on the public sector, social policy, and economic management, before examining in a 31-page chapter the implications of the Treaty of Waitangi. In addition, Treasury provides an annex of "Background Papers on Social Policy", including the "Role and Goals of Social Policy", "Ethics and Social Justice", "The Concept of Rationality", and "A Checklist of Issues for Social Policy Making". Treasury admits that with the inclusion of the background theoretical sections, *Government Management* goes beyond what would usually be presented to a minister, but says the annex papers are included "for completeness, in order that the logical underpinnings of the ideas may be seen".[6] In another sense, however, the briefing is incomplete: it is "largely bereft of the footnotes, or the other standard academic references, which help place a work in some sort of intellectual context".[7] The 1990 briefing paper repeats many of the arguments of the earlier papers in its 11 chapters covering topics including monetary and fiscal policy, the public sector, social policy, the labour market, regulation and taxation. It has dropped the theoretical chapters of *Government Management* (1987), but includes a new chapter on "The Balance of Policies" in which it returns to a theme of *Economic Management* (1984) that a "long-standing problem for New Zealand is a lack of harmony between policies".[8] The 1993 briefing has only five chapters and takes a markedly different approach to the earlier papers. Its discussions on the various issues are shorter, with previously distinct areas such as social policy, the public sector and the labour market subsumed into chapters on "Higher Incomes from a Growing Economy" and "Unemployment, Skills and Disadvantage". This paper has abandoned the explicit discussion of theory characteristic of the 1987 briefing in favour of a more "fact-based approach" to the state of the New Zealand economy.

Comparing the state and the market

All of the briefing papers examine to a certain extent the relations between the state and the market, or the public and private sectors, with the first two

---

6 *Government Management, op. cit.*, Preface p. vi.

7 Brian Easton, "*Government Management*: A Review of its Political Content", *Political Science* vol. 42 no. 2 (December 1990), p. 36.

8 *Briefing 1990, op. cit.*, p. 39.

making overt arguments in favour of reducing the role of the state in favour of market mechanisms and the latter two being much less obvious in their pro-market arguments, that is, their statements are more subtle forms of the earlier ideas.[9] Treasury sets up its pro-market argument in *Economic Management* (1984), commenting on "the question of the chosen role for government in the economy" in a statement couched in language that implies its view is common sense.

> While this (the government's role in the economy) is often expressed as a philosophical choice between free markets and planning, this is not a helpful distinction for *practical* purposes. Powerful government influences are at work in all markets all the time -- indeed markets cannot function without a set of rules for governing private transactions laid down by the government. This includes such matters as the legal framework for the conduct of commercial affairs. The question for government choice is not whether to intervene but rather to decide what set of interventions is most appropriate for a particular purpose.[10]

It repeats the argument in *Government Management* (1987): "If governments may be the basis of markets, to speak of them interfering in markets seems slightly misplaced. Government involvement in markets is pervasive and therefore the notion of a market totally free of government intervention may be meaningless."[11] Treasury says the question is not *whether* the state should intervene, but *how much* it should intervene:

> With regard to choosing the most effective policy, the reason so-called market forces are the appropriate touchstone in many areas of economic activity is because most policies are to be judged in terms of how well they succeed in marshalling those forces to achieve greater welfare. Markets generally offer an efficient means for reconciling competing demands so that the government is more likely to achieve its ends effectively by harnessing and supplementing markets rather than suppressing them.[12]

---

9 For example, in 1984, Treasury says "[m]arkets generally offer an efficient means for reconciling competing demands so that the government is more likely to achieve its ends effectively by harnessing and supplementing markets rather than suppressing them". *Economic Management, op. cit.,* p. 111. In 1987, as will be outlined in this chapter, Treasury devotes 40 pages to proving that the market is a better means of achieving the country's goals than state intervention. *Government Management, op. cit.*, pp. 9-48. In 1990, Treasury says social policy is likely to be most effective when it strengthens and supplements, rather than supplants, the mechanisms that promote self-reliance and family and voluntary community support. *Briefing 1990, ibid.*, pp. 75, 96. This is the same phrase as used in Economic Management, except the word markets has been replaced with "mechanisms".

10 *Economic Management, ibid.,* p. 111. My emphasis.

11 *Government Management, op. cit.*, p. 24, 25.

12 *Economic Management, op. cit.*, p. 111. The first sentence of this quote demonstrates one of the difficulties with understanding Treasury's position -- that the discourse is often circular and confusing. For example, this sentences appears to say that "market forces" are an appropriate standard by which to select policies because most policies are judged by how well they use these market forces to improve the over-all welfare of the population. Market forces are therefore being used to judge market forces. The reasoning of the sentence is unclear, but the meaning is taken that the market is superior. Treasury's confusing discourse will be discussed later in the chapter.

This is an important, if confusing, statement of Treasury's faith in market forces. Treasury is assigning much weight to the claim that markets are an "efficient" means for the state to "effectively" achieve its ends, without explaining why the state should elevate efficiency above other considerations. For example, the state may prefer "fair" or "equitable" means of reconciling competing demands, which may not necessarily be the most efficient means.[13]

Treasury's justification of the state's role in relation to the market also demonstrates a common arguing style throughout the briefing papers. Treasury outlines an extreme position then argues against it with its own view, so that its own position seems logical and reasonable. In the argument over the state's role in the market, for example, Treasury first makes a statement that seems as though it is proposing no change at all to current arrangements. It then presents an extreme position -- no role for the state at all -- as if it were a stance that someone in New Zealand could realistically argue.[14] In fact, no-one is suggesting that the state have no involvement in the market, but the statement serves the purpose of making the role Treasury is about to set up for the state, that of minimum intervention in the market, seem moderate by comparison.[15] Another important point to note when reviewing the briefing papers is that Treasury's use of language often affects the clarity of its arguments. As touched on briefly in chapter one, the way Treasury uses some terms is often different to the accepted interpretation of meaning, or it uses a single term in several different ways.[16] Sometimes the meaning is clear from the context; at other times it is not, which makes the line of reasoning ambiguous. The remaining four chapters of this thesis will note, where it is relevant, some of the areas where the argument is difficult to understand, although this is not the primary focus

---

13 The elevation of efficiency to a primary concern of policy will be discussed in chapter five.

14 Bruce Jesson, "The Libertarian Right", in Bruce Jesson, Allanah Ryan, and Paul Spoonley, *Revival of the Right: New Zealand Politics in the 1980s* (Auckland: Heinemann Reed, 1988), p. 43.

15 Another important example of this arguing technique, in which Treasury argues against state intervention to alleviate inequalities in society on the basis that "the efficiency cost of *complete* equality would be prohibitively expensive", is discussed in chapters four and five. *Government Management, op. cit.*, p. 123. My emphasis.

16 For example, Treasury uses the term "rights" to cover a multitude of meanings. This will be discussed later in the chapter. As noted in the introduction to the thesis, another example is the use of the term "government" -- in some places it means the Cabinet, in others the Cabinet and caucus, and in others the Cabinet, caucus *and* the bureaucracy.

of the thesis. A related problem is that Treasury's presentation is often circular, and important material is lost in confusing -- and careless -- phraseology and sentence structure.[17] Again, this thesis will note where it is relevant some of the areas where this occurs, and where it presents difficulties for Treasury's argument. As noted in the introduction to this chapter, such comments from this point will be made in footnotes.

The pro-market model[18]

The clearest exposition of Treasury's pro-market stance is in *Government Management* (1987), and in the first chapter, the "Role and Limits of Government", Treasury sets out the ideas on which its later chapters are grounded. According to Treasury, New Zealanders aspire to secure a "fair and thriving society", based on equity, efficiency and freedom.[19] However, it warns from the outset that it is not always possible to make things better on all of these fronts, and "one has to accept trade-offs where they exist".[20] Its discussion then centres on the nature of social and economic interaction, and consideration of the means by which social goals can be, and are, achieved and underachieved. Treasury says its fundamental message is that there are "limits to private solutions to social problems, and limits to

---

17 An example of this has already been noted in footnote 11. For an interesting exchange on Treasury's use of language and rhetoric, see P. C. Dalziel, "The Rhetoric of Treasury: A Review of the 1990 Briefing Papers", *New Zealand Economic Papers* vol. 25 no. 2 (1991), pp. 259-274.; Peter Gorringe and Peter Bushnell, "The Rhetoric of 'The Rhetoric of Treasury'", *New Zealand Economic Papers* vol. 26 no. 1 (1992), pp. 127-142.; and P. C. Dalziel, "The Rhetoric of Treasury: Reply", *New Zealand Economic Papers* vol. 27 no. 1 (1993), pp. 91-99.

18 The following discussion follows the format set by Treasury in *Government Management, ibid.*, pp. 9-48.

19 *Ibid.*, p. 9.

20 *Ibid.*, p. 9. This is an unusual statement from Treasury. Trade-offs are not usually thought of as something that "exist" independently, but are a result of negotiation in order to resolve a conflict. That is, claims for equity, efficiency or freedom may conflict, with resolutions via negotiated trade-offs. MacPherson offers a useful definition, saying that a trade-off is a decision, or an action resulting from a decision, between two things both of which are desired (positively or negatively), but which are seen to be incompatible with each other. "If the two desires are indeed incompatible alternatives, a choice must be made: so much of one against so much of the other." C. B. MacPherson, *The Rise and Fall of Economic Justice and Other Essays* (Oxford: Oxford University Press, 1987), p. 45. From this it can be seen that one may have to argue for or against a trade-off, and eventually accept or decline it, but the trade-off does not "exist" independently as something that *must* be accepted. Trade-offs also imply that the choice is between two alternatives. One can have either one or the other, but not both, which may not be true in the case of equity, efficiency and freedom. This will be discussed in chapter five.

government designed solutions".[21] In considering policy options, therefore, the state needs to take a "comparative systems approach" by which it first identifies the objectives and rationale of state policy and the problems it seeks to address, and second establishes that the state can improve things.[22] Treasury's stance on this point is telegraphed with its statement that any "claimed" problem with private arrangements should be subject to detailed scrutiny because "in the past the limits of private contracting have often been overstated".[23] Treasury calls for empirical research, or information and analysis of private arrangements that deal with perceived problems, saying it is not convincing enough evidence for the state that, for example, particular groups are not competent to look after their own interests. Comparative analysis of state versus private actions must be based on an evaluation of the full impact of a state policy over time and its consequent impact on other areas of the economy.[24] In order to "perform well", the state must understand the effects and nature of its policy instruments, the limitations of central control, and the "appropriate" level of state intervention.[25]

---

21 *Ibid., p.* 9. "Private solutions" refers to the market in line with Treasury's use of the terms "public" and "private" to distinguish the activities of the state and its agencies from those economic activities that are independent of state control. In other words, Treasury equates "public" with the state and "private" with the market. Shim and Siegal provide a definition of "private sector" that usefully explains Treasury's stance, saying it encompasses all economic activities that are "independent of state control, carried on principally for profit, but also including non-profit organisations directed at satisfying private needs, such as private hospitals and private schools. Included are enterprises owned by individuals or by groups (such as corporations with numerous shareholders) as well as the self-employed." Jae K. Shim and Joel G. Siegal, *Dictionary of Economics* (New York: John Wiley and Sons, 1995), p. 278. This is different to a more philosophical split where public is seen as "'out there', impersonal, distant, formal", while private is "'in here', personal, intimate and closest to self". Hanna Fenichel Pitkin, "Justice: On Relating Private and Public" *Political Theory* vol. 9 no. 3 (August 1981), p. 328.

22 This point was also made in *Economic Management, op. cit.*, p. 117. "All things considered, the question in relation to an economic activity is whether a government action, fiscal or otherwise, will improve on what would otherwise occur."

23 *Government Management, op. cit.*, p. 10.

24 *Ibid.*, p. 10. Treasury does not acknowledge that such a comparison might show that the limits to state arrangements have also been overstated. Nor does it advocate an evaluation of the full impact over time of private sector arrangements. It simply assumes the private sector, that is, the market, is better than the state.

25 *Ibid.*, p. 10. "Noble and clear objectives are not all that is needed for a government to perform well. It also requires a clear understanding of the nature and effects of its policy instruments, the limitations of central control, and the appropriate level of government involvement." The second sentence appears to imply that in order to perform well, the state may have to abandon some of its noble and clear objectives in order to meet the criteria listed -- knowledge of effects (costs), limitations, and the appropriate level of involvement. Treasury does not explain who sets the "appropriate" level of state intervention, or how this and the "limitations of central control" are to be judged.

I) Constraints on the Achievement of Social Goals

Treasury says that several "fundamental factors" have to be recognised as "constraints on our ability to secure an ideal society", and in comparing state and market arrangements to overcome these constraints and the limits to their success, it is important to recognise that "the state is not an omniscient and omnicompetent solver of social problems, but rather is subject to largely the same pitfalls that face private solutions to social problems *plus other ones*".[26] Again, such a statement signals Treasury's intent to prove from the outset that the state can never offer better solutions than the private sector, in that Treasury contends that the state's solutions will always be beset with more difficulties. Given this, the state is unlikely to be able to improve things, which is one of the comparative criteria that Treasury says the state must consider before deciding on policy options and intervention. The implication, therefore, is that the state should leave the achievement of social goals to the market, limiting its role to setting the rules by which private arrangements are governed.

Treasury outlines a model of constraints on the achievement of social goals, which it then applies to both the private and public sectors.[27] According to this model, the basic constraint a society faces is the **scarcity** of resources (both physical and human) relative to the demands placed on them. This creates the need to use both physical and human resources efficiently, to make them go further, and to ensure that the uses to which they are allocated are those that are most highly valued. A second constraint is **interdependence** where one person's use of a resource impacts on another person either beneficially or detrimentally, which means society has to find methods to resolve "interdependencies" -- that is, conflicts of interest -- in a way that takes account of the welfare of all those affected.[28] A third constraint is **uncertainty** about the future and consequences of actions, deriving from the "bounded rationality of individuals", that is, "the inability of humans to comprehend fully the nature of their environment, to .anticipate or devise strategies to cope with

---

26 *Ibid.*, p. 10. My emphasis.

27 *Ibid.*, pp. 10, 11.

28 Treasury does not elaborate on why a beneficial interdependency would need to be resolved.

change and to communicate effectively with each other".[29] This means people must plan on the basis of a largely uncertain future, and are forced to adapt to change and adopt strategies that minimise risks. A fourth constraint, linked to bounded rationality, is the problem of obtaining **information** that allows people to make correct judgments. The acquisition of information involves costs, it is not free and is therefore valuable, but there is also a point at which a trade-off has to be made between acquiring further information and the cost of doing so. A fifth constraint is **opportunism** in that individuals are motivated "at least in part" by a concern for themselves (self-interest) and thus have "opportunistic tendencies".

> The organisation of society towards the achievement of social goals would be immensely easier if individuals were always generous, altruistic, honest and forgiving. When they are selfish, jealous and spiteful then the costs of social organisation are raised.[30]

Faced with difficulties in interacting, individuals have to protect themselves against the opportunism of others, and finding the best form of social organisation therefore means ensuring that individuals face incentives that align their interests with those of others. The combined problems of scarcity, interdependence, uncertainty (bounded rationality), the costs of information, and the problems of opportunism (or incentives) make social organisation towards desired goals "an immensely difficult task", and the problem is to find the best methods of social organisation that minimise these constraints in order to marshal individuals towards common or consistent ends.[31]

II) The Role and Limits of Private Arrangements

i) The role of private property

Treasury postulates that the solution to the problem of scarcity lies in the specification of enforceable rights, which express relationships between individuals in respect of the use of scarce resources (property rights) or with respect to each other (human rights).[32] The existence of scarcity and the need to reconcile

---

29 *Ibid.*, p. 11.

30 *Ibid.*, p. 12. This is another example of Treasury making an extreme statement in order to justify its position. While Treasury has initially used a qualifier ("at least in part") for its observation on individuals' motivations, its subsequent use of the word "always" implies that people never exhibit the former, positive characteristics it lists, because their behaviour is always guided by the latter, negative characteristics. However, while it is true that people are not *always* generous or altruistic and so on, it is not true that people *never* exhibit these attributes. This assumption of negative human behaviour will be discussed again in the next three chapters.

31 *Ibid.*, p. 12.

competing claims through the definition of rights creates the need for an institution with a monopoly on coercive powers to adjudicate on rights when necessary.

> This is perhaps the fundamental explanation for the existence of government. It is the ultimate safeguard to ensure that individuals in pursuit of their own self-interest reconcile their competing claims through peaceful means rather than waste resources, time and effort in violent and aggressive behaviour.[33]

The institution of private property enforced by the state enhances incentives toward careful husbandry of scarce resources. A state also helps resolve the problem of interdependencies because "individuals look to government institutions to define or change rights in order to balance the welfare of all, not merely the welfare of the owner" with owners being prevented by the coercive powers of the state from imposing costs on others.[34]

ii) The role of voluntary contracting

Treasury says individuals not only look to the state to enforce rights, they also look to voluntary contracting or market exchange as a means to resolve scarcity and interdependencies. Trade, for example, allows transfer of ownership between contractors when one person values a resource more highly than its current owner and is prepared to compensate the current owner for it. The result is that, through exchange, social welfare can be improved. Through voluntary exchange contracts, either based on barter or facilitated by money, "ownership titles to resources are transferred, ensuring that resources flow towards those who value them the most".[35] Treasury says arguments in favour of the use of markets or private

---

32 Having raised the issue of human rights, Treasury turns its focus to property rights, without examining the links between these two sets of rights. For example, if one individual owns a lot of property and another owns none, then what happens to the relationship between the individuals with respect to human rights? Treasury defines property rights as being: the right to use a resource and to retain income accruing from its use; the right to change the nature of a resource (for example, to put a factory on farm land); and the right to transfer these rights. "The crucial feature of all these rights is the extent to which they are exclusive or good against all comers, or against the competing claims of others." *Ibid.*, p. 13.

33 *Ibid.*, p. 13.

34 *Ibid.*, p. 14. Treasury offers noise control bylaws and the restrictions on the erection of nuclear power plants as examples of what it means by this, but the limits of the extent to which the argument can be applied are not clear. Also, it could be argued that the state is expected to enforce rights rather than define or change them in the manner suggested. This point demonstrates a difficulty with Treasury's conception of rights that will be discussed later in the chapter.

35 As will be examined in later chapters, this statement demonstrates a fundamental flaw in Treasury's argument in that it equates "value" with ability to pay. (Treasury admits that modern societies are unlikely to barter, having developed a "sophisticated monetary system" to facilitate exchange and avoid the problems in barter where both parties in an exchange have to have a commodity

contracting to solve economic and social problems focus on three main features. First, markets enable efficient use to be made of information because they allow those with access to information, the acquisition of which bears a cost, to find their own solutions, "rather than risk ill-informed interventions by third parties".[36] Second, markets co-ordinate individual actions and "resolve interdependencies", creating "efficient" outcomes because the price mechanism conveys to market participants information about competing claims to resources, the returns resources can earn in alternatives uses, and the costs of production.[37] Individuals use prices to make production and consumption decisions in a way that incorporates wider social claims on resources. "Efficient markets force individuals to make choices about the priorities they have, reconcile their demands with those of others and further provide incentives for individuals to conserve the use of resources wisely."[38] All of which, Treasury says, are socially desirable outcomes.

The third feature of arguments in favour of markets is that market competition puts in place a selection mechanism that over time guides resources to those users and uses that maximise the value of production secured from the resources, as measured by consumers' willingness to pay. That is: "Markets at their best resolve conflicts impersonally and ensure that over the longer term, less efficient producers are penalised and the more efficient rewarded."[39] Treasury dismisses concerns about markets resulting in undesirable consequences such as exploitation,

---

the other wants.) In fact, an individual may "value" something highly, but not have the money to pay for it, which undermines the claim that resources "flow towards those who *value* them the most". My emphasis.

36 *Government Management, op. cit.,* p. 15.

37 *Ibid.,* p. 15. The claim that markets "resolve interdependencies" is repeated throughout the model, although Treasury does not give a concise explanation of how this occurs. Given Treasury's earlier definition of an interdependency as occurring when one person's use of a resource impacts on another person either beneficially or detrimentally, at this point in Treasury's argument it appears that interdependencies are resolved by price, that is, the person who has the most money -- and therefore "values" the resource the most -- is the person to obtain it. This will be discussed again later.

38 *Ibid.,* p. 16. Treasury's use of the price mechanism is subject to the same flaw as its use of the notion of value. According to Treasury's argument, if many people want a resource, then the demand will push up the price until it is supplied only to those who can afford to buy it at the higher price. This means that only those who have wealth will be able to obtain resources. It is not clear how this "incorporates wider *social* claims on resources" (my emphasis), given that society may want a fairer or more equal distribution. The linking of "efficient" markets with price and ability to pay, and the claim that this results in "socially desirable" outcomes, will be challenged in chapter five.

39 *Ibid.,* p. 15.

unfair trading and monopoly practices, saying these are often disciplined by the market itself through competition. Exploitation or unfair trading by an individual or firm that gives them a higher return than others get elsewhere creates incentives for others to enter the market and compete, thereby undermining the longer term survival aspects of such practices.[40] Decentralised markets based on competition have dynamic properties over protected markets or centralised control in that competition imposes a selection process on different methods of organising production and distribution, and provides incentives to discover new opportunities, new ways of doing things, and new products and services, while also providing a check against abuse of power and privilege. Treasury concludes that competition and markets are "organisational arrangements that economically allow individuals to undertake mutually beneficial transactions while aligning the interests of the individual with those of society".[41]

iii) Limits to markets

Treasury acknowledges limits to private contracting, including uncertainty, information problems and opportunism, but dismisses these saying they are unlikely to be uniformly present in all exchanged transactions, and "even less perfect markets can nevertheless work well".[42] Individuals face problems arising from the difficulty of measuring the quality of goods and services being sold, but can resolve these by crafting safeguards in their contracts or by seeking alternative organisational forms that minimise the problems. For example, the capitalist firm when viewed as an organisational innovation -- consolidating autonomous agents contracting across markets into an internal organisation of production -- may be seen as socially beneficial in the way it may ensure the efficient production of goods and services for a market using teamwork. The firm allows owners of labour, capital and land to join together to provide goods or services to a market "in an organisational

---

40 *Ibid.*, p. 16. This argument ignores that the costs of entering the market may be too high to attract the envisaged competition, that the monopoly may have become established in the market and therefore be in a strong position to fight off competitors, and that the market may be too small to support more than one supplier. Railroads, communication systems, and electricity supply are all examples of where non-regulated barriers to entry may restrict competition. The limits of the ability of competition to eliminate "undesirable consequences" will be discussed in the next chapter.

41 *Ibid.*, p. 16.

42 *Ibid.*, p. 17.

unit that enables greater gains for each than independent or autonomous contracting".[43] Treasury then offers a view of benevolent monopolies, saying that while there is often a "general expression of hostility" towards large dominant firms, "recent research ... suggests that attempts to expand or take control of different levels of production and distribution may be based on the efficient adaptations of private individuals to eliminate the problems experienced with contracting".[44] While Treasury admits that "firms can behave opportunistically and exploit a monopoly advantage", it is confident that competition will prevent this occurring, especially if there are no state regulations imposing barriers to entry.[45] It claims a firm's need to maintain its reputation, and monitoring by consumers, potential rivals and the state (involving the threat of regulation), all act as checks on monopolistic behaviour. Treasury implies that individuals have power in the market, saying "one needs to be sensitive to the incentives of private individuals to eliminate practices which are exploitative and take precautions against them in mutually beneficial ways."[46]

Other forms of organisation to minimise the uncertainty, opportunism and information problems that may limit voluntary contracting include voluntary associations of individuals -- clubs, churches, unions and so on -- which comprise individuals "contracting with each other" to deliver a good or service of benefit to themselves, either exclusively or in the wider community.[47] Treasury acknowledges that opportunism, or the free-rider problem, may undermine the effectiveness of voluntary associations especially in the case of public goods, that is, goods that can be used by additional consumers at no extra cost and for which it is not possible to exclude people from consumption. However, it warns against over-emphasising the free-rider problem, saying few goods are likely to involve "zero marginal cost for use

---

[43] *Ibid.*, p. 21. Treasury offers only a positive view of this "teamwork", ignoring the differentials in power between the owners of inputs, and that this inequality may not result in "greater gains" for all parties to the contract. The effects of inequality in the market will be covered in chapter five.

[44] *Ibid.*, p. 20. This is an example of the problem caused by the lack of footnotes and references in the briefing paper. "Recent research" is so vague as to be meaningless, given that it says nothing about who conducted the research, where, and whether it is applicable in a New Zealand context.

[45] Treasury does not acknowledge that there may be other barriers to entry besides state regulations. This will be discussed in the next chapter.

[46] *Government Management*, *op. cit.*, p. 20.

[47] *Ibid.*, p. 21.

across any significant range". If people "free-ride" rather than join clubs or associations seeking to provide public goods, then the quantity or quality of public goods will "probably" fall, which means a cost is incurred by the free-riders. Their "ride" is not free, but "rather cheap". Voluntary attempts to deliver goods are better than compulsory attempts by the state that may prevent cheap riders, because the goods may be better tailored to the needs of the benefiting population.[48] Club or association members make decisions on what goods should be provided, and those that disagree can "freely leave the group" and seek another one that better meets their needs.[49]

III) The Role and Limits of Centralised Government

i) The role of the state

Treasury moves from its market model into examining the role and limits of centralised government, building on its argument that a state is needed to enforce the rights or relations between individuals that underpin the system of voluntary exchange or markets. It says the definition of rights through voluntary exchange is a dynamic process that responds to factors such changes in technology, preferences, income, relative prices, population, and the need to minimise the problems of the previously outlined constraints of scarcity, interdependence, uncertainty, information costs, and opportunism.[50] In voluntary market exchange, individuals seek to reinforce and mutually recognise each others' exclusive rights to use and transfer scarce resources in an interdependent world, and "the glue that makes a contract stick is the mutual advantage that underlies it".[51] However, there are problems with purely private regulation and formation of rights, including that rights formed on the basis of contract alone are not likely to be respected by all individuals, only those party to the contract, and that attempts by individuals to create

48 *Ibid.*, p. 22.

49 This argument has been used to justify voluntary unionism and voluntary membership of student associations. A discussion of the issue is outside the scope of this thesis.

50 Treasury appears to be again referring solely to property rights because it is hard to see how human rights would change according to the factors mentioned. The specification of a basic set of human rights that apply despite a person's income or preferences and so on is designed to avoid changes in their rights according to say, a drop in income or a change in technology that makes their work redundant. The rights problem will be discussed in the next section.

51 *Ibid.*, p. 23.

absolute exclusivity of rights may lead them into conflict where "the law of the jungle" may prevail. Other problems are that a purely private process of rights formation may not be ethically desirable and that private arrangements may provide insufficient safeguards for the dignity of people, leading to alienation with consequent losses in over-all welfare. These problems mean that "one can identify a socially desirable role for a state".[52] Given its previously outlined position that the state cannot be extracted from the market, being necessary to specify and enforce property relations or rights, Treasury then tackles its question of *how* (and how much) the state should intervene in the market. It says relevant questions include i) the objectives or criteria that guide social decision-makers in a state, ii) the likely effects of various types of state involvement in private transactions, iii) the limits of the state (those factors that may undermine the state's ability to achieve the objectives commonly expected of it), and iv) the appropriate level of state involvement that results from consideration of the previous three questions.

ii) Objectives or criteria for making social choices

Treasury says the commonly identified social objectives the state is called on to pursue include efficiency, equity, liberty, and public morals and the maintenance of human dignity. At this point, Treasury returns to its discussion on rights, saying that these issues are linked to what rights people have that the state should observe, and admits the "fundamentally political nature of rights specifications".[53] It claims it is "clearly not possible to establish that individuals have any transcendental or natural rights", so rights are relative, being grounded on mutual observance and accommodation.[54] Rights definitions are therefore a "matter of public choice and ultimately of politics". In making choices on rights it is "usually hoped" that the state's decision makers will use general criteria, and treat individuals impartially, so that rights are defined according to reason and are not political favours, or an arbitrary exercise of power.[55] Treasury claims the general criteria

---

52 *Ibid.*, p. 24.

53 *Ibid.*, p. 25. Treasury appears to be returning to a broader discussion of rights, including both human rights and property rights.

54 *Ibid.*, p. 26.

55 *Ibid.*, p. 26

usually promoted as relevant to the definition of rights are efficiency, equity, liberty, and social norms or morals.[56]

Efficiency: Treasury says a commonly argued reason for state intervention rests on the notion of market failure, which is often inferred when there seems to be a divergence between private and social costs. The argument focuses on interdependence between individuals, claiming that private individuals may fail to take into consideration the costs or benefits their activities impose on third parties. Treasury gives the examples of pollution when a factory does not take account of the cost to the neighbourhood, and public goods when a potential provider does not take account of the benefits to others and under-provides the good, for example public parks and defence.[57] Treasury dismisses concerns that in these circumstances scarce resources are not being used efficiently, saying the fact that one individual's activity may impose costs or confer benefits on a third party is insufficient reason to

---

[56] Treasury's discussion of these "criteria" to define rights to some extent shows its bias. It devotes five pages to efficiency, two pages to equity, a third of a page to liberty, and a page to public morals and human dignity. *Ibid.*, pp. 26-34. It also shows that Treasury is taking a peculiar approach to rights. Efficiency is not a generally accepted factor in definitions of rights, nor it is uncontroversial to claim that individuals do not have natural rights. A detailed discussion of the foundation of rights will not be attempted here; rather some general comments will be made on Treasury's use of rights in order to highlight some of the difficulties with its argument. Treasury's concern to maximise efficiency and control costs leads it to offer a definition of rights as "socially agreed" claims by individuals on others in society that in certain circumstances can be traded off or reduced for the greater good of others. It makes this clear in its *Government Management* annex paper, "Ethics and Social Justice", when it says that although the central tenet of social policy must be that the interests of the most disadvantaged are the first concern, "we cannot forget the interests of others in society so it is not sufficient to always attend to the need of the poor without regard to cost". *Ibid.*, p. 424. It uses the example of health care, saying that the question of what the state should do "needs to be pursued under the issue of promoting the greatest good for the greatest number". p. 425. Trade-offs between individuals are necessary, and although these "should not be carried so far as to abridge individual rights", rights are "not some absolute right which the individual takes, but are instead socially agreed rights which are offered for the individual". p. 426. This argument shows that in order for its cost-benefit approach to work, Treasury needs to treat rights as matters of negotiation whereas more conventional understandings of rights do not accept that they can be traded away in this fashion. Treasury is trying to justify a utilitarian approach to policy, but it is not universally accepted that utility and rights can be mixed in this way. For a discussion on this see Michael Freeden, "Utility and Rights", *Rights* (Minneapolis: University of Minnesota Press, 1991), pp. 83-100. Freeden also discusses natural rights -- which Treasury rejects -- as absolute, non-negotiable, universal, innate, inalienable and indefeasible, that is, they "cannot be denied without a potentially critical loss of what constitutes being human". p. 27. Treasury's weak conception of rights allows it to treat individuals as means rather than ends in themselves, which means there are no "limits to the sacrifices that can be asked of one person for the benefit of others". Will Kymlicka ,*Contemporary Political Philosophy* (Oxford: Clarendon Press, 1990), p. 104.

[57] *Ibid.*, p. 26.

discourage or encourage that individual's behaviour. Interdependence is reciprocal: for example, a polluting factory may impose costs on a neighbourhood, but it might also provide essential or highly valued services to large numbers of consumers.[58] The "problem", therefore, is to decide what rights to use air should prevail, with the question being whether the factory should be able to "harm" the neighbourhood or whether the neighbourhood should be able to "harm" the factory and its consumers. The task is to avoid the more serious harm.[59]

Expanding its discussion of efficiency and interdependence, Treasury says interdependencies can be explicitly or implicitly contracted for -- for example, neighbours of an aircraft landing strip in a remote area may have implicitly accepted the noise cost because the airline provides them with discounted trips or a service they rely on to transport themselves and goods in and out of a remote area.[60] Problems arise, however, with contracting costs, which may lead parties not to attempt to mutually accommodate all interdependencies. In the case of the polluting factory mentioned above, the costs the local neighbourhood will face if it wants to contract with the factory to change its activities are severe. Organisers will have to be found, meetings called, attempts made to achieve a consensus on how to bargain, lawyers' fees paid, and some residents may rely on the actions of others, not contributing yet benefiting from the exercise. In these circumstances, even though the value the neighbourhood places on clean air may outweigh the net benefits the factory confers (for instance, on its workers and consumers), the pollution may continue. A mutually beneficial arrangement might have been made if there had been no contracting costs.[61] Treasury denies that such uncontracted-for

[58] The costs and benefits in this example are unevenly distributed. The neighbourhood pays the costs, while the benefits accrue to the factory and consumers.

[59] *Ibid.*, p. 27. Treasury has argued against state involvement on what appears to be a utilitarian claim that the greater good should prevail, but this is inadequate reasoning. A generally accepted reason for state intervention is to protect smaller and/or weaker groups against the power of the larger groups. Treasury's argument implies that it is common sense to not "harm" the larger group, but does not acknowledge that the personal costs of doing so may be high. In the case of the polluting factory, it could be ill health or even death for neighbourhood residents.

[60] *Ibid.*, p. 28. In the real world, such an arrangement with "discounted trips" is unlikely. An airline flying to a "remote" area where people "rely" on the service to transport themselves and their goods is likely to charge a premium price rather than offer a discount. The market works according to a profit motive, not altruism.

[61] *Ibid.*, p. 28.

interdependencies indicate market failure, saying they simply reflect that there are costs to putting things right. People have weighed the benefits against the costs and decided not to attempt to correct an effect when it is too costly to do so.[62] Given the constraints, this is socially beneficial because if the uncontracted-for effects are too costly to put right then society may be better off with them.

Treasury says the role of the state on efficiency grounds then becomes first, to assess what will be the effects of alternative policy regimes and second, to assess what policy regime is to be socially preferred given the outcomes it is likely to produce. "The first question is one of analysis and is a question policy advisers can assist with. The second is a question for elected representatives who have been selected by the electorate and are accountable to them for the choices they make."[63] When efficiency is used as a guide for social decision making, it "probably" implies a concern for the maximisation of wealth in a society. Efficiency involves a concern for ensuring valuable resources are not wasted and are allocated to their most "socially productive" uses, and implies evaluating alternative institutional options according to these concerns.[64] Policy therefore needs to be based on a comparative assessment of the effectiveness of alternative policies, not on a neglect of the two-sided nature of interdependency or inadequate assessment of the sources of the problem. The full effects of state intervention must be accounted for when making social choices, and the limits of the bureaucracy to accomplish the task and assess the effectiveness of private arrangements needs to be acknowledged.[65] Given this,

---

62 *Ibid.*, p. 29. Again, the differential in power between the groups affects the argument. The interdependency is "resolved" by the party with the most power, in this case the polluting factory, getting its way. (This ties with Treasury's earlier argument on resolving interdependencies where the person with the most money obtains the resource.) The costs to putting things right are not distributed evenly across actors in the market, and those with more power (money) win, which is a reason why the state should intervene. Treasury acknowledges that a "regulatory regime" or state allocation and specification of property rights can change the contracting costs and therefore outcomes, and says these should be selected according to preferences over outcomes they produce. This would still leave power with the polluting factory, however, as Treasury argues in the next section for decisions on policy regimes to be made according to their ability to maximise wealth in society; that is, it returns to its argument that the "rights" of those who produce the greatest good should prevail. This reinforces the difficulty with Treasury's definition of rights, as discussed in footnote 56.

63 *Ibid.*, p. 30.

64 *Ibid.*, p. 30. In its previous briefing paper, Treasury says efficiency is concerned with achieving the greatest level of national income for a given quantum of resources. *Economic Management, op. cit.*, p. 296. Treasury's use of the term "socially productive", which is again linked to the ability to pay for the resources, will be analysed in chapter five.

however, the state can still improve things through "carefully selected interventions", such as changing "rights" to minimise the costs facing parties contracting or allocating "rights" to the party that is judged as able to make the most "socially valuable" use out of them.[66]

Equity: Treasury uses the terms justice, equity and fairness interchangeably.[67] It says that when the state defines access to scarce resources and resolves interdependencies through establishing rights, it defines relationships between people, making decisions that affect people's relative welfare and raising concerns for equity or fairness. Equity concerns also arise when the impact of problems of bounded rationality and information costs is not spread evenly on the population -- "Some groups for instance may be relatively less able to guard their own interests without assistance."[68] -- and if people act opportunistically to exploit one another where circumstances permit. The state historically has been seen as the "fountain of

65 *Government Management, ibid.*, p. 30. Treasury has already set these limits, saying that the state is subject to the same pitfalls as private arrangements, plus other ones.

66 *Ibid.*, p. 30. Treasury uses the example of giving parents the right to choose what food a minor should eat rather than the child, or someone who is less likely to care for the child's welfare. However, if this argument is applied to the earlier example of the polluting factory then the "beneficial results" that Treasury claims are not so easily judged. The problem, again, is the cost-benefit analysis that allows the "rights" of the more powerful to prevail, in order to achieve the greater good or the most "socially valuable" use. This will be discussed in chapter five.

67 *Ibid.*, p. 31. A detailed discussion of the problems with this approach -- treating justice, equity and fairness as interchangeable terms -- is outside the scope of this thesis, but it will be noted here that such use is not generally accepted. John Rawls is probably the most well-known proponent of justice as fairness, arguing with his "difference principle" that social and economic inequalities are just or fair as long as they enable the least well-off person in society to be made as well-off as possible. Such a situation may result in a fair distribution in that everyone is better off and no-one is worse off. However, it is not necessarily an equitable distribution according to equity theory -- where equitable outcomes are judged on contributions -- or if equity is interpreted as an attempt to equalise the distribution of income and wealth. Robert Nozick is perhaps the most obvious challenger to Rawls's views, claiming that justice is a respect for law and established rights, that is, justice is judged according to acquisition or process, not outcomes. According to this view, an outcome may be just although it is not necessarily fair or equitable. Treasury's use of these terms as interchangeable is not uncontroversial. A survey of the most basic sources, dictionaries of political and economic terms shows much disagreement as to the meaning of the terms. See John Rawls, *A Theory of Justice* (Oxford: Clarendon Press, 1972); John Rawls, *Political Liberalism* (New York: Columbia University Press, 1993); Robert Nozick, *Anarchy, State and Utopia* (New York: Basic Books, 1974); John Eatwell, Murray Milgate, and Peter Newman, eds., *The New Palgrave, A Dictionary of Economics*, vol. 2: *E to J* (London: Macmillan Press, 1987), pp. 169-172., 184., 275-276., 1039-1042.; David Miller, Janet Coleman, Alan Ryan, and William Connolly, eds., *Blackwell Encyclopedia of Political Thought* (Oxford: Blackwell, 1987), pp. 260-263.

68 *Ibid.*, p. 31.

justice", with its decision-makers called on to redefine property rights, regulate contracting practices, or tax and spend money in order to improve social equity.[69]

Three main approaches to equity are outlined: first, those that focus on outcomes or the nature of emergent social states according to some structural principle (ends); second, those that focus on the fairness of the process by which particular social states emerge (means); and third, those that focus on starting points or opportunities (beginnings).[70] Calls for equity in the distribution of income focus on outcomes while neglecting procedural aspects, Treasury says, adding that it is conceivable that "unequal distributions could be fair if they are based on acceptable or fair processes of exchange between otherwise equal individuals".[71] For example, unequal distributions may reflect differences in preferences in respect to work and leisure or the amount of training a person undertakes. On the other hand, an emphasis on process tends to suggest that whatever distribution ultimately results from a fair process is just, although a problem with this argument is identifying a "fair process". Both of these approaches ignore starting points, yet the fundamental problem with private voluntary contracting is that it is based on an initial distribution of resources and natural talents. "Concerns about the justice of private contracting are likely to arise to the extent that inequalities in these initial distributions are seen to impact both on the likely fairness of processes (for example voluntary exchange) and on the ultimate distributions that result."[72] Concerns for the weak bargaining power of a contracting agent are based on these grounds in that differences in starting points, such as wealth, information, alternative opportunities, may mean that some can drive a harder bargain than others. Treasury again discounts these concerns, saying that while this may be true, there are factors that limit these problems, including competition. No matter how poor a buyer is, if there are many sellers to choose between, competition will drive prices down towards a level that reflects all the costs of production, including a "reasonable return" for capital and risk.[73]

---

69 *Ibid.*, p. 31.
70 *Ibid.*, p. 31.
71 *Ibid.*, p. 32. Such unequal distributions are not necessarily equitable, however.
72 *Ibid.*, p. 32.
73 *Ibid.*, p. 32. Treasury does not acknowledge that a "poor" person has little or no money with which to buy goods or services, and that perfect competition of the kind envisaged as driving down

Treasury says the state's specification and allocation of rights through the tax-benefit system, regulation and other means has distributional effects, with decisions that benefit one group over another involving efficiency trade-offs. It may be that groups benefited do not maximise the social value of the rights they possess; thus a tax or subsidy may lead people to under-invest or work less.[74] Treasury links equity back to its efficiency argument, saying it also must be recognised that markets perform an important allocational task: through changes in prices, changes in demand and supply are signalled to resource owners and resources are guided to more "highly valued" uses, which assists growth and improves the welfare of all. If it interferes too much in the income received by owners in order to achieve equity, the state may adversely affect incentives to efficiently allocate and use resources. Because of this, the necessity to evaluate trade-offs between efficiency and equity "cannot be over-emphasised".[75] However, while trade-offs imply "a perfect world may not be possible", in many areas of existing policy it may be possible to improve both equity and efficiency.

Liberty: The freedom individuals have can be thought of in terms of the level of barriers to their achieving desired ends, Treasury says. The basic rule is that an individual's freedom should be as full and as extensive as that which is consistent with the freedom of others.[76] Negative conceptions of freedom emphasise limitations on others from interfering with the freedom of an individual, while positive conceptions emphasise freedom from interference *and* the ability to achieve one's own ends. Both involve the freedom to achieve objectives free of constraining conditions, with constraints for negative approaches being the interference of others and for positive approaches including lack of access to resources.

---

prices is unlikely to exist. A poor buyer may be unable to enter the market at a price that reflects all the costs of production, including a profit margin, and sellers may not want to enter the market if there is little profit (that is, the return is not "reasonable"). If competition did cause prices to fall, or the area did not offer "reasonable returns" to begin with (for example, low-income housing), then sellers may decide to invest in other areas where their returns are higher. Treasury fails to explain what happens to the bargaining power of poor buyers if there are not "many sellers to choose between". The inequality of power in the market will be discussed again in chapter three.

74 *Ibid.*, p. 33.

75 *Ibid.*, p. 33.

76 *Ibid.*, p. 33.

Public morals and human dignity: Treasury says it is often suggested that private arrangements may lead to an "undervaluation" of dignity, and that loss of dignity or alienation has important social consequences and is not merely a matter of private concern.[77] Centralised solutions "ought to be considered" if institutional standards of dignity are not privately created; a concern that allows the enforcement in law of human rights. However, because such loss is unlikely to be uniformly important in all areas, but more important for some, "public policy may therefore need to ascertain those areas where dignity is most important and examine possibilities for safeguards, beyond the general protection of human rights legislation".[78] For example, labour markets are "probably" an area where the need for sensitivity to human needs for self and social regard become important, which is why, for example, slavery was abolished even when it was based on a voluntary contract designed to discharge a debt. Despite this, some individuals may be willing to trade some of their self-respect in the short-term in order to gain in the future.[79] The effects of centrally determined institutional safeguards of dignity on output and wealth need to be considered. For these reasons, it is important to carefully analyse individuals' need for dignity and to evaluate what trade-offs alternative institutional structures may involve.

iii) The instruments of government policy and their effects

Having discussed the problems of defining social goals, clarifying objectives and identifying why they may not be achieved, Treasury then discusses the means the state has at its disposal to effect social outcomes. Taxes, subsidies, regulations and state ownership are some of the instruments by which the state

---

77 *Ibid.*, p. 34. Treasury raised this problem itself earlier, saying that alienation caused by a loss in dignity could reduce over-all welfare, which meant one could identify a "socially desirable" role for the state. p. 24 .

78 *Ibid.*, p. 34.

79 *Ibid.*, p. 34. "Nevertheless, it is possible to argue that individuals will tend to protect their desire for self-respect, and have regard to others, but not at all cost. In some circumstances, they may be willing to accept lower standards for future benefits." This is an example of Treasury's confusing use of phraseology: it is not clear what is meant by "protect their desire for self-respect" as it could be assumed that individuals would be concerned with protecting their self-respect rather than their desire for it. This clause is also difficult to relate to the second sentence which talks of "standards" and "benefits". It is hard to see how these terms are related to a "desire for self-respect". This argument is also dangerous in that it appears to be saying that slavery would be permitted if it promoted efficiency. This will be discussed again in chapter five.

specifies the rights of individuals, and they work by creating incentives that affect the behaviour of economic actors.[80] In its overview of these instruments, Treasury says the effect of subsidies or state expenditure may discourage work, or encourage investment in areas where it would not otherwise have been undertaken, which means there will be a forgone activity or opportunity cost that the state needs to take into account. Indirect costs of subsidies include that for debt financing of public sector borrowing, which affects the supply of capital and rate of savings in the economy and puts pressure on interest rates that crowd out private sector activity. Financing expenditure through taxes or debt financing has both direct and indirect equity and efficiency effects. Taxes take from one person to pay another and debt financing places a burden on future generations, which means the state needs to consider not only who gets the subsidy, but who pays for it.[81]

Treasury argues against many forms of subsidy and subsequent taxes, saying that if the subsidy receiver and the ultimate tax payer tend to be the same people, "then one needs to consider the reasons why one would want to incur the administrative cost involved in taxation to support such a spending policy".[82] Tax has equity and efficiency effects, with the former depending on whether the money is given back to the individual. If it is, then tax credits or tax rebates to the individuals may be more useful. Taxation affects efficiency by altering the incentives facing individuals and firms, creating disincentives to work and invest, and encouraging "economically wasteful" activities aimed at avoiding tax. The effects of regulation are "complex, less well understood and more hidden" than those of spending or taxation, and "it is possible to suggest that ignorance about the perverse effects of regulation may create a tendency for its overuse in the same way that smoking was widely tolerated before people knew about its costs".[83] Treasury claims that regulation prevents more effective private arrangements, raises the cost of

---

[80] *Ibid.*, p. 35. These mechanisms would appear to relate more to property rights than broader notions of rights, which would be more easily dealt with constitutionally or through a bill of rights.

[81] This argument could be just as easily applied to private contexts, such as the case of the polluting factory; that is, there is a need to consider not only who gets the benefit, but who pays for it. Treasury appears to use this line of reasoning only when it wants to limit the role of the state.

[82] *Ibid.*, pp. 36, 37.

[83] *Ibid.*, p. 37.

contracting, protects privilege, and imposes a quasi-tax on some and a quasi-subsidy on others.[84] Regulation "on balance" is often a poor means for achieving equity objectives, with the tax-benefit system being a preferred way to handle equity concerns.

Treasury contests state ownership of enterprises saying that while the companies may have been nationalised to ensure they pursued appropriate social goals, the information costs facing the state when trying to manage large commercial enterprises tends to result in the companies "proceeding to do their own thing at a net social cost".[85] Firms in competitive or "contestable" markets supplying goods to a consumer face checks on their behaviour and need to ultimately serve consumers as well as other firms can or they will be driven out of business. State-owned firms do not have the same controls because the state as owner "has a tendency to underwrite losses and a greater capacity to do so through its ability to tax".[86] Both private and state firms have the ability to hire and fire managers, but state-owned firms do not have the same checks in the form of possible take-over bids brought about by the poor performance of a company resulting in lower share-market prices that cause a decline in the value of capital assets or cash flow. Treasury claims that the first change a successful take-over company is likely to make is restructuring with a new group of managers, therefore managers of private firms have built-in checks that do not exist in the state sector "to the same extent" to stop them from pursuing sub-goals such as shirking, budget maximisation and generally inefficient policies.[87] A major problem with state ownership is the weak incentives to gather and provide information on the performance of state-owned enterprises, with "many studies" indicating the "relative poor performance or poor use of scarce resources exhibited by

---

[84] Earlier, however, Treasury argued that the threat of regulation was part of what kept large, dominant firms from behaving opportunistically and exploiting monopoly advantage. *Ibid.*, p. 20.

[85] *Ibid.*, p. 38.

[86] *Ibid.*, p. 38. This point ignores that the state may well have agreed to provide certain loss-making goods or services because they are socially desirable, but will never make the profits that would encourage a private firm to undertake their provision. For example, the cost of accident and emergency care is too high for private firms to want to enter the market, yet its provision is socially desirable. This issue will be discussed again in later chapters.

[87] *Ibid.*, p. 38, 44. It is not clear how this "restructuring with a new group of managers" is different from the ability to fire managers, which Treasury says the state can do.

state-owned enterprises".[88] Social objectives may, therefore, be more efficiently achieved through subsidies or taxes, or regulation of privately owned companies or contracts with them, rather than state ownership. In areas where the state cannot secure an objective without ownership, or there are net gains to ownership, the state needs to continually review and improve its internal management control systems because the same processes of competition as described above that lead to successful enterprises in the private sector do not exist in the state sector.

In summing up its analysis of the instruments and effects of government policies, Treasury says the increase in the size of the state and the nature of its involvement in the economy since World War II has created the need to clarify the objectives of state policy and the likely effects. "At many times in the past government policy formulation could be characterised as falling foul of the old saying that 'the road to hell is paved with good intentions'. In short insufficient attention was paid to the second round effects of government interventions given an interdependent world."[89] Fundamental principles in the formulation of policy need to include greater transparency and consistency in state policies, with increased certainty and credibility of policy stances in order to avoid any complexity that may discourage economic activity. Complex interventions may create uncertainty because of the information costs of discovering rights and obligations, and the potential for policy changes; a high level of state involvement in the economy may therefore discourage investment to the detriment of the economy's long-term potential.[90] Another principle to consider is that while redistribution through the tax and benefit systems has an important role in achieving equity objectives, there is a need to be wary of the incentives and disincentives of this form of intervention, including the

---

88 *Ibid.*, p. 38. The lack of a reference or source for "many studies" makes it impossible to judge whether these studies are of the New Zealand public sector or other countries with comparable public sectors.

89 *Ibid.*, p. 40.

90 The detrimental effect of uncertainty on investment and the subsequent impact on growth is an opinion repeated throughout the briefing papers. *Economic Management, op. cit.*, p. 110., *Briefing 1990, op. cit.*, p. 39., *Briefing 1993, op. cit.*, pp. 16, 17. Treasury appears to overlook that the aim of some state intervention -- for example, agricultural subsidies and supplementary minimum prices -- was to reduce such uncertainty and thus encourage investment.

potential to create poverty traps.[91] Targeted expenditure policies to, for example, disseminate information or enhance consumers' abilities to make choices in education or housing are also relevant. Treasury warns, however, that particular care is needed over the need to own suppliers of social services given the problems of monitoring and incentives, claiming that contractual arrangements with suppliers may provide better incentives and enable the more efficient achievement of equity objectives. Ownership, therefore, "should only be undertaken after a case has been clearly established".[92] Regulation is "generally" not a useful way to achieve equity objectives and should be restricted to the definition of rights to use resources in order to facilitate private contracting and minimise conflicts of interest.[93]

iv) The Limits of Centralisation:

Treasury identifies sources of "potential failure" in attempts by the state to minimise the problems of scarcity, interdependence, bounded rationality, information costs, and poor incentives, saying the same problems that compound or undermine private arrangements also undermine central planning, although "in many ways ... the problems may be more severe".[94] While the state can intervene to enforce "efficient rights systems" for the collective good, "equally it can fail".[95] A comparative systems approach allows the state to assess what rights system it is likely to enforce, given certain constraints and incentives, against alternatives. In intervening, the state may exacerbate scarcity by distorting the incentives of individuals, particularly with taxes and subsidies, and regulatory interventions.[96] The

---

91 *Government Management, op. cit.,* p. 40. Poverty traps and a fear of exacerbating dependency on the state are also recurring themes, especially in the social policy chapters. *Economic Management Ibid.,* pp. 249-259., *Briefing 1990, ibid.,* p. 95-117., *Briefing 1993, ibid.,* p. 84.

92 *Government Management, op. cit.,* p. 41.

93 This relates to Treasury's previous discussion on rights to resources, and whose rights should prevail (it used the example of the polluting factory). Treasury wants regulation confined to defining the rights to resources, saying there is a "fundamental need to be wary of detailed regulatory interventions restricting rights to contract" because "[s]uch interventions may hinder dynamic efficiency". *Ibid.,* p. 41. Leaving aside for now the question of whether it is possible to define rights in this way -- and the equity implications of defining such rights -- this is an important demonstration of Treasury's attitude to equity and efficiency. Treasury is prepared to sacrifice equity for efficiency without acknowledging that society may be more concerned with the former than the latter, and be prepared to forgo some efficiency to achieve equity. This will be discussed in chapter five.

94 *Ibid.,* p. 41.

95 *Ibid.,* p. 41. But what does an "*efficient* rights system" entail? Generally accepted notions of rights are not thought of in this way.

96 Treasury raises this argument in *Economic Management* (1984), saying welfare programmes,

state's ability to tax may mean it does not face the true cost of resources and the consequences for its use of resources on other sectors of the economy, and when it owns resources or organisations, its incentives to efficiently monitor the use of resources may be weak. Its efforts to tackle interdependencies may create worse outcomes because an intervention in one market may have adverse consequences elsewhere that are not foreseen.[97]

Treasury postulates that one reason for the state's difficulties in dealing with scarcity and interdependence is that it is made up of individuals subject to the same limitations as private sector actors.[98] In the private setting, individuals accept risks and adapt to unexpected occurrences, creating strategies to cope when they are caught out and have to suffer the consequences of their mistakes. With central planning, mistakes tend to be excessively costly and impact on everyone, with few alternatives being available when things go wrong.

> The bounded rationality of central planners and the complexity of the world creates strains for the relative efficacy of centrally determined solutions. Indeed, given typically economy-wide effects of government actions, the complexity of the problem solving state decision-makers are expected to engage in may place even more severe demands on their bounded rationality than is the case for private planning. The only safeguard is conscious and purposive policy review.[99]

An added problem, however, is the difficulty the state has in obtaining the information necessary to exercise judgment, meaning decisions are likely to be based on incomplete information with consequent adverse effects. Opportunism creates

---

especially tax and transfer payments, affect incentives for individuals to work and save, with many choosing not to make provision themselves for retirement or the potential temporary loss of employment. "The assumption of too large a role by the state (e.g. in caring for the blind or the intellectually handicapped) can reduce individual or voluntary organisation effort, which is often a highly effective and low-cost way of meeting social needs." *Economic Management, op. cit.*, p. 257. Although it has argued for self-reliance, Treasury appears here to accept dependency as long as it is not on the state. The problems with looking to voluntary organisations, and whether Treasury's principles foster such charitable attitudes, will be discussed in the next chapter.

97 *Government Management. op. cit.*, p. 42., and *Economic Management, ibid.*, p. 257. The impact is not only on the service in question, but also on substitute and complementary goods and services and on labour and capital markets. "Various policies adopted for the best of reasons have sometimes sought to use processes which conflict with the fundamental workings of the market, or private incentives." *Economic Management*, p. 256. For example, rent controls hold down rents in the short term, but limit the long-run supply and accessibility of rental accommodation, thus penalising future tenants. "Many studies have demonstrated this perverse effect of controls, and their tendency to discriminate against the very poor." p. 256. Note the use in *Economic Management* also of the vague term "many studies".

98 *Government Management, ibid.*, p. 42.

99 *Ibid.*, p. 42.

problems for the performance of central government as it does in the private sector, appearing in the form of political favours, featherbedding and waste of public resources. The mechanisms through which opportunism and incentive problems work in the state are "more subtle and complex than are widely appreciated", and the problems are fundamental to an evaluation of the most suitable level and form of centralised state decision making in a society.[100]

Turning to the incentives facing the state in relation to property rights, Treasury says such rights remain central in that they impact on the over-all growth of the economy, and on the rents accruing to particular groups. If coalitions of individuals can gain direct control of the state's power to define property rights, or bargain with the state to change property rights, then they can affect the value of, or acquire better, property rights. Conflicts of interest and the state's role in resolving them remain critical to the efficiency and equity of the economy, and in this respect, the state is "a double-edged sword. It can pursue generally accepted social goals or it can be diverted to pursuing the interests of particular groups."[101] The state faces dangers from capture by external sources (lobby groups) or internal sources (its own bureaucracy), and the mechanisms of policy capture and safeguards against it need to be continually reviewed.[102] External capture is possible because of the differential effects of policies on people -- benefits are concentrated on particular groups while the costs are dispersed, setting up a dynamic process where those who benefit find it easier to organise and lobby for the policy's introduction and maintenance, while

---

100 *Ibid.*, p. 43. This is an extremely negative vision of the motivations of public services, a critical analysis of which is outside the scope of this thesis.

101 *Ibid.*, p. 44.

102 Such a comment from Treasury is somewhat ironic, given the subsequent allegations about the influence of Treasury (internal capture) and the Business Roundtable (external capture) on state policy during the reforms. For arguments for and against these claims see Shaun Goldfinch and Brian Roper, "Treasury's Role in State Policy Formulation During the Post-War Era", in Brian Roper and Chris Rudd, *State and Economy in New Zealand* (Auckland: Oxford University Press, 1993), pp. 50-73.; Brian Roper, "A Level Playing Field? Business Political Activism and State Policy Formulation" in *State and Economy in New Zealand, ibid.*, pp. 147-171.; Brian Roper, "Business Political Activism and the Emergence of the New Right in New Zealand 1975 to 1987", *Political Science* vol. 44 no. 2 (December 1992), pp. 1-23.; Andrew Mansfield, *The Power Elite: the Treasury and N.Z. Business Roundtable's Power in the Formation of the Privatisation Programme 1984-1987 - A Theoretical Analysis* (Canterbury: University of Canterbury, M.A. thesis, 1990); Jonathan Boston, "The Treasury: Its Role, Philosophy and Influence", in Hyam Gold, *New Zealand Politics in Perspective* (Auckland: Longman Paul, 1992), especially pp. 204-211.; and Len Bayliss, *Prosperity Mislaid* (Wellington: GP Publications, 1994), pp. 75-78.

those who bear the costs find it too difficult to organise an effective opposition.[103] Internal capture results from the "bilateral monopoly" between a government and its bureaucracy in which elected representatives are at a disadvantage because they do not have access to the same information as their bureaucrats.[104] The bureaucracy's better information about how state services actually operate creates the potential for opportunism among its members. Treasury argues that given these limits to centralisation, what is "sorely needed" is an ongoing detailed review of the operation and performance of New Zealand's system of central government.[105]

v) The level of government involvement in the economy

In the final section of its model, Treasury says that whether or not that state "could or should effectively reduce its role to a minimalist task of merely enforcing property rights formed by private means, has to be approached on the basis of a relative assessment of the limits of private arrangements and the limits of centralised control with respect to *generally accepted criteria* for evaluating the processes and outcomes of societies discussed earlier".[106] Without a comparative systems analysis in every area of policy, it is hard to say whether the appropriate level of government involvement of the economy should be more or less, although "there are reasons for believing the level of involvement in some areas may have become too high, and that there are tendencies to generate excessive levels of government involvement".[107] These reasons include the tendencies in the past to heavily emphasise problems with private arrangements, the inadequate attention to both clearly specifying state objectives and the often adverse and hidden impacts of state

---

103 Treasury appears to overlook that this argument is equally valid to the polluting factory. The benefits accrue to the factory, which argues on behalf of its consumers, while the costs are borne by individual residents of the neighbourhood, who face difficulties in organising for effective opposition. Treasury makes selective use of the cost-benefit argument in order to justify its position.

104 *Ibid.*, p. 44. For example, it could be argued here that Treasury had to opportunity to take advantage of this "bilateral monopoly" by presenting briefing papers that outlined only one position on tackling the country's economic problems.

105 *Ibid.*, p. 45.

106 Ibid., p. 46. My emphasis. Treasury does not give details of what these "generally accepted criteria" actually are, but given the contentious nature of many of its claims throughout its state versus market model, it is likely that they are not as "generally accepted" as Treasury claims. Easton says the criteria are not generally accepted because "it gives priority to efficiency over equity, which is equivalent to favouring the income of the rich over the poor". Easton, *op. cit.*, p. 38.

107 *Ibid.*, p. 46.

policy, and the easy capture of policy by interest groups. "Government failure" as well as the need for society to find effective solutions to complex problems led to the increase in the size of the state, suggesting the need for the state to review existing policies.[108]

Treasury argues that the state needs to adopt a comparative systems analysis to review the way it organises itself because failures can be traced to institutional as well as human causes. Such an approach means assessing alternative "institutional structures" -- both state and private -- according to the processes and outcomes they involve, "utilising *generally accepted criteria* for making social choices", and requires in-depth consideration of the goals of society and the means to achieve them.[109] In comparing different means or institutions, the state should assess primarily: i) their efficiency implications by examining the incentives they create; their effect on the efficient use of information; the evolutionary or dynamic adaptability characteristics of the institution; and the scope they leave for voluntary contracting and decentralised decision making, and ii) their equity implications by examining their effect on the opportunities of individuals; their effect on the fairness of outcomes; their effect on the fairness of processes.

Conclusion

One of the ironies of the Fourth Labour Government was that it spent six years dismantling the welfare state structures that previous Labour governments had spent years developing. Even National governments had accepted the established pattern of state-society relations in New Zealand. The state had duties to its citizens to ensure they each had adequate food, shelter, education to realise their talents, treatment of illness, and an income (either from work or from the state in cases of ill health, unemployment or old age).[110] "In essence ... each individual was to have the right to be a full citizen of the society in which he or she lived and it was to be the

108 *Ibid.*, p. 47.
109 *Ibid.*, p. 47. My emphasis.
110 Colin James, *New Territory: the Transformation of New Zealand 1984-1992* (Wellington: Bridget Williams Books, 1992), p. 332.

state's duty to ensure that right was met."[111] Accordingly, the state's role was to provide good quality public services for all and to ensure that levels of income were sufficient to enable people to participate in their society instead of merely surviving.[112] Treasury has a completely different notion of the role of the state, and in a mere 40 pages in *Government Management* (1987), it makes a clear statement of the philosophical position underlying its policy approach in the four briefing papers being examined in this thesis. The model outlines a distinct change in state-society relations, with citizens portrayed as self-interested individuals entering into voluntary exchanges in the market to achieve their needs and wants. Treasury says its discussion points out the useful role of private arrangements as a means for resolving conflicts of interests and achieving collective goals even in the context of serious organisational difficulties, as well as highlighting common fallacies or misconceptions about the poor effectiveness of private arrangements. When comparing the state and the private sector, it says it is clear that the weaknesses or limits of private arrangements arising from scarcity, interdependence, information costs, uncertainty, and opportunism are also problems causing the failure of state solutions. "A comparative systems approach is 'level headed' about the limits of government, and the limits of private arrangements, eschews the blind pursuit of ideal worlds by recognising trade-offs between goals, and places emphasis on a detailed microanalytical approach or, simply, attention to detail including empirical evidence and argument."[113]

However, it is not clear that Treasury's model has actually achieved this, given its simplistic portrayal of both the market and the state. Treasury casts the market as a neutral venue for actors to meet and exchange to achieve their goals. Inequality and power differentials between actors, which cause such massive

---

111 *Ibid.*, p. 332.

112 Jonathan Boston, "Redesigning New Zealand's Welfare State", Jonathan Boston, ed., *The Decent Society?* (Auckland: Oxford University Press, 1992), p. 4 . This is not to suggest an argument in favour of all the state interventions that existed before the 1984 reform period. A distinction can be made between the interventions introduced to improve the quality of life for individuals (such as the minimum wage, access to health, education and housing, and basic infrastructure) and the interventions affecting the functioning of the economy (such as Muldoon's wage and price freeze or trade restrictions). The "duties of the state" refer to the former, not the latter.

113 *Government Management*, *op. cit.*, p. 47.

problems for outcomes in the real world, are eliminated with claims that where "exploitation, unfair trading and monopoly practices" create large profits, there will be incentives for others to enter the market, thus competition "undermin[es] the longer term survival prospects of such practices".[114] Such a view ignores that real-world competition is not perfect, and is unlikely to result in the anticipated outcome. The model also ignores that the market and the state are not aiming for the same thing -- whereas participants in the market are looking to maximise their gains, either profit for businesses or "wealth" judged on a wide range of values for individuals, the state is aiming to provide the elements of life that the market does not supply to all citizens. The state uses its coercive powers, not just to enforce the rules of the market, but the ensure that all citizens have the ability to fully participate in society. These issues will be explored in the next three chapters.

---

[114] *Ibid.*, p. 16. "Economic rents and privileges tends to be transient in the context of competitive processes, and are likely to develop and persist in the context of arrangements that inhibit such processes."

CHAPTER THREE

The political philosophy of the Treasury papers

Introduction

In advancing its model of the state versus the free market in its briefing papers, Treasury claims it is fulfilling its role of presenting "independent economic and financial advice and information to the government", an assessment backed by Finance Minister Roger Douglas in 1984 when he endorsed *Economic Management* as a "comprehensive, independent, and professional assessment of the state of New Zealand's economy and of the many difficult policy decisions which confront us all".[1] While, as Goldfinch and Roper observe, it is not exactly clear what Treasury means by "independent", it seems Treasury is claiming that its economic and financial analysis are essentially scientific and value-free, and that the department itself is politically neutral because it is not formally aligned to either of the major parties or linked to any vested interest in society.[2] On the former claim, Treasury is following neo-classical economists who "believing they are 'hard' scientists ... have attempted to establish the existence of immutable economic 'laws' which all living creatures must obey, in the same way the law of gravity must be obeyed...."[3] According to these laws, people are assumed to be rational and self-interested, pursuing their own visions of happiness in an ideal world of free individuals voluntarily exchanging in the market. The result of these exchanges is a competitive market equilibrium, which is said to allow the maximum number of individual wants to be satisfied.

Treasury's assumptions are neither apolitical nor uncontroversial. Treasury's prescriptions are not value-free or free from links to vested interests in

---

1 Shaun Goldfinch and Brian Roper, "Treasury's Role in State Policy Formulation During the Post-War Era", in Brian Roper and Chris Rudd, eds., *State and Economy in New Zealand* (Auckland: Oxford University Press, 1993), p. 64., and New Zealand Treasury, *Economic Management* (Wellington: Government Printer, 1984), p. iii.

2 *Ibid.*, p. 64.

3 Greg Davidson and Paul Davidson, *Economics for a Civilised Society* (London: Macmillan Press, 1988), p. 55.

society, because the unequal power of the actors in the market means that policies based on maximising the use of the market favour the more powerful actors. Treasury's model in fact sits comfortably with the ideology that came to be called neo-liberalism. This chapter will discuss neo-liberalism and the neo-classical economic model that underpins it before examining weaknesses in three basic assumptions it makes that cause problems for Treasury's model of state and market relations. It will show that markets do not work as the model postulates, individuals cannot be reduced to "rational, self-interested maximisers", and negative liberty, or freedom from coercion, is not enough to allow people to fully participate in society.

Modelling neutral, scientific truth

Three main propositions underpin neo-classical economics: first, that human nature is such that humans are self-interested and rational, that is they know their own interests and choose from among a variety of means in order to maximise those interests; second, that the purpose of human life is for individuals to pursue happiness as they themselves define it, therefore it is essential that they be left free to do so; and third, that the ideal social world is a gathering of individuals who are free to compete with each other under conditions of scarcity to achieve self-interested ends.[4] It is assumed that in the social world, as in the natural world with physical entities, there are forces at work that move economic agents towards equilibrium positions. This motivating force in economic life -- satisfaction of self-interest -- is contained in the first two propositions, with the third spelling out the context in which the forces work themselves out.[5] The first two propositions also contain a judgment of value that permeates the neo-classical economic paradigm: that is, if the purpose of life is the pursuit of happiness by individuals, and if individuals pursue happiness self-interestedly, then it would be good for them to receive what they want. Hence the basic notion that individuals should be free to get as much as possible of what they want. "Other value judgments of the neo-classical paradigm either qualify what types of individual wants will be considered or are derivative from this basic

---

4 Charles K. Wilber, "Ethics and Economics", in Charles Whalen, ed., *Political Economy for the 21st Century* (Armonk, New York: M.E. Sharpe, 1996), pp. 47, 48.

5 *Ibid.*, p. 48.

value judgment."[6] One such derivative value judgment is that the competitive market equilibrium is the ideal situation because it maximises the value of consumption, allowing the greatest number of individuals to be satisfied. Competitive market institutions should therefore be established whenever and wherever possible, with market prices used to determine value.[7] This sets up competitive equilibrium as an ideal and as a standard by which to measure the real value of current economic conditions. As Charles Wilber explains:

> Because it serves as an ideal for which we strive, it leads directly to the value judgment that wherever competitive markets do not exist or are weak, they should be instituted or promoted. Wherever markets do not exist, the natural competitiveness of human beings will be channelled into non-productive directions. It would be better to establish markets where this competitiveness and self-interest-seeking behaviour could be channelled into mutually satisfying activities. Wherever markets are weak and distorted due to monopoly power or government interference, there is sure to be a reduction in actual consumption. Therefore, perfectly competitive markets should be promoted so that the ideal competitive equilibrium can be achieved.[8]

Treasury claims both scientific truth and political neutrality for its model, saying it is concerned only to maximise social and economic welfare (in the Pareto-optimality sense) as determined by empirically measurable variables such as growth, inflation, and employment.[9] In its analysis, free markets are presented as a positive force to achieve the country's goals. Treasury's markets are seen as politically neutral because of the "value neutrality" of the underpinning economic theory, that is, the assumption that all values are merely preferences and economics is neutral in the choice between values.[10] When applied to the state's goals or "ends" for New Zealand, Treasury claims its policies are the "means" to achieve the desired ends. Treasury sees its "independent, value-free status" as putting it in a position to promulgate policies that represent the interests of the nation as a whole, and not just sectional interests.[11] Economics is a technical issue, focused on the best means of achieving society's ends, which are set by politicians. Economic theory, therefore, is

---

6 *Ibid.*, p. 48.

7 *Ibid.*, p. 48.

8 *Ibid.*, p. 49.

9 Goldfinch and Roper, *op. cit.*, p. 65.

10 Davidson and Davidson, *op. cit.*, p. 27.

11 Goldfinch and Roper, *op. cit.*, pp. 64, 65. In particular, Treasury says the failure of much state effort to correct "perceived" social problems arises because it has focused on desired outcomes and ignored processes (means). "That is, the question about what is the most efficient means of achieving desirable outcomes has not been addressed sufficiently". *Economic Management, op. cit.*, p. 252.

seen as equally applicable to socialist, capitalist, or mixed enterprise society, to a democracy or a dictatorship. Such a "value-free" stance leads to claims that, for example,

> In deciding whether a vaccine should be used to halt the spread of a threatened epidemic, we need not worry about the political or economic ideology of those inoculated. Nor will the optimal scheduling for refuse trucks depend on whether it is capitalist or socialist trash that is being collected.[12]

The problem with this, as Davidson and Davidson observe, is that the context of economic efficiency is of "great importance" to society: "The optimal scheduling of refuse trucks that applies to both capitalist and socialist trash can be equally useful in improving the effectiveness in transporting the victims to Auschwitz or the Soviet gulags."[13] Treasury claims markets are efficient mechanisms for identifying, transmitting and satisfying human needs and wants because they are simply mechanisms to allow contractual relations between individuals to achieve these ends. "Voluntary contracting or market exchange is thus a powerful process that allows interdependencies between individuals to be reconciled, facilitates organisational solutions to the problems of scarcity and enables scarce resources to flow to their most highly valued uses."[14] It claims economics can be separated from politics and argues implicitly, as did the nineteenth century liberals, that the "free and voluntary" contracting that occurs between individuals in the marketplace reflects a society in which power and compulsion are absent, and society is shaped by people's wishes alone.[15]

Neo-liberalism revealed

The politics inherent in this view are those of the neo-liberal paradigm, according to which most people aim to achieve prosperity and liberty, and the institutions of free markets and the limited state are said to maximise these goals better than any known alternative.[16] Markets are seen to provide the best means of allocating scarce resources so that people are as well off as they can be, given that the

---

12 Edith Stokey and Richard Zeckhauser, *A Primer for Policy Analysis* (New York: W.W. Norton, 1978), quoted in Davidson and Davidson, *op. cit.*, p. 27.

13 *Ibid.*, p. 27.

14 New Zealand Treasury, *Government Management* (Wellington: Government Printer, 1987), p. 15.

15 Karl Polanyi, *The Great Transformation* (New York: Farrar and Rinehart Inc, 1944), p. 254.

16 Norman P. Barry, *The New Right* (London: Croom Helm, 1987), p. 26.

way in which scarce resources are distributed affects individual prosperity. This proposition is defended on the grounds that markets are efficient because they reflect the transactions of people who know what they are doing when buying and selling, investing and consuming. It is assumed that when people buy and sell things, they are doing so for good reasons, and in some way must be better off after the transaction or they would not have agreed to it. T. M. Wilkinson offers a useful summation of the efficiency defence:

> A market is made up of many such transactions between many different people, and so the result of these should be that many people are better off than they were before. If we stop people making these transactions then they will be worse off than they need be. If we care about how well off people are, we should leave them to buy and sell what they want. So we ought not to interfere with market transactions by regulating, requiring or prohibiting economic actions.[17]

State involvement distorts the price signals of the market and encourages rent-seeking activities, whereby extra payment is derived over and above that required to induce the owners of a resource to supply it. The more the state is involved in the market, the less efficient the economic system is because intervention disrupts market information flows resulting in sharp differences between market and "shadow" prices leading to inefficient resource allocation.[18] State intervention "atrophies the market so that the flexibility and quick responses to changing circumstances that the evolutionary process requires is stunted".[19] The market fails because of exogenous or outside forces, not internal factors. Neo-liberals are not saying that markets are perfect, just that through the supply and demand price mechanism, they will allocate resources more efficiently than alternative mechanisms: "In settling matters of resource allocation, imperfect markets are better than imperfect states."[20]

---

[17] T.M. Wilkinson, "Rationality, Efficiency and the Market", in Jonathan Boston, ed., *The State Under Contract* (Wellington: Bridget Williams Books, 1995), p. 178. Wilkinson acknowledges that this is "a simple (and simplistic) version" of the argument.

[18] Christopher Colclough, "Structuralism versus Neo-liberalism: An Introduction", in Christopher Colclough and James Manor, eds., *States or Markets? Neo-liberalism and the Development Policy Debate* (Oxford: Clarendon Press, 1991), p. 6.

[19] Barry, *op. cit.*, p. 40. In *Economic Management, op. cit.*, p. 107., Treasury complains about the "sclerosis that has built up through the regulation of many markets of the economy", and in *Government Management, op. cit.*, p. 3., it talks of "markets that operate less efficiently than they could because they are heavily regulated (with entry barriers, unnecessary exit costs and other restrictions that create rigidities and interfere with the market clearing process)".

[20] Colclough, *op. cit.*, p. 7.

Neo-liberals therefore want the state restricted to setting and enforcing the rules by which markets operate, which means politics and economics should be separated. "Thus the role of politics should be limited to the enforcement of those general *rules* of just conduct which guarantee some predictability and certainty for transactors in an otherwise unpredictable and uncertain world."[21] The separation of politics and economics also resolves the problem of the state intervening in response to short-term pressures from electorally significant groups or sectional interests, thus distorting the market mechanism in favour of these groups, while economic processes are long-term, with the benefits diffused widely across an anonymous public. The neo-liberal view embraces that of neo-classical economics, believing applied economics to be value-free because it is concerned more with addressing the causal connection between means and ends than pronouncing on the value of the ends themselves.[22] For example, in criticising generous state welfare and unemployment benefits as providing disincentives for people to enter low-paid work, neo-liberals say they are not making moral judgments on those who choose benefits over work, because these individuals are "simply maximising their utilities in the manner prescribed by neo-classical economics textbooks".[23] Neo-liberalism also has adopted the neo-classical economic dogma that treats a nation as an aggregate of "isolated self-interested individuals locked in a perpetual struggle with each other", with the monetary incentives that shape some behaviour being taken to represent individuals in their entirety.[24] Individuals are seen to be interested only in maximising their own material wealth, and thus respond only to monetary incentives.

The Treasury model clearly reflects the neo-liberal paradigm, with many of the ideology's basic tenets restated in economic forms without their political conclusions being made explicit. In order to demonstrate the superiority of the market, Treasury has in its briefing papers presented a simplified neo-classical economic model of the market as a benevolent place of equal partners exchanging

---

21 Barry, *op. cit.*, p. 38. Author's emphasis.
22 *Ibid.*, p. 56.
23 *Ibid.*, p. 41.
24 Davidson and Davidson, *op. cit.*, p. 21.

resources according to the laws of supply and demand. In doing so, it reduces human relations to purely market or economic relations -- X wants something and is prepared to pay its owner, Y, to get it. Such transactions, in which individuals freely exercise their choices, ultimately lead to market equilibrium, and everyone is better off than they were before. The state cannot improve on these voluntary contracts because of the distortionary, second-round effects of its interventions.[25] For its model to be viable, however, Treasury has made some basic assumptions that may not hold when exposed to further scrutiny. Its assumes: i) that unhindered or unregulated markets work to produce certain outcomes (equilibrium); ii) that people can be reduced to rational self-interested maximisers; and iii) that the ultimate goal of the state is to create an environment in which these individuals can maximise their income -- "the passport to participation in society" -- which will increase their opportunities to make their own welfare-improving choices.[26]

Faults with the model: markets

i) abstracting the market from reality

In simplifying markets to voluntary contracts following the laws of supply and demand, Treasury has stripped individuals of their beliefs and divorced them from their social relations, allowing it to focus on economic actions free from "complicating" factors.[27] Yet the market is only one dimension of a society in which individuals make choices and exercise responsibility. As John Gray succinctly says: "People also live in families and belong to churches and other voluntary associations in which market exchange is inappropriate or peripheral."[28] Culture, that is, "a system of inter-related patterns of behaviour, meaning and belief", influences individuals in their decision-making, so that economics and cultural factors are intertwined and cannot be separated.[29] Economic factors and choices are shaped by

---

[25] See *Government Management, op. cit.*, pp. 35-41.

[26] *Ibid.*, p. 7., and *Economic Management, op. cit.*, p. 251. Income enables "individual choices to be utilised to maximise individual and social welfare". *Economic Management*, p. 254.

[27] Terence K. Hopkins, "Sociology and the Substantive View of the Economy" in Karl Polanyi, Conrad M. Arensberg, and Harry W. Pearson, *Trade and Market in the Early Empires: Economies in History and Theory* (New York: The Free Press, 1957), p. 286.

[28] John Gray, *Beyond the New Right: Markets, Government and the Common Environment* (London: Routledge, 1993), p. 63.

cultural factors, and cultural factors, in turn, are shaped by economic ones. This means that in order for economic terms to mean anything, they must be related to other terms, to their cultural context. In this way, "individuals ... are enmeshed in social relations and must hold dear at least those beliefs corresponding to the values defining their major role obligations."[30]

The market is only one structure through which individuals satisfy their wants and needs, and reducing the market to a simplistic construct of voluntary contracts excludes the material, institutional and social reality of economic life. The market therefore should be seen as "one category of social relations involving consumption, production and exchange under a variety of cultural and structural settings".[31] Gray quotes G.L.S. Shackle to demonstrate this point:

> The trouble is that the world is not economic. It is political-economic, it is economic only subject to unappeasable greeds and rivalries and implacable enmities. A general *economic* explanation of economic affairs is an ambition that flies in the face of history and the observable contemporary scene. The economist's only hopeful objective is to provide an account of that shawl of loosely interknotted strands which waves in the wind of the other human influences, political contention, technological invention, explosion of the population. He can seek to describe its modes of potential response to each fresh kaleidic shift of the environment, during the time till that shift is superseded by another. But he cannot tell what these shifts will be. Economic affairs are not self-contained or insulated, they cannot have a self-sufficient explanation.[32]

In the real world, the simplifying assumptions of the neo-liberal model do not hold -- "markets are embedded in complex 'social economics' that seriously inhibit the ability of market processes to function in the way that neo-classical models assume, and to produce the outcome it predicts".[33] In reality, markets are battlegrounds of social conflict and competing interests; they are political constructions that reflect the distribution of political, economic and cultural power in society generally.[34]

---

29 William M. Dugger, "Redefining Economics: From Market Allocation to Social Provisioning", in Whalen, *op. cit.*, p. 35.

30 Hopkins, *op. cit.*, p. 285.

31 Vivian Zelizer quoted in David Hogan, "The Social Economy of Parent Choice and the Contract State: Some Theoretic Issues". Paper presented at the Conference on "The New Contractualism", Griffith University (November 1995), p. 14.

32 G.L.S. Shackle, *Epistemics and Economics: a Critique of Economic Doctrines* (Cambridge: Cambridge University Press, 1972), quoted in Gray, *op. cit.*, p. 71. Author's emphasis.

33 Hogan, *op. cit.*, p. 16.

34 *Ibid.*, p. 17.

ii) unequal power in the market

Reducing markets to individuals exchanging in voluntary contracts, however, allows neo-liberals to assume that markets are powerless and have no motives; that power and compulsion are absent and the resulting society is shaped by people's wishes alone. This ignores that these "powerless" mechanisms of co-ordination contain much economic power, such that "the idea that modern society approximates, or could progressively approximate, to a world where producers and consumers meet on an equal basis seems, to say the least, implausible".[35] The reality of the free market is marked by complex patterns of market formation, oligopolistic structures and economic rivalry, not just within a state, but within regional power blocs.[36] "This is not a world in which it is at all straightforward to claim that markets are free, responsive mechanisms of collective choice."[37] Power in the market is not equal, but affected by many things, including how well endowed people are with factors of value in the market: ownership of land and capital, and possession of skills and physical attributes that affect earning power. On this point, a major flaw in Treasury's argument is obvious when it dismisses concerns for the "weak bargaining power of a contracting agent" on the grounds that this can be resolved by competition.[38] Poor "buyers" often have no money with which to enter the competitive market, which creates problems when they are meeting their "needs" or the basic goods and services needed for survival rather than their "preferences", a problem Treasury does not see because it subsumes needs into preferences.[39] Treasury's claim ignores the fact that the result of unequal power in the market -- inequality -- is a reason why states do intervene in the market. As economist Stuart Birks says: "If outcomes depended on market processes alone, the old, disabled,

---

35 David Held, *Democracy and the Global Order* (Cambridge: Polity Press, 1995), p. 245.

36 As previously stated, the argument about the effect of the global economy on national economies will not be covered in this thesis.

37 Held, *op. cit.*, p. 245.

38 Government Management, *op. cit.*, p. 32., "... no matter how poor a buyer is, if there are many sellers to choose between, competition will drive prices down towards a level that reflects all costs of production, including a reasonable return for capital and risk".

39 Competition in the free market may not result in the supply of the goods and services people "need" if these are not profitable for the supplier, for example, health and education for the poor. Suppliers are in the market to make a profit, not to ensure that the goods and services are supplied at a cost that the poor can afford. The difference between "needs" and "preferences" will be discussed in the next chapter.

orphaned and other disadvantaged groups may find themselves in an unenviable position."[40] Particularly in times of high unemployment, the power in the contractual relationship between employers and their workers is heavily weighted in favour of the former, who can replace striking workers from the pool of jobless. In a small job market such as in New Zealand, with a limited number of workplaces, it is often difficult for workers unsatisfied with the price obtained for their labour to take their skills elsewhere as there may not be an "elsewhere". Treasury's promotion of a world of self-interested individuals joined by voluntary contracts between equal partners ignores such inequalities; it also ignores, as Davidson and Davidson note, "the potential for deception and the use of brute strength to gain one's ends".[41]

In today's free markets, corporate actors, including capitalist enterprises, are increasingly influential and have transnational effects.[42] The decline in competition in the face of large concentrations of capital has left a few very large corporations dominating markets in increasing sectors of the economy. "When corporate capitals become so large that they control markets instead of being controlled by them, it can no longer be said that the market treats buyers and sellers equally, or that every exchange by definition is a just exchange."[43] Unrestrained competition between rivals may create, as Treasury says, situations where inefficient producers are penalised and efficient producers are rewarded, but this language conceals that "penalised" means the firms will go out of business and "rewarded" may lead to the remaining firm being a monopoly or member of an oligopoly.[44] While Treasury takes the neo-liberal view that the prices obtained by a monopoly would in turn attract new competition into the market and restore prices to a market equilibrium, this claim can be disputed if the entry costs to the particular industry or

---

[40] Stuart Birks, "The Public Sector: An Overview", in Stuart Birks and Srikanta Chatterjee, eds., *The New Zealand Economy: Issues and Policies* (Palmerston North: The Dunmore Press, Second Edition, 1992), p. 269.

[41] Davidson and Davidson, *op. cit.*, p. 10.

[42] Barry Hindess, "Liberty and Equality", in Barry Hindess, ed., *Reactions to the Right* (London: Routledge, 1990), p. 25.

[43] C. B. MacPherson, "The Rise and Fall of Economic Justice", in *The Rise and Fall of Economic Justice and Other Essays* (Oxford: Oxford University Press, 1987), p. 15.

[44] *Government Management, op. cit.*, p. 15., "Markets at their best resolve conflicts impersonally and ensure that over the longer term, less efficient producers are penalised and the more efficient rewarded."

service are high, the monopoly has become established in the market, or the market is too small to support more than low numbers of suppliers. Contrary to Treasury's claims, it is not only state regulation that imposes barriers to entry in the market.[45] In a country the size of New Zealand, oligopolies in many areas are likely, as was recently proved with Kiwi Air's foray into the trans-Tasman market. Competition led to an initial fall in air-fare prices, something consumers had demanded for some time, but Kiwi Air's failure returned the power to existing firms, which immediately raised their rates, not only to meet costs but to increase profits.[46] Another undesirable outcome of competition can result in times of shortage when, arguably, the price mechanism will be the most effective and efficient allocator of scarce resources. However, the consequence of competition is that the "haves", those who can afford the resource, are set against the "have-nots", those who cannot afford it, which may be a socially undesirable outcome. Davidson and Davidson give the example of petrol shortages in the 1970s, when price allocation via the market turned out to be an unfair method of rationing.[47] A much better resolution came not from the market mechanism, but from car owners agreeing to buy petrol only on certain days according to their licence-plate number. "People complied with this simple odd-even rule, not because they were forced to by their pocketbooks, but because it was a fair and just solution."[48]

iii) general factors causing market failure

Several factors may cause the free market to fail to produce an optimal outcome: imperfect information, that is, in the real world information is neither free,

---

45 Treasury says low barriers to entry are a check on monopoly behaviour, adding: "frequently, where they exist, barriers to entry are in fact created by regulation". *Government Management, op. cit.*, p. 20.

46 Air fares across the Tasman increased 32 per cent after the collapse of Kiwi Air in September 1996, with Air New Zealand justifying the increase on the basis of a rise in fuel costs (the International Air Transport Association had sanctioned a 3 per cent fuel-price rise) and demand for flights. The airline's chief executive Jim McCrea said profit had dropped 43 per cent for the last half of 1996 partly due to the cost of matching Kiwi Air's fares. He does not give the amount of profit, either before or after the drop. Sharon Williams, "Airfare rise no surprise", *Evening Post* January 16, 1997, p. 11., Les Bloxham, "Tickets to Australia soar 32%", *The Press* January 14, 1997, p. 1., and "Air New Zealand credits Kiwi with holding down airfares", *Evening Post* February 21, 1997, p. 11.

47 Davidson and Davidson, *op. cit.*, p. 17. In New Zealand, people agreed to carless days and car pooling.

48 *Ibid.*, pp. 17, 18.

readily available or intelligible by all; externalities or costs and benefits not considered in the normal economic transaction occurring in the market, for example, pollution; public goods or those goods such as defence and street lighting that may benefit society but where it is not possible to isolate users or beneficiaries to charge them according to the benefit they receive; failure of co-ordination when co-operation and co-ordination would produce a more beneficial result than unfettered competition; and inappropriate responses to risks where all individuals and firms in the market decide against taking a risk of new opportunity and under-investment occurs.[49] Treasury's claim that consumer demand will bring forth products in the market at prices to meet individuals' preferences, expressed by their willingness to buy the products, may also not be true in that advertising and propaganda may change consumer preferences. This means it is not possible to measure market efficiency in terms of satisfaction of existing demands because the market shapes preferences and choices. There is also no way of knowing whether there are unmet demands and in a small market with monopolies or oligopolies, consumers may have no choice as to whether to buy certain products, such as basic food items or electricity. Again, there is a problem between demand for preferences and a demand for needs.

Faults with the model: rational, self-interested actors

i) incentives as a motivating force

Many of the recommendations in Treasury's market model focus on the role of incentives in inducing individuals to respond in certain ways to suggested policies, with Treasury saying that economic policies generally operate by affecting the environment in which people make decisions. "Few policies operate by the government commanding directly the result it wants. Even in the public sector, the government must attempt to further its objectives by establishing a favourable incentive structure."[50] Incentives are linked to Treasury's constraint of opportunism; that individuals are motivated "at least in part" by a concern for themselves and thus have opportunistic tendencies. Treasury argues that the best form of social

---

49 Birks, *op. cit.*, pp. 266-269.

50 *Economic Management*, *op. cit.*, p. 111.

organisation involves the need to ensure individuals face incentives to align their interests with those of others.[51] Similarly, when Treasury discusses "social welfare and tax policies influenc[ing] people's attitudes to work, training and risk taking", it is assuming that such programmes act as incentives or disincentives for people:[52]

> The design of social programmes needs to consider the extent to which they undermine self-reliance. For example, do they reduce the capacity of individuals to make decisions that improve their earnings potential and health and education status? It is important to consider the *incentives* on individuals to look after themselves or for families or for voluntary community organisations to assist and these considerations are complicated by the ways in which various social policies interact to affect the level of support received and the incentives faced by different groups.[53]

When discussing social policy, Treasury says a useful principle to bear in mind for its design includes the need to strengthen the *incentives* (Treasury's emphasis) on consumers to take care of themselves and the incentives on parents, administrative and social service providers to act as effective agents of social policy.[54]

In assigning such a powerful role to incentives, Treasury is building on its assumption that people are rational, self-interested actors. By rational it is meant that individuals have a rank order of preferences and will choose those preferences ahead of others. Rationality works in markets characterised by voluntary choice and initial sets of property holdings, when individuals trade their holdings for other things that they prefer.[55] Economists claim that rational actors exchanging in this fashion

---

51 *Government Management, op. cit.*, p. 12.

52 New Zealand Treasury, *Briefing to the Incoming Government 1990* (Wellington: GP Print Ltd, 1990), p. 1.

53 *Ibid.*, p. 97.

54 *Ibid.*, p. 98. "The extent to which government can rely on the detailed information held by groups like administrators, doctors and consumers will depend in part upon the incentives these groups face. Providers need incentives to act in the interests of the intended beneficiaries of social policy. But providers are also called upon to control expenditure and ration services. Problems in creating the appropriate balance between incentives to serve beneficiaries and incentives to control expenditure may sometimes be eased by separating the roles of funding (rationing) and provision and developing competition among funders and providers. The better these incentives, the greater reliance can be placed on decentralised decision-making." Treasury fails to see that a problem with separating funders and providers is that the funders are no longer in direct contact with consumer preferences, but are responding to the demands of service providers, who are in contact with consumers. The split may mean that providers are following incentives to maximise profits rather than meet the needs of consumers. In promulgating the funder/provider split, Treasury does not acknowledge that providers may seek profits, and this may create a conflict between provider motives and consumer needs. For a discussion on problems with the funder/provider argument, see Linda McGuire, "Service Delivery Contracts: Quality for Customers, Clients and Citizens". Paper presented at the conference on "The New Contractualism", Griffith University (November 1995).

55 Wilkinson, *op. cit.*, p. 182.

will lead to efficient outcomes because when people trade to gain what they prefer, both parties are better off than before, each preferring what the other is offering and trading into their preferred situation. Because each has what they prefer relative to what they had before, there has been a gain in efficiency in terms of Pareto-optimality, that is: "A state of affairs is Pareto-optimal when there is no feasible set of affairs which someone prefers and no-one disprefers."[56] Self-interested actions arise because "the person with the strongest incentives to attend to the needs of an individual is that individual".[57]

The neo-liberal assumption of self-interest is built on the premise that the human needs which any single individual can effectively care for are those of a narrow circle of family and friends, of which the individual is the centre. "No individual or group of individuals can know or care about the effects of their actions outside this sphere nor should they seek to inhibit others from pursuing their own self-interest."[58] A rational, self-interested actor is thus someone who knows his or her own needs and wants, and who will choose according to his or her interests. The needs and wants are subjective, with individuals having their own notions of well-being.[59] This leads the neo-liberals to conclude that society's over-all well-being cannot be a goal organised collectively by the state because society's well-being simply accrues (as an aggregate) from individuals following their own self-interested paths. A major problem with this conclusion is that the very opposite may result: individual rational behaviour may lead to collective irrational outcomes. For example, individual tourist operators seeking to make money for themselves from say, organising walks through the Milford Track, may end up destroying through over-crowding and so on, the very thing on which their business is based.[60]

---

56 *Ibid.*, pp. 182, 183.

57 *Government Management, op. cit.*, p. 124.

58 Naila Kabeer and John Humphrey, "Neo-liberalism, Gender, and the Limits of the Market", in Colclough and Manor, *op. cit.*, p. 79.

59 *Government Management, op. cit.*, p. 124.

60 Another example, given by Peter Self, is that of individual farmers who may behave rationally in responding to a fall in farm prices by increasing output to maintain their incomes, but the effect is to reduce farm prices further. Peter Self, *Governing by the Market?: The Politics of Public Choice* (Boulder and San Francisco: Westview Press, 1993), p. 9.

ii) self-interested maximisers

Incentives are based on the assumption that rational self-interested individuals will choose to maximise the gains from their preferences, and take advantage of any opportunities available to them, even if this is not in the interests of others. "Selfish, jealous and spiteful" actions may result, raising the cost of social organisation and creating the need for incentives to align individuals' interests with those of others.[61] When this view of humans as rational self-interested maximisers is combined with that of the market as a place divorced from cultural and social context, the neo-liberal conception of the individual as an economic actor is revealed as "a-social, a-moral, classless, raceless, genderless, ageless, tribeless, country-less, even transcultural and transhistorical."[62] But when the actions of individuals are analysed within the neo-liberal framework, it can be seen that for the neo-liberal model to work, the individual must be interpreted as "a healthy, employed, educated white adult male" with constant preferences.[63] Such a narrow view ignores that it is not always appropriate to treat individuals as economic instruments in this way, because it ignores that people do not regard themselves as simply utility-maximising individuals, but as members of collective bodies: families, trades and professions, and ethnic groups.[64] People pursue collective interests as much as individual ones. Individuals are not "unencumbered selves", but are born into families, "encumbered without our consent by obligations we cannot by voluntary choice renounce".[65] If people did act in this rational, self-interested way, it is not clear how Treasury would encourage people to take part in the voluntary community organisations to which it assigns a growing role in its attempts to reduce the claims on the state. For example, in *Economic Management* (1984), Treasury says that the "assumption of too large a

---

61 Barry, *op. cit.*, p. 12.

62 Hogan, *op. cit.*, p. 27.

63 Desmond King, *The New Right: Politics, Markets and Citizenship* (London: Macmillan Education, 1987), p. 10. Ann Mari May explores the gender issues of "economic man" in "The Challenge of Feminist Economics", in Whalen, *op. cit.*, pp. 65-83., saying that while economic man is "unapologetically self-interested, unidimensional and autonomous", economic woman is implicitly sculpted as "altruistic, naturally affectionate, nurturing, and, most likely, always home when the kids get out of school". pp. 69, 70.

64 Andrew Sharp, "The Case for Politics and the State in New Zealand: An Introduction", in Andrew Sharp, ed., *Leap into the Dark: The Changing Role of the State in New Zealand* (Auckland: Auckland University Press, 1994), p. 14.

65 Gray, *op. cit.*, p. 52.

role by the state (e.g. in caring for the blind or the intellectually handicapped) can reduce individual or voluntary organisation effort, which is often a highly effective and low-cost way of meeting social needs".[66] Self-interested, rational maximisers are unlikely to offer their services to such groups.

iii) challenging self-interest notions

One of the most prominent writers on the issue of rational, self-interested actors, Amartya Sen, says there is an abundance of empirical evidence to indicate that the presumption of uncompromising pursuit of narrowly defined self-interest is mistaken, and it is wrong to assume everyone is constantly motivated entirely by personal self-interest.[67] Such an assumption "can significantly misrepresent the nature of social concerns and values", and implies that driven to further personal gain, people are honest only to the extent they have economic incentives for being so, and that they cannot be governed unless bribed.[68] Yet people are clearly driven by other motives including sympathy and commitment, with sympathy or concern being an emotion that directly affects one's own welfare, and commitment occurring when one believes something is wrong and is prepared to do something about it. An example of commitment would be those car-owners who chose to boycott Shell Oil over its links to the authoritarian Nigerian leadership even though the company's petrol might have been cheaper than other brands. Such motivation "drives a wedge between personal choice and personal welfare", and contradicts the assumption of rational actors in the free market being driven by price signals under which the individual always chooses to maximise material gains.[69] It could be argued that such decisions are consistent with rationality in that the

---

66 *Economic Management, op. cit.*, p. 257. In its 1990 briefing, Treasury says the design of social programmes needs to "consider the incentives on individuals to look after themselves or for families or *voluntary community organisations* to assist". *Briefing 1990, op. cit.*, p. 97. My emphasis. In 1993, it says the problems of long-term unemployment and multiple disadvantage meant effective management "may require a more substantial role for community groups or others close to the problems". *Briefing 1993, op. cit.*, p. 22.

67 Amartya Sen, "Rationality and Social Choice", *American Economic Review* vol. 85 no. 1 (March 1995), p. 15.

68 Sen, *ibid.*, p. 18., and Amartya Sen, "Rational Fools: A Critique of the Behavioural Foundations of Economic Theory", in Amartya Sen, *Choice, Welfare and Measurement* (Oxford: Basil Blackwell, 1982), p. 96.

69 Sen, *Choice, Welfare and Measurement, ibid.*, p. 94.

individual who acts according to a preference, that of foregoing cheaper prices for a principle, has increased utility, and is now happier than they would otherwise have been, but in a market economy, individuals are assumed to be driven by price. Such a broad interpretation of rationality also expands the concept to make it so all-encompassing and unfalsifiable as to be meaningless.

Part of the problem is with the assumption that an individual adopts *one* preference ordering and this is supposed to reflect her interest, represent her welfare, summarise her idea of what should be done and describe her actual choice and behaviour. As Sen observes:

> Can one preference do all these things? A person thus described may be 'rational' in the limited sense of revealing no inconsistencies in his choice behaviour, but if he has no use for these distinctions between quite different concepts, he must be a bit of a fool. The *purely* economic man is indeed close to being a social moron.[70]

There is a need to acknowledge a difference between "ethical" and "subjective" preferences, where the former is what an individual prefers on the basis of impersonal social considerations alone, and the latter is what an individual prefers on the basis of personal interests or any other basis. "This dual structure permits us to distinguish between what a person thinks is good from the social point of view and what he regards as good from his own personal point of view."[71] Individuals are not only sociable, but have consciences, with the assumption of self-interest ignoring the "abundant" other evidence that motives such as duty, loyalty, goodwill are also important, even in market relations.[72]

Faults with the model: limited notions of choice

i) the role of income

In order for rational, self-interested actors to maximise their interests, they must be free to do so, which raises the issue of choice and freedom. Neo-liberals claim that the market is the mechanism that allows individuals the freedom to choose and pursue their own conceptions of the good life. When the state is limited to setting the rules by which market exchange operates, individuals are free

---

70 *Ibid.*, p. 99. Author's emphasis.

71 *Ibid.*, p. 99.

72 Hogan, *op. cit.*, p. 36.

to engage in voluntary contracts to pursue their needs and wants. An important facet of choice then becomes possession of the factor endowments that enables participation in the market; land, labour, or capital. Treasury reduces most of its discussions on choice to income, saying that in modern economies, "a cash income provides not only the means to meet essential needs, but is also the key to wider participation in society by providing the individual with the opportunity to exercise choice".[73] The interaction of economic and social performance, therefore, is not just a question of a growing economic "cake" with consequently less pressure on how it is distributed, but "an issue of increased opportunity for individuals to make their own welfare improving choices".[74] An element of income redistribution would then appear to be justified, in order to give all members of society an equal opportunity to exercise choice. Treasury appears to argue in favour of this, saying that a crucial role for the state is to mitigate any poor results from voluntary exchanges by redistributing income among individuals, families, and other groups. "Income redistribution has the advantage of enabling individual choices to be utilised to maximise individual and social welfare."[75] However, the role that Treasury assigns to incentives and rational self-interested behaviour leads it to conclude that redistribution may decrease the incentives for individuals to choose those options that reflect self-reliance and self-responsibility. In formulating policy, the state needs to "encourage individuals to make choices for their own good", because "welfare programmes, especially tax and transfer payments, ... affect incentives for individuals to work and save".[76] It is therefore important to construct a social welfare system in a way that encourages individuals to choose to look after themselves where that option is available rather than accept a benefit.[77]

---

73 *Government Management, op. cit.*, p. 169.

74 *Economic Management, op. cit.*, p. 251.

75 *Ibid.*, p. 254.

76 *Ibid.*, pp. 259, 256. Unemployment benefits affect the incentives to quit existing jobs, to seek and accept new employment, and to acquire skills. "The higher the level of the benefit relative to wages, the more it may tend to prolong the duration of unemployment and to hinder the acquisition of skills." p. 244. Treasury says the design of the welfare system "needs to ensure that people have an incentive to accept work or undertake training, while still providing an adequate level of income". It says this raises the issue of "trade-offs between encouraging desirable behaviour and ensuring adequate living standards". *Briefing 1993, op. cit.*, p. 84.

77 *Briefing 1990, op. cit.*, p. 103.

Treasury's arguments therefore lead it inexorably to a neo-liberal paradigm in which the state's role is limited, leaving individuals as free as possible to make their own choices according to their preferences. Treasury assumes that because markets allocate resources efficiently, they are less likely than planning to interfere with liberty and opportunity, and best accord with equal concern, respect and autonomy to choose one's own conception of the good life.[78] In this context, it is promoting the classic neo-liberal conception of negative liberty, that is freedom from coercion (freedom to pursue one's preferences without interference from others). This ignores a more positive notion, where freedom is judged in terms of what one is free to do "taking everything into account, including interference or help by others, as well as one's own powers and limitations".[79] Within the context of the market, these can be seen as a difference between process, that is, the freedom to have autonomous choice or the levers of control in the individual's hands, and opportunity, which gives individuals the ability to achieve their objectives or things they have reason to value.[80] The former includes the negative freedom of immunity from the interference of others, which the market mechanism has a role in protecting because "[i]n a competitive market, the levers of decision and control are in the hands of the respective individuals, and in the absence of particular types of 'externalities' (dealing with the control of decisions), they are left free to operate them as they choose".[81] However, if importance is attached to the actual opportunity individuals have to lead the lives that each would choose, then the opportunity aspect of freedom also needs to be fulfilled. Freedom of opportunity cannot be "sensibly" judged merely in terms of possession of commodities, but must take note of the opportunity of doing things and achieving the results that each individual has reason to value. "The freedom in question must include freedom to live the way one would like, rather than judging freedom simply by commodity holdings."[82]

---

78 Arthur DiQuattro, "Political Studies and Justice", in Cohen, Ronald L., *Justice: Views from the Social Sciences* (New York: Plenum Press, 1986), p. 109.

79 Amartya Sen, "Market and Freedoms: Achievements and Limitations of the Market Mechanism in Promoting Individual Freedoms", *Oxford Economic Papers* vol. 45 (1993), p. 524.

80 *Ibid.*, p. 522.

81 *Ibid.*, p. 527.

82 *Ibid.*, p. 532.

ii) choice in context

A broader conception of choice incorporating the opportunity for individuals to achieve their objectives means that the notion of choice is meaningless if abstracted from its social and cultural context. Being free to choose says nothing about what life would be like, merely that individuals would be as free as possible to do as they wanted. The point here is that what people will want to do "will depend to a large extent on the character of the society in which they live and the conditions they find themselves occupying within it".[83] In the market, some choosers are "rich, privileged, educated, motivated, engaged, informed and sophisticated", while some are "poor, uneducated, indifferent, disengaged, and uninformed".[84] This affects the options from which each group may choose. Income redistribution, especially if it is limited to alleviating the worst poverty, may not be enough to allow people to achieve their desired choices. As previously outlined, Treasury is particularly concerned with keeping such redistribution low enough that it does not interfere with incentives for individuals to enter the market, that is, get a job, and help themselves. Those on low incomes may be free to choose, but will have limited options when the power in the market belongs to those with more wealth, especially as the more powerful actors in the market are not interested in supplying the needs of the poor, but only those goods and services that will make a profit.

"Freedom of choice" may therefore not make people more free. Quality of life is important in developing the ability to choose because lives that are dominated by poverty and hardship result in the "atrophy of the powers of choice on which responsibility depends; they are not examples of human flourishing".[85] Nor, perhaps more important, are they examples of the "fair and thriving society" that Treasury says New Zealanders want.[86] McKenna and Zannoni discuss the need for choice to extend beyond simple freedom from coercion with reference to the Aristotelian principle, which says that,

> other things being equal, humans beings enjoy the realisation of their capacities, and that this enjoyment increases: 1) the more complete the realisation of a capacity, or 2)

83 Hindess, *Reactions to the Right*, *op. cit.*, p. 24.
84 Hogan, *op. cit.*, p. 8.
85 Gray, *op. cit.*, p. 52.
86 *Government Management*, *op. cit.*, p. 9.

> the greater its complexity. A person takes pleasure in doing something as she or he becomes more proficient at it, and of two activities that she performs equally well, she prefers the one that requires the greater number of more subtle and intricate operations. Thus, a meaningful conception of the good is one that enables the person to experience difficult and meaningful challenges. ... To develop one's capacities is to fulfil one of the 'higher' ends that define a human; hence it may be concluded that an individual is defined as someone attempting to implement a conception of the good that requires the development of her or his capacities in a manner consistent with a conception of justice and the Aristotelian principle.[87]

This builds on the views of Charles Taylor that individuals develop their conceptions of the good through social interaction, so that an individual's sense of self has meaning only in the context of the social matrix within which individuals act.[88] When making choices, the individual does so within a cultural context, although the common culture does not possess an identical meaning for all. "Since different individuals find themselves differently placed in the cultural order, and since such differences can often lead to differing perspectives, individual choices will differ."[89] The neo-classical economic and neo-liberal models postulate that an individual should have a protected domain within which she or he is free to choose as she or he desires, unhindered by the actions of anyone else, including the state.[90] Framed in terms of choices among preferences, the atomistic nature of this view forbids those types of interaction of individuals that would alter the nature of the person or allow an historical or institutional context in which the choice could be made.

> Thus the neo-classical economic agent finds herself in a situation devoid of meaningful context, unable to gain meaningful insight from others. ... Neo-classical theory -- in particular, its atomist structure -- is unable to provide the resources a person would need to make a choice between [preferences]. Locked inside her individual domain, the atomistically isolated agent finds the concept of choice either irrelevant or impossible. Thus, negative freedom seems a rather hollow notion.[91]

Conclusion

Treasury has constructed a framework for policy based on what it claims is a scientific, value-free, neutral model of state and market relations. However, the model is clearly not neutral but follows the neo-liberal paradigm in its

---

87 Edward J. McKenna and Diane C. Zannoni, "Philosophical Foundations of Post Keynesian Economics", *Journal of Post Keynesian Economics* vol. 15 no. 3 (Spring 1993), p. 397.

88 *Ibid.*, p. 398.

89 *Ibid.*, p. 403.

90 *Ibid.*, p. 404.

91 *Ibid.*, p. 404.

promotion of the institutions of free markets and a limited state to allow people to achieve prosperity. This can be traced to Treasury's assumption that the neo-classical economic model, on which it wants to build New Zealand's "fair and thriving" society, is scientific and value-free. Treasury sees economics as a science following immutable laws in which self-interested actors free to pursue their own happiness compete with each other under conditions of scarcity to achieve their self-interested ends.[92] Competitive market equilibrium is claimed to maximise the value of consumption and is therefore said to be the best of all possible economic situations because it allows the maximum number of individual wants to be satisfied. Treasury has consistently argued throughout its briefing papers that its policies would increase the opportunities and the over-all welfare of New Zealanders because economic policies based on the superiority of the free market would increase growth and incomes, and decrease the size of the state and dependency on it that stunts the economy. Individuals would be left free to pursue their own interests through the objective mechanisms of the free market.

However, the "scientific" propositions of Treasury's argument contain several major flaws that challenge the likelihood of it producing the anticipated outcomes. Treasury's over-simplification of the market and the motivations of the actors within it give a false picture of what is likely to happen if policies based on this model are applied. The assumption of society "held together solely by the impersonal nexus of market exchanges ... is at best a mirage, at worst a prescription for a return to the state of nature".[93] It is not possible to extricate the market from its social and cultural context because market capacities are constrained by factors located outside the market in the community. "Power, the state, classes, interest groups, the family and other sites of preference formation ... are not so much exogenous to the market as neo-classical economics assumes, but an endogenous, and vitally important, part of the market economy."[94] People do not see themselves as

---

92 As mentioned in chapter one, in this Treasury follows the Chicago School claim that it was "a matter of observable fact [that] markets maximised economic welfare and political intervention diminished it". Colin James, *New Territory: the Transformation of New Zealand 1984-1992* (Wellington: Bridget Williams Books, 1992), p. 89.

93 Gray, *op. cit.*, p. 52.

94 Hogan, *op. cit.*, p. 11.

utility-maximising individuals but as members of collective bodies, for example, families, trades and professions, and ethnic groups. Because they think not just of their own interests but those of others, they will pursue collective interests as well as individual ones, which means they may not respond to incentives in the way that Treasury predicts.

Nor is it possible to claim that increased growth and income would maximise the over-all welfare of the community. Treasury makes this claim based on the false assumption that well-being is made up entirely of commodities that can be bought and sold by individuals. Economic goods and services are only two among several sources of satisfaction for individuals, who are also driven by other motives such as comfort and pleasure, and some notion of collective interest or good.[95] This undermines the emphasis economists place on national income and national product as measures of a rise in human welfare. Such economic indicators may be useful for their quantitative and quantifiable nature, but income is an index only of economic welfare, which is a very small part, "and often a very poor indicator", of human welfare.[96] Also, national income and other "national" measures are aggregates that conceal the status of individuals within the broader measure. For example, a high "national" income may reflect the wealth of a few rich people, which masks the true level of poverty -- and misery -- in the community. Treasury's assumptions that its policies would ultimately lead to increased opportunities for New Zealanders to choose welfare-maximising options are also problematic in that Treasury equates freedom from coercion with the freedom to pursue choices. Such a narrow notion ignores that while people may be free from coercion, they may be limited in their ability to choose to be free from a life that is "solitary, poor, nasty, brutish and short" because what they can choose may be constrained by factors including wealth, talents, family circumstances and so on. Treasury's argument for increased maximum use of the market and minimum use of the state is based on certain presumptions

---

95 Scitovsky uses over-eating as an example of people being driven by a motivation other than economic satisfaction. He says some people may overeat, continuing to eat for the pleasure of it long after their physiological hunger is satisfied. Tibor Scitovsky, *The Joyless Economy* (New York: Oxford University Press, 1976), p. 63.

96 *Ibid.*, p. 145.

about how markets work and how individuals act. Ultimately, however, because of weaknesses in these presumptions, the outcomes may not necessarily be what New Zealanders want from their modern democracy. At the very least, there is a need to be aware of the neo-liberal politics underlying Treasury's economic advice and policy framework.

CHAPTER FOUR

Applying Treasury's neo-liberal model

Introduction

New Zealand's first MMP election in October 1996 brought with it a new approach from New Zealand's media to the coverage of the election campaign. Newspapers, magazines, and television stations tossed out the old-style interviews with politicians, reports of campaign meetings, and the details of tit-for-tat spats between candidates, filling their pages and screens with public focus groups, surveys, and telephone hot-line results. The aim was to communicate to candidates the issues about which New Zealanders were concerned and on which they wanted the government to focus. The results were clear and consistent -- health, education, and care for the elderly were placed well above concerns for the economy and economic growth, the policy areas that had claimed the attention of successive governments for the past 12 years. Aucklander Kerry Alcock summed up the views of many New Zealanders when he told *North and South* about his disquiet over the direction of social policy:

> It's immoral to expect old folk to fund their medical care by having to sell their homes. I object to that very strongly. I don't think it's what New Zealanders want at all. Similarly with education. Surely a country is stronger for having its people well-educated? A system which makes education something that's available only to the highest bidder is a very sad state of affairs.[1]

These opinions demonstrate that New Zealanders, as a society, have substantive goals that cannot be reduced to economic terms. Notions of a "fair and thriving" society are defined by society's members (the community), through a political process; the state, as an embodiment of the collective will, is entrusted with intervening to secure these aims because they do not trust that market to do so.

In achieving their vision of the society in which they want to live, community members may decide to place economic growth behind their other concerns, such as whether or not each citizen has access to the basic necessities of

---

1 David McLoughlin, "New Zealand at the Crossroads: MMP election special issue", *North and South* July 1996, p. 49.

life. In other words, as a society they have decided to bear the cost of ensuring their objectives are achieved. Two areas usually entrusted to states are health and education, without which citizens are limited in their ability to participate in their community. Society assigns high values to these areas, that is, their achievement for all -- regardless of ability to pay -- is seen as desirable, and the state is expected to intervene in the market on the grounds that the market may fail to provide these "goods" to all citizens.

Treasury's neo-liberal argument for reduced state involvement in health and education, and increased use of the market, is based on the premise that the private sector is a more efficient mechanism to achieve society's aims. However, neither health nor education can easily be reduced to a commodity amenable to exchange in the market; both are valued by society in ways that cannot be reduced solely to monetary terms. It is in society's interests to have a healthy, well-educated population, and the inherent weaknesses of the market mean there is no guarantee that society's desired outcomes will be achieved if left to the private sector. When restricting health-care and education to budgets, the choice of how much should be spent, on what and on whom are political decisions that cannot be satisfactorily resolved by the market. The complex nature of health and education, and the dire consequences for both individual citizens and society of their inadequate provision, make them into political, not market, issues. This chapter will begin with a brief discussion of Treasury's views on social policy, examining its notions of social well-being and outlining Treasury's claim that the most efficient mechanism to attain the elements of social well-being is the market. It will then discuss Treasury's application of the market model to health and education, examining Treasury's views on each before offering a critique of the potential outcomes. It will show that because of the complexity of health and education, and the fact that these areas deal with "human beings, not cans of beans", Treasury's neo-liberal market model will not produce the desired outcomes.[2] The state is needed to overcome the limits of market provision. The maximum market, minimum state model does not work.

---

[2] Anna Kominik, "Health Care Still Sick After Radical Cure", *The Dominion* August 9, 1996, p. 9.

Treasury's view of social welfare

Treasury's discussion of health and education is premised on certain assumptions about the function of social policy and the relationship between social welfare, where welfare is seen as social well-being, and economic performance. A problem for Treasury is the difficulty it has in reconciling its often conflicting and confusing views on what constitutes social welfare and how it is best provided. On the one hand, Treasury takes a broad perspective, seeing social well-being as multi-faceted and a complex blend of basic needs.

> At the most basic level the fundamental requirements for well-being include food and shelter, without which life cannot continue. All people need a reasonable degree of safety from various physical dangers. This means that the maintenance of law and order is essential to social well-being. People need to be in good health so that they are not suffering from unnecessary pain or discomfort and are able to lead their lives to the full. People need to learn about the world around them so that they can participate in society and contribute productive effort to help improve their situation and that of others. People need to be able to participate in social networks that include their family or tribe and need to be able to rely on various forms of community support. The ability to relax and take part in recreational activities is important to the maintenance of well-being. Similarly, the opportunity to find and develop a cultural identity is critical and spiritual aspects of life are central to the well-being of many people.[3]

Such a definition implies a role for the state, given that if well-being is concerned with food, shelter, safety, health and education as basic needs, then the state should ensure that these are provided to all citizens. On the other hand, because Treasury's neo-liberal framework demands a limited role for the state in people's lives, it seeks to move well-being into the private sector, as something people provide for themselves. In this argument, it says social well-being is a private concern involving activities that are "mostly matters which result from private actions by individuals and people in voluntary social networks".[4] The best way for the state to achieve its social objectives is to promote a more efficient economy and a stable macroeconomic environment that is conducive to improved living standards and full employment.[5] "The main means available for the state to support social well-being is through the promotion of sound economic management."[6] A well-functioning economy increases

---

3 New Zealand Treasury, *Government Management* (Wellington: Government Printing Office, 1987), pp. 121, 122.

4 *Ibid.*, p. 122.

5 New Zealand Treasury, *Economic Management* (Wellington: Government Printing Office, 1984), p. 251.

6 *Government Management, op. cit.*, p. 122. "Balanced and consistent economic policies can be used to control inflation; until inflation is controlled it is difficult for investment to be directed into efficient activities and for savers to receive a reasonable and predictable return on their investments. In a stable economic environment with a reasonable return on investment it is likely that productive activity will be encouraged and employment can expand. Paid employment provides the cash income

the opportunities for individuals to make their own welfare-improving choices, and "in general, efficiently functioning markets can be expected to maximise opportunities for welfare gains".[7] Poorly functioning markets limit opportunities and exacerbate the need for social programmes.[8]

Such an argument rests on the notion of income, with Treasury saying that social welfare is essentially determined by the ability and opportunity to earn an income. It says that for most people, "social objectives (like dignity, security and opportunity) are met through the self-reliance that comes from working, saving and investing, and through the support offered by their nuclear or extended family at critical points in their life-cycle".[9] The most effective social policy, therefore, strengthens and supplements, rather than supplants, the "mechanisms" that permit self-reliance and family and voluntary community support. Treasury says people should be encouraged to be self-reliant, rather than looking to the state, and given incentives to take care of themselves. In keeping with its neo-liberal framework, Treasury attacks redistribution policies on the basis of the need to maintain incentives for effort and to encourage "employment and independence".[10] This creates a problem for its argument in that it does not adequately account for those people who cannot find work or whose incomes are too low to support all the needs that are part of their well-being. Treasury wants people to provide for themselves, but in order to do so, they must have their basic needs met. The argument is circular

---

that gives households the freedom to access many of the material goods and services that are critical to their well-being."

7 *Economic Management, op. cit.*, p. 251.

8 This argument is repeated in *Briefing to the Incoming Government 1990* (Wellington: GP Print Ltd, 1990), p. 96. "Social and economic objectives need to be well integrated. Economic growth may help reduce inequality, but it is not usually enough on its own to meet wider social concerns. No matter how effective social policies are, securing objectives like dignity, security and opportunity is intimately linked to economic performance."

9 *Economic Management, op. cit.*, p. 250. Income is derived either from direct involvement in economic activity (selling services), from the market activity of a spouse or parent, or from past market involvement that allowed the accumulation of savings. See also *Briefing 1990, ibid.*, p. 96.

10 *Government Management, op. cit.*, p. 170. This does not mean that Treasury argues for no income redistribution; just that benefits be kept low enough to act as incentive for people to find work and support themselves. "The costs associated with income redistribution policies suggest that there will be limits to the amount of redistribution that should be undertaken. Determining the appropriate level of redistribution thus involves a difficult trade-off between the equity values of permitting participation in society and the equity value and important efficiency questions of retaining incentives for effort for both beneficiaries and taxpayers."

-- an income is needed to provide the food, shelter, health, education and so on that are essential to well-being, but without this well-being, the ability to earn an income is limited.

Treasury says the state, in pursuing societal well-being, must contend with uncertainty in that factors influencing the well-being of individuals are complex, and the state has no better ability to predict the outcomes of social processes than any other institution. It says that given these constraints on the pursuit of well-being, it seems likely that an appropriate role for the state is to define a clear set of rights for people and to permit individuals to voluntarily transact between one another in order to pursue their own well-being.[11] In this context, rights are not solely based on promoting the free flow of efficient exchange, but also relate to equity.

> If the rights are defined in a way which supposedly permits exchange, but an individual is unable to use the opportunities offered then there would seem to be inequity of opportunity and probably inequity of outcome. In other words, equity relates to both the initial allocations of rights and resources that an individual holds, and the fairness of the processes through which people may develop their interests.[12]

Rights should be understood to include rights to the use of resources, and the definition of rights to income and income transfers are an "important part" of the state's role.[13]

While this argument would seem to present a clear case for state intervention, Treasury is reluctant to concede such a role. It says the coercive powers of the state can "sometimes" be used to achieve particular ends that would not otherwise have been realised, but for the state to intervene there must be a clear balance of benefits over costs from the proposed action, taking into account both equity and efficiency considerations.[14] While conceding there are reasons for state intervention, it warns that although this *might* improve welfare by rectifying unsatisfactory outcomes, it will be difficult for it to do so given the "inevitable costs of any such attempt": "The fact that voluntary exchanges have failed to produce the

---

11 *Ibid.*, p. 124.

12 *Ibid.*, p. 125.

13 *Ibid.*, p. 125.

14 *Ibid.*, p. 122., and *Economic Management, op. cit.*, p. 254.

'optimal' result does not mean that government processes or measures will necessarily succeed."[15] The state "does have a central role as the provider of justice", Treasury says, but it has to be aware that the "efficiency cost of complete equality would be prohibitively expensive", and that intervention to promote social justice or equity has an opportunity cost.[16] "Excessive attempts to impose a predetermined concept of justice might be very stultifying of economic activity and can act as a powerful disincentive to private and voluntary activities which could promote social well-being."[17]

The flip side of this argument, which Treasury does not mention, is that when private and voluntary activities do not contribute to social well-being, they may need equally powerful incentives to do so. Nor does Treasury justify why economic activity should be elevated above social justice or equity when it has failed to produce the expected outcomes of improved living standards and full employment. Again, Treasury seems to imply that New Zealand can have social justice and equity *or* economic growth, but not both, without explaining why this must be so. For example, in the 1993 briefing, Treasury admits that while economic growth would lead to a higher standard of living for "many" New Zealanders, lower-skilled people -- who account for half the long-term unemployed -- would be slower to benefit from growth. "A group of people experiencing multiple disadvantages -- including poor health, poor housing, low income, and low skills and education -- will, without some assistance, be less likely to benefit from growth."[18] Yet Treasury has argued against assistance on the grounds that it is bad for the economy and a disincentive to self-reliance.

---

15 *Economic Management, ibid.,* p. 256. Treasury lists four broad rationales for state involvement: providing public goods or those goods that have characteristics that suggest collective or state action to ensure their provision will increase society's welfare; acting as agent for those who lack the capacity to pursue their own welfare satisfactorily; promoting merit goods and services or particular outcomes that society deems to be intrinsically worth while; and improving social outcomes that would otherwise result from voluntary exchange by redistributing income among individuals, families and other particular groups. pp. 252-254.

16 *Government Management, op. cit.,* p. 123. This is an example of Treasury using an extreme position in order to make its own position appear moderate. Few, if any, New Zealanders would argue that the state's role is to provide "complete equality", but most are in favour of alleviating the position of the worst off in society.

17 *Ibid.,* p. 123.

18 *Briefing to the Incoming Government 1993* (Wellington: GP Print Ltd, 1993), p. 14.

Part of the problem is that Treasury is reluctant to become involved in assessments of need, which it says implies both a lack of resources and an absence of any reasonable opportunity to acquire further resources. It says that measuring a lack of resources is difficult, and identifying the absence of opportunity is even more difficult. Those in the best position to judge these issues are the individual, "neighbours, family and friends", not the state, which can never collect accurate and full information on the opportunity facing individuals.[19] Social policies should, therefore, encourage individuals to choose to look after themselves rather than accept a benefit, "so that only those in *true need*, and without reasonable alternatives, will accept state benefits".[20] While the state may want to assume responsibility for equity, aiming for a reasonable level of well-being for people with particular attention paid to those with the least access to the resources, this does not necessarily mean that the state should directly provide goods and services for those who "need" them.

Reverting to its argument that "individuals" are rational, self-interested maximisers, Treasury says that when aiming to meet the needs of the people, the state has to take into account that needs are subjective and individuals have their own notions of well-being, and that the person with the strongest incentive to attend to the needs of an individual, is that individual. "Others may have an altruistic concern, and some individuals may be self-destructive or nihilistic some of the time, but as a general rule individuals have a strong incentive to attend to their own interests."[21] These comments reflect Treasury's belief that *in general* individuals (or their guardians) can pursue their own interests satisfactorily, or at least as well as others could for them.[22] It also, however, confuses needs and wants (or preferences). It is

---

19 *Briefing 1990, op. cit.*, p. 102.

20 *Ibid.*, pp. 103, 104. My emphasis. Treasury does not define "true need", but advocates the use of an income test as well as other tests such as the presence of dependents or personal incapacity. *Ibid.*, p. 104.

21 *Government Management, op. cit.*, p. 124.

22 *Economic Management, ibid.*, p. 251. Treasury's emphasis. Treasury says that exceptions to the rule that individuals can pursue their own interests satisfactorily are, i) those whose interests conflict with others or it is in nobody's individual interest to provide a socially desirable service and collective action is therefore needed (for example, law and order); ii) those who are especially disadvantaged (for example, the disabled) or not able to take fully cognisant decisions (the intellectually handicapped and children); and, iii) when society dislikes outcomes that individuals' voluntary actions seem likely to produce and prefers alternative ones, including the distribution of income and consumption of particular goods and services (for example, it may regard home ownership as desirable). Again, while it appears

hard to see how basic needs, such as food, shelter, health, education and so on, could be "subjective" given their essential role in a person's survival. A generally accepted reason for direct state intervention in the provision of some goods and services relates to their nature as "needs" rather than "preferences". Treasury fails to produce a convincing argument that these needs would be adequately met if that provision were left entirely to the market.[23]

Applying the neo-liberal model: health

I) Treasury's view of health

Treasury says the basic objectives of New Zealand's public health policy are to improve the over-all health status of New Zealanders, use resources in the health sector as efficiently as possible, make sure individuals are not denied health care through inability to pay, to alert people to ways in which they can reduce the risks of their being afflicted by accidents and illness, and to encourage them to take preventive action.[24] The state is involved in promoting these objectives because individuals are not entirely responsible for their state of health (contracting an illness is often beyond a victim's control), society views good health as intrinsically worth while, and some individuals are unable to adequately look after their own welfare.[25] Treasury uses the World Health Organisation definition of "health" as the physical, mental and social well-being of the individual, and says the main influences on health arise from private voluntary actions of individuals and groups, and the environments in which they live.[26] Life-style related health problems caused by diet, alcohol, drugs, smoking and lack of exercise are illnesses over which society and individuals may

---

that Treasury is making an argument for considerable state intervention, it immediately contradicts its exceptions, saying that when the state assumes responsibility for individuals' decisions, " an inevitable consequence is the reduction of freedom for individuals to make their own choices". p. 253. Treasury argues that it is unreasonable for society to act as if "it knows better what is good for at least some of its members than they do themselves", and that state action may not be able to do better than voluntary arrangements in providing for individual welfare. pp. 253, 254.

23 The reasons why the market does not adequately provide for needs will be discussed in the next chapter.

24 *Briefing 1990, op. cit.*, p. 118., and *Economic Management, op. cit.*, p. 270.

25 *Economic Management, ibid.*, p. 270.

26 *Government Management, op. cit.*, p. 147.

exert some control, albeit in some areas more than others, but there are other conditions that are beyond the control of anyone:

> The relevant point for policy analysis is that most of the matters that can influence the health of individuals are beyond the control or effective influence of government ... (and are) matters which are best understood as being within the area of private choice.[27]

Health policy goals must therefore encourage people to make lifestyle choices that take account of future health risks. Such an explanation of health and health policy is limited in the emphasis it places on the individual's ability to influence their own health. While some aspects of health, as Treasury points out, are within an individual's control, others, such as genetic conditions or accidents, cannot be affected by the individual. Treasury's definition is too narrow and does not allow that while some kinds of illness or injury are a result of lifestyle choices, many -- or even most -- are not.

Treasury says that the traditional explanation of the state's role is that health, or health care, is different:

> At times of illness the need of the patient is so great, and their ignorance so profound, that any real choice and control is lost. It is suggested by many that it is best in such a context to rely on the state and the health professional to make the necessary arrangements for the care of the sufferer. Thus health policy is seen as a special case where the role for the state is to provide medical care for the ill, and public health measures which promote a healthy environment.[28]

Treasury challenges this idea using its market versus state model, and a comparison based on the constraints of scarcity, interdependence, uncertainty, information costs and opportunism. Treasury says health is subject to these constraints, and offers a short discussion on each:

Uncertainty: Treasury says illness strikes unpredictably, outcomes are uncertain, and medical treatment to repair the problem is expensive. A logical response in this situation would be insurance, where people pay in advance to spread risk over time or across the community so that the cost of health care may be paid in easy instalments while earnings are available. Treasury gives several reasons why voluntary insurance is "said to be preferable" to public finance of health care: first,

---

27 *Ibid.*, pp. 147, 148.

28 *Ibid.*, p. 148.

private markets may be more responsive to consumers' preferences than the state, which has to cater to an average New Zealander; second, people have different attitudes to risks and abilities to deal with risks, which calls for a variety of insurance policies rather than the single cover the state offers; and third, competition between insurance funds may create better incentives for controlling costs than are possible for a state funding agency.[29] Treasury acknowledges concerns about insurance markets, including that a large proportion of the population is likely to remain with low levels of cover in voluntary markets and that those with higher than average costs in terms of risk are more likely to take up insurance than those with lower risk, meaning higher costs for the insurance company, that is, for all those buying insurance policies.[30]

Information: Medicine has information difficulties for consumers, both in knowing when they will be ill and knowing how to do something about it, Treasury says. Patients may self-diagnose minor ailments, but rely on a doctor to give informed opinion on serious medical issues. The difficulty for patients of knowing whether the doctor or health professional is competent to provide care is usually resolved through regulations governing the entry and professional behaviour of health professionals.[31] Regulatory rules are justified on the grounds that they provide an equal benchmark for services and reduce the costs of searching for an appropriate provider when the consumer has little information or opportunity to "shop around". Treasury attacks this justification, saying life-long regulations are "inappropriate indicators of quality", and regulation measures quality from a professional point of view even though it is consumer satisfaction and not professional purity that is the reason for regulation.[32] Professional restrictions such as restrictions on advertising

---

[29] *Ibid.*, p. 149. Treasury gives examples of the types of cost-control methods in the private sector that it says have resulted from competition. These include part-charges, admission reviews (where the need for treatment is double-checked by independent experts), preferred provider organisations (which offer cut-price deals with selected doctors) and Health Maintenance Organisations.

[30] *Ibid.*, p. 150. Treasury says voluntary medical insurance without state assistance is likely to be unsatisfactory, and attempts to overcome this by regulation or subsidy "may prove complex, and create difficult incentive problems". Treasury does not consider the argument that a universal (state) insurance system allows the costs in terms of risk to be spread as widely as possible.

[31] *Ibid.*, p. 151.

[32] *Ibid.*, p. 152.

increase the costs of acquiring information and emphasise homogeneity, obscuring the differences in quality in the market.[33] The lack of comparative information may lower consumer influence over professional pricing decisions and lead to higher costs. Treasury says voluntary mechanisms such as brand names, trademarks and the formation of voluntary trade associations achieve the same social objectives without imposing the same costs. Such private associations are "contestable" so that if their standards and prices are unpopularly high, alternative associations may form, although on this point Treasury does not say how consumers deal with the new information problem of knowing which competing association is better.[34]

Interdependence: Treasury says the health and actions of others nearby may influence the health of an individual, but it is theoretically possible for people to voluntarily make arrangements to cope with sources of infection (for example, measles) or environmental health risks (for example, the disposal of rubbish or sewage that may become a source of infection). It says the likelihood of private arrangements arising depends on the costs of organising and implementing a deal, compared to the private gains to be made, but if the costs of the private arrangement are too high, and the state is able to offer the social benefit more cheaply, then there are grounds for state intervention.[35] However, the fact that something is identified as a public health issue does not mean that the state has to provide the service. For example, although waste disposal may be made compulsory on public health grounds, the provision of waste disposal services need not necessarily be done by the state.[36] This means that "even in the health area, the existence of interdependence is not sufficient to require direct state provision. The appropriate form of response to an issue must be defined in the light of costs and benefits to different solutions."[37]

Scarcity and equity: The central concern for equity is access to health care, and the prime concern in providing access to health care is cost, therefore

---

33 *Ibid.*, p. 152.
34 *Ibid.*, p. 152.
35 *Ibid.*, p. 153.
36 *Ibid.*, p. 154.
37 *Ibid.*, p. 154.

affordability and income distribution are central issues.[38] Treasury says that in its simplest form, the problem of privately funded health care, even with medical insurance, comes down to the question of affordability and income distribution. If people do not have adequate income to purchase health care or insurance, the state can provide assistance. The biggest concern, however, is that some individuals who choose not to insure may still require medical care they cannot afford, creating a trap for the state if it pays for those people as it creates an incentive for people not to insure in the first place.

> As soon as the state intervenes in the supply or purchase of health on equity grounds that dislocates the nexus of choice, benefit, payment and accountability. The central interest in health policy must be to design institutional structures which protect equitable access to quality health care while maintaining incentives to continue self-prevention of illness and efficiency of health care delivery.[39]

Incentives: Treasury says that when illness strikes there may "seem" to be little choice but to seek medical care, and for all members of society to have equal access to health care, they must be able to choose medical services without too much concern for cost. Both of these considerations suggest that incentives ought to be of little relevance in health, but this ignores that health care imposes costs and that there are choices in health. "Every time that choices are made that take no account of cost then there is a likelihood that resources will be misused."[40] This is so whether the choice is made by the patient or the doctor: neither faces the costs. This means that the funder (a private insurer or the state) has little control over the costs, and "often the funder must attempt to constrain costs by restricting choice".[41] Treasury says choices arise between radical and conservative treatments including complex surgery or the choice of expensive drugs, between institutional treatment or treatment at home or in the community, between preventive care or treating symptoms. All such choices are influenced by the relative cost to the person deciding the form of treatment, with an incentive to adopt the option that is the cheapest to the people involved in the choice. If the true cost is hidden, say by the cost of the drugs being

---

38 *Ibid.*, p. 155.

39 *Ibid.*, p. 155.

40 *Ibid.*, p. 156. The difficulty with this argument is that it equates "cost" solely with money. This will be discussed in a later section of the chapter.

41 *Ibid.*, p. 156.

unknown to the doctor or patient, or the state paying for institutional care, then these options may be used more often even though they are more expensive.[42] Incentives matter wherever there are choices, which means that state interventions need to avoid favouring particular forms of health care.

> Ideally policies should not choose between different treatments, but should establish an environment that is conducive to the most efficient form of care in each case, while ensuring that the equity goal of fair access to health care is protected.[43]

II) Treasury's market model

In applying the market model to health, Treasury says the state should structure health services and subsidies in ways that allocate resources to achieve the greatest benefits at the least cost. It claims resources have not traditionally been put to their best use because the provision of many services at no charge to consumers removed the role of price signals in ensuring the amount and quality of services reflect as closely as possible consumer demands and the costs of supplying them, and provision via state-funded institutions reduced the incentive for suppliers to provide services at the least cost.[44] According to Treasury, the design of the public hospital system has exacerbated the tension between fiscal and social policy goals.

> It has been difficult to ensure that we get an adequate level and quality of service for the money we spend in the public-hospital system. Problems with the efficiency of the hospitals and with access to care, which has to be rationed, are well documented. Public hospitals use a large asset base, worth perhaps $3 billion, so the efficiency with which these assets are managed has a major impact on the ability to provide services.[45]

To resolve this conflict, the state must get better value from its current health spending, and increase the level of private funding of health by those who can afford it. "Increasing the effectiveness of spending requires increased efficiency in the production of services, and increased efficiency in funding. Efficiency in funding involves paying the lowest price for a given level of service, and funding those services which best meet the needs and preferences of the community."[46]

---

42 *Ibid.*, p. 157.

43 *Ibid.*, p. 157.

44 *Economic Management, op. cit.*, p. 271.

45 *Briefing 1990, op. cit.*, p. 118.

46 *Ibid.*, p. 123. This statement appears to suggest that "effectiveness" can be equated to "efficiency". Treasury's understanding of these notions will be examined in the next chapter

i) the role of competition

Treasury argues that public institutions have weak incentives to choose efficient, minimum-cost methods of delivering quality services. Providers of hospital services therefore need stronger incentives to improve efficiency in production and keep costs down, although such cost minimisation must be balanced with safeguards on the level and quality of service provided. Treasury advocates an increased use of competition with responsibility for funding or purchasing hospital services for the community separated from responsibility for providing services. Providers would have to compete for funds on the basis of cost and quality, thereby creating the incentive to provide efficient, cost-effective services.[47] The state's withdrawal from direct provision of hospital and related services would allow it to benefit from the efficiency gains of organising public hospitals "along more commercial and businesslike lines providing medical services in direct competition with private suppliers".[48] In suggesting this, Treasury emphasises that competitive provision still allows the state to buy services on behalf of the population, and provide them to citizens free or at a subsidised rate. However, separating funders and providers of hospital services gives consumers the choice about which agency buys services for them, which could increase the "responsiveness" of the health system to consumers.[49] "Contestable" funding should lead to the private insurance industry moving from supplementing publicly funded services into a role as an alternative provider of comprehensive health care cover. It should also, "over time", lead to increased innovation and diversity in the kinds of health cover offered, and in methods used to control health expenditure while meeting consumer preferences.[50]

ii) the role of price signals

Despite these moves, Treasury still claims some form of rationing or management of the supply of care is necessary because patients and doctors do not face the full costs of their decisions. It says rationing needs to be based on "fair and

---

47 *Ibid.*, p. 123.
48 *Government Management, op. cit.*, p. 158.
49 *Briefing 1990, op. cit.*, p. 124.
50 *Ibid.*, p. 125.

rational priorities" for use of health resources, and rationing hospital services by price -- "accompanied by income assistance for poorer and sicker patients" -- should "increase further the equality of access".[51] Other cost control methods Treasury suggests include prospective payment systems (fixing in advance the price paid for treating patients), and management systems that "discourage unnecessary tests and treatment".[52] Treasury says these methods would help minimise the cost-control problem that arises when doctors and patients do not face the costs of their decisions. It also urges liberalisation to the "barriers to entry into the market" in the form of occupational licensing and regulation in order to create competition. It uses the example of the restrictions on chemists, saying that these offer little benefit to consumers, and that some liberalisation might permit more competition between chemists, and between chemists, nurses and doctors in the prescription of a "suitably restricted" range of medicines.[53]

Treasury resolves the "critical" problem of how to achieve comprehensive cover in order to give everyone access to health care without disrupting incentives by recommending that assistance for social services be offered on a targeted basis, direct to consumers where possible, leaving choice with the beneficiary of the service.[54] It advocates using price signals as incentives to encourage more individual self-responsibility when tackling lifestyle related health problems, saying that the "significant" increase in the costs of the Accident Compensation Corporation "illustrates what tends to happen to expenditure when people have little disincentive to take advantage of the benefits of a scheme and little

---

[51] *Ibid.*, p. 125. Presumably this would work by encouraging those who could pay to use the private sector, thus making public hospital services available for use by those who could not afford private health care.

[52] *Ibid.*, p. 124. Treasury does not say how "unnecessary" is to be judged.

[53] *Government Management, op. cit.*, p. 158.

[54] *Ibid.*, p. 159. This is consistent with the neo-liberal view that what limited assistance the state provides should be given in cash rather than kind so that the individual's freedom of choice is maintained. Treasury devotes four pages to a discussion on this in its *Government Management* annex paper "A Checklist of Issues for Social Policy Making". *Ibid.*, pp. 455-458. "Because we ... consider that the empowering of disadvantaged people through control over choice of services is central to a successful society and successful identification within society, we would tend to favour an increased emphasis on the provision of assistance through some form of purchasing power rather than the direct provision of goods ..." p. 458.

incentive to take action themselves to reduce the risk of accidents".[55] The increased use of incentives could persuade individuals to do more to safeguard their own health, it says:

> Greater use of charging patients in respect of the health care associated with their own actions, and/or health and accident insurance incorporating some fair and reasonable 'loadings' on to those who are in high risk groups, may encourage desirable behavioural changes.[56]

III) Critiquing the market model

Treasury takes a neo-liberal approach to health in its allocation of paramount importance to individuals as rational self-interested maximisers being free from state interference to choose their own path guided by mechanisms in the market (supply and price signals). The state's role is limited to setting the minimum rules for voluntary transactions between individuals and health providers because many of the problems in the health sector are attributed to inappropriate state interference in the market place. Resources are not used efficiently, that is, the most benefit is not achieved at the least cost, because the state does not have the same controls as the private sector. Individuals should be left free from state interference to pursue their own preferences in health, the same as in all others areas of life. However, health is different to an ordinary commodity, despite what Treasury claims. Not only is health a basic need for every New Zealander, being essential to their social well-being, but the consequences of "exchange" in the market can be dire -- lives are at stake. The market approach is unlikely to work in the health sector in the way envisaged, and may result in undesirable social outcomes. The following sections will examine the faults of the market mechanism in four areas: that it treats health as a commodity with a monetary value; that competition may fail to produce health care of sufficient quality; that people may not act in the rational manner that the model expects; and that choice is problematic in this area because the individual is not qualified to judge the standard of health care and decisions made on cost considerations alone are unlikely to fit society's goals for adequate health care for all citizens.

---

55 *Economic Management, op. cit.,* p. 271.

56 *Ibid.,* p. 271.

i) health as a commodity

Treasury sees the production, distribution, and consumption of health services as being the same as any other commodity, the supply and demand of which is best reconciled by prices set in a free market. But there are serious problems with treating health as a commodity to be bought and sold. Unlike health, the function of a typical commodity is relatively well defined, and the person who uses it is capable of judging its quality. While it may be desirable to regulate standards for the production of typical commodities, it is not necessary to interfere unduly with the production process, and much of the responsibility for assessing value for money can be borne by the consumer.[57] The same cannot be said for health, where the patient is not capable of judging the quality of care or how much health care is needed. Health professionals train for many years to achieve the levels of knowledge necessary to be proficient in medicine; the patient has limited, if any, knowledge in this area. Patients, therefore, rely on health professionals to make the best decisions for their care, and these medical specialists are expected to take the needs of the patients into account in decision-making. Needs in this sense cannot be defined in monetary terms, but include primarily curing them of their illness as well as such aspects as the relief of pain and anguish, or improving the quality of life. Patients need to know that their health professionals will make the best decision, to a certain extent regardless of cost.[58] Some health professionals may engage in self-promoting behaviour in terms of maximising their budgets, or seeking to enhance their prestige, but there is an underlying relationship of trust between patients and health professionals that the health of the patient is paramount. Resolving such a problem by introducing market mechanisms is therefore an inadequate response and may cause greater harm in that "[a]n increased tendency to view health care as a commodity to be bought and sold could damage the underlying social consensus and diminish the constraints to self-seeking behaviour by health workers".[59]

---

[57] Gerald H. Bloom, "Managing Health Sector Development: Markets and Institutional Reform" in Christopher Colclough and James Manor, eds., *States or Markets? Neo-liberalism and the Development Policy Debate* (Oxford: Clarendon Press, 1991), p. 219.

[58] This argument is not suggesting that an unlimited amount be spent on each patient, simply that generally cost would not be the first or primary consideration.

[59] Bloom, *op. cit.*, p. 220.

A distinct problem with the commodification of health is that it is not an area that lends itself to being discussed purely in terms of monetary cost. Whereas Treasury's model focuses on the "efficient" provision of services, saying that "resource waste may occur because providers lack incentives to economise", both doctors and patients may be driven by factors other than money, including (as mentioned above) the relief of pain and anguish, or improving quality of life. Treasury and health-care providers thus diverge on motives -- Treasury says medical practitioners in public hospitals may be encouraged to "raise the quality and technological level of health because they face few or diffuse costs signals", but doctors may be driven by the desire to save lives and to use all means of technology at their disposal to do so.[60] The question of how much should be spent to save a person's life is not simply one of cost, but has ethical and moral components. As such, it is a matter for society to decide through the political process. This issue will be discussed again in a later section.

ii) market failure

Although Treasury argues for the increased use of market mechanisms such as competition in the health sector, there is no reason to believe that the system would work as envisaged. Geoff Fougere points out that evidence so far is restricted to that from the United States, which is the only major developed country in which health-care provision is characterised by any significant degree of competition.[61]

> The United States example is not encouraging. This is not only because of the macro outcomes of rapid cost escalation, growing inequality of access, and poor health status indicators with which most people are familiar. It is also because a number of micro-level studies suggest that the more competitive the hospital market in a locality, the higher hospital costs, the higher the number of inpatient admissions per year and the higher the average length of stay.[62]

The separation of funders and providers may not offer many benefits for several reasons. Administration costs are likely to increase with the development of a new

---

60 *Economic Management, op. cit.*, p. 257.

61 Geoff Fougere, "The State and Health-Care Reform", in Andrew Sharp, ed., *Leap into the Dark: the Changing Role of the State in New Zealand Since 1984* (Auckland: Auckland University Press, 1994), p. 114.

62 *Ibid.*, p. 114.

level of bureaucracy between the state and the service provider.[63] In many of New Zealand's regions there are few providers of services (giving those that exist considerable bargaining power), and where there is a choice, purchasers may fund parallel services to retain options for the future and to increase the choices available to users. This may lead to the "same bundle of services" costing more in the new system than in the old.[64] Services may also cost more because providers are driven by the profit motive and not an altruistic desire to provide health services for New Zealanders. Even with "competition", providers are still likely to build in a profit margin, and will also need to cover the costs of advertising to attract the attention of both the funders and the users of the service. The separation of funders and providers may actually increase the costs of the services.

An added difficulty is that an OECD survey in 1996 showed little "real competition" between providers in health, "either because of natural local monopolies or because of the RHAs' (Regional Health Authorities') difficulties in specifying the services they want to buy with sufficient precision to permit tendering".[65] In 1996, Health Minister Jenny Shipley admitted that market models for health

> wildly overstated the potential to compete. The private sector is already very reluctant to get into acute medicine and surgery and when we use the word competition there's only a relatively small part of the sector where true competition as an alternative to the present system will emerge.[66]

A reason for this is that many areas of health care, such as trauma medicine or transplantation surgery, are inherently unprofitable because of the high costs involved. Private providers, who are seeking to maximise profits, will not want to compete in areas where there is a risk that their costs may exceed the price at which they have agreed to supply the service. This is particularly relevant when looking at

---

63 *Ibid.*, p. 115. New administration costs arise in the form of the negotiation of contracts with franchised service providers specifying price, quantity and quality, resulting in the need for new information technology, new staff and new skills. Fougere says that in the United States, 22 per cent of every health dollar is spent on administration, an amount that increased as more competition was injected into the system in the 1980s. In New Zealand in the 1995 financial year, the state injected more than $250 million into surgical services, but regional health authority estimates show that only about 40% got to its goal, with the rest lost in the "black hole" of health bureaucracy or diverted to other problems. Kominik, *op. cit.*, p. 9.

64 Fougere, *ibid.*, p. 115.

65 Kominik, *op. cit.*

66 *Ibid.*

the market model's promotion of "contracting out" of health services, where providers tender for service supply. Contracts that specify a certain price for a service have similar faults to Treasury's cost-control methods that pay for a specified number of operations in advance -- they take little account of the difference between patients and that some may be sicker than others when using the service or that some may develop complications calling for the increased use of medicines and technology. Profit-seeking market actors are risk-averse and may not enter the market in the numbers needed to make the competitive model work.

More fundamental to the competition argument, perhaps, is whether it is an "efficient" use of resources in a country the size of New Zealand to have the duplication of services necessary for true competition between providers. Given the high cost of specialised medical equipment and trained staff, duplication may escalate costs both for that service and in others if the provider has to cover the costs of purchasing equipment that sits idle when the contract is awarded to another provider. It may be a less efficient use of resources to have two or more providers in the same centre competing for funding each year when service contracts are negotiated, especially when to obtain the work they engage in attempts to undercut one another on price. The problem, of course, being as Fougere says:

> Finding effective ways to monitor quality, already a major difficulty in the old system, is an issue requiring sustained attention in the new one. Competition may encourage providers to skimp on those aspects of quality least visible to purchasers.[67]

This a particular problem in health where, as mentioned in the previous section, patients are not competent to judge on the quality of care. Given that the ultimate "purchaser" is a sick patient who may die if quality of service is poor, the cost of competition may be high both in resource use and lives.

This problem is exacerbated if user-pays charges act as a deterrent for those whose health care costs would be less if treated at an early stage. The market may not be the appropriate mechanism for allocating health resources because "there is a considerable risk that people with treatable conditions will be deterred by fees

67 Fougere, *op. cit.*, p. 115.

and that ability to pay will become an important criterion in determining the pattern of health services provision".[68] In New Zealand, for example, after the cost of visiting a general practitioner rose significantly, hospital accident and emergency departments reported an increase in the number of people attending with complaints that would have been better seen by the local doctor. More expensive medical resources were used because people tried to avoid paying their doctor, especially the much higher rate charged by after-hours medical services, by using "free" hospital services. Inadequate treatment through insufficient quality of service or a delay in obtaining health care can "generate substantial costs due to expenditure on health care, loss of working time, and disability or death".[69]

Medical Association chairman Brian Linehan warned of this is in January 1997, saying that under the market model, people may not be getting care when they need it, as evidenced by a "well-documented" increase in acute medical and surgical cases at hospitals.

> My impression is that it especially affects those in lower socio-economic groups who don't see the doctor nearly early enough. Glue ear is the classic example.[70]

British Medical Journal associate editor Tessa Richards wrote scathingly in July 1996 of the market ideology, language, principles and practices introduced in OECD countries over the last 15 years.[71] She said the market had not adequately resolved equity concerns in health, with efficiency gains having been "more than offset" by rising inequality in the quality and distribution of care. Health economists Guy and Helen Scott report that under a free market in health there are "inequities for the elderly, now paying for long-stay beds in public hospitals, those in rural areas having to travel further for hospital services, and the mentally ill".[72] Guy Scott warns of a return to the free market of New Zealand health in the 1930s:

> If you didn't have money -- and remember this was depression-era New Zealand -- you didn't get care. The aged, the orphaned, widowed, unemployed or crippled poor had to rely on private and religious charity or family and friends.[73]

---

68 Bloom, *op. cit.*, p. 221.
69 *Ibid.*, p. 221.
70 Quoted in Frances Ross, "So Much Promised, So Little Delivered", *The Dominion* January 16, 1997, p. 11.
71 Quoted in Kominik, *op. cit.*
72 Ross, *op. cit.*
73 Quoted in Frances Ross "Salvaging the System", *The Dominion* January 13, 1997, p. 11.

A problem here is that charity has inherent difficulties in that people are not legally entitled to such help and rely on the goodwill of others to provide it, which may be coercive if the person or group giving help demands behavioural changes of those receiving it. Charity is also unreliable and uneven; for example, Christchurch food banks often run short of food and have nothing to give. Such reliance on charity may be more problematic today if New Zealanders conform to the market's portrayal of them as rational, self-interested maximisers, who care little for anyone but themselves.

iii) rational self-interested maximisers

Treasury's assumption that people are basically rational, self-interested maximisers in health care as in all other areas of life may not bring the results it anticipates. For example, the assumption of using price signals as incentives to encourage more individual responsibility is fundamentally flawed. It ignores that the price signal as a disincentive for "bad" health behaviour does not work when people are well, but only after they are ill, by which time they are unlikely to care about cost in their wish to be cured. People may choose to smoke, eat and drink too much because there is a chance they may not become ill from engaging in this behaviour. While they are healthy, they do not suffer the consequences of their actions -- either physically or monetarily. The threat of having to pay for future health care may have little effect. For example, those who are not deterred from smoking by the prospect of lung cancer or heart disease are unlikely to be deterred at the prospect of having to pay more for their health care *if* they became ill at some unknown point in the future.

Tibor Scitovsky describes two other factors that undermine the rational self-interested actor approach: first, people may not be as rational about health care in the face of costs as supposed. He says that some people, especially if they are highly educated, have high expectations of what medicine -- particularly surgery -- can accomplish, and as incomes increase so may demands for medicine and medical technology:

> It is difficult for a physician to resist a patient's demands. If the patient (with a stomach ulcer) prefers a gastrectomy -- with the expectation of an instant cure -- to the effort and inconvenience of medical management, he will go from the surgeon who is reluctant to another who is more willing.[74]

Cost has not acted as a deterrent in the way Treasury envisages.[75] A second problem is what Scitovsky calls the "seduction of pleasure", which may lead to "irrational" actions. For example, some people overeat; "that is, they continue eating for the pleasure of it after, sometimes long after, there physiological hunger is satisfied".[76] Also, although people know that fresh food tastes better and is better for them, today's modern life brings a demand for quick, easy and convenient foods. Much food is bought pre-cooked (junk food) and pre-packaged (heat-and-eat), despite being high in the fats and sugars that can cause illnesses from obesity to heart disease. When the cost is not paid until illness arises, the "disincentive" of having to pay for health care may not change behaviour. In this sense, health care "is an unusual commodity. Most people prefer to have as little of it as possible. But when they are ill, they want as much as is needed to get better."[77]

iv) maximising choice

This issue of choice in health can be approached at two levels: the individual and the state. On the individual level, Treasury advocates the removal of occupational licensing and regulation, albeit not across the board, and such things as targeting of assistance for social services direct to consumers, leaving choice to the individual. Treasury neglects the information problems of making choices, that people may not be interested or have enough knowledge -- they want only to get well -- and that some people may be too sick to "rationally" consider their options for treatment. It also ignores the information problems that patients face in choosing from the range of health care options and health professionals. Treasury claims that professional restrictions on advertising increase the costs of acquiring information and obscure differences in quality in the market, which suggests that Treasury sees

---

74 Tibor Scitovsky, *The Joyless Economy* (New York: Oxford University Press, 1976), p. 169.

75 Arguably, this does not matter if these people are paying the costs themselves, but the example shows that people may not be as rational as supposed.

76 Scitovsky, *op. cit.*, p. 63.

77 Bloom, *op. cit.*, p. 220.

advertising as a better source of information than regulatory standards.[78] It also overlooks that the person with the flashiest advertisement or the cheapest service may not be offering an adequate standard of care and that advertising does not provide reliable, impartial information on which patients can make good decisions. The removal of professional licensing and restrictions on advertising may exacerbate the information problems facing patients. Health workers are trained to "subject patients to risk by recommending the use of toxic chemicals and cutting the body surgically", which means that the consequences of a "bad" choice of practitioner can be very serious or even fatal.[79] Because the patient cannot assess the advisability of a particular form of treatment without expert advice, it is not clear the market would be the best mechanism for ensuring the services provided are of adequate quality.[80]

At the state level, Treasury's discussion of the market in health ignores the fact that many of the basic questions about health-care provision are political questions that must be answered in the public arena. Given the ever increasing technology in health care, and the ability to keep people alive for long periods using expensive equipment and drugs, the basic question in health provision becomes "what price life", a question society may not want doctors -- or accountants -- to answer.[81] Decisions need to be made on how much of society's resources should be spent on health over education or housing or defence, how these resources are then to

---

[78] *Government Management, op. cit.,* p. 152. Treasury says the lack of comparative information provided by advertising "may also lower consumers' influence over professionals' pricing decisions and lead to higher costs". Such statements demonstrate a startling faith in advertising to be truthful and accurate.

[79] Bloom, *op. cit.*, p. 219.

[80] This point was confirmed in January 1997 by Medical Association chairman Brian Linehan who said: "The competitive model assumes the consumer can make an informed choice as in the commercial market, but that's not so. Health is different because of the asymmetry of information between the doctor and the patient, so the patient can't really make an informed judgment." Frances Ross, "So Much Promised, So Little Delivered", *The Dominion* January 16, 1997, p. 11.

[81] Nor may doctors want to answer this question. Arguably, physicians follow the technological imperative, which holds that technology should be used if it offers any possibility of benefit, whatever its cost. "Whether to protect themselves from malpractice suits, to provide the most thorough care for the patient, or to increase profit, many physicians would rather err -- heavily -- on the side of over-using diagnostic and therapeutic technology." Robert H. Blank, *Life, Death and Public Policy* (DeKalb, Illinois: Northern Illinois University Press, 1988), p. 13. While this comment obviously applies to the United States, where doctors more easily may be sued than in New Zealand, given the recent high-profile manslaughter trial of heart surgeon Keith Ramstead, few doctors would want to face court action on the grounds that they had not done enough to save a patient's life. Decisions on the limitation of the use of high technology therefore must be made by society via the political process.

be distributed among the many areas of health care, and to whom.[82] The elevation of the individual and individual choice in the market model is problematic to cost containment because an individual's "rights" to health care may increase costs. Market-driven solutions are "bound to fail because they serve to reaffirm individual claims to resources and favour acute care for individuals, regardless of prognosis, over those measures which would improve the health status of the community as a whole".[83] If health resources are limited, and full and complete care cannot be given to everyone, then the systems by which individuals qualify or are excluded must be decided.[84] Such choices about rationing in health care are political because the consequences are counted not just in resources, but in lives. Allocation decisions will mean the difference between life and death for thousands of individuals, so it is essential that the criteria for making these decisions be clarified and monitored to ensure that all members of society are well served by the health-care system.[85] Robert Blank argues that those who claim that competitive forces, if left alone, will resolve the problems of spending priorities and moderation of unrealistic expectations, "obscure the complexity of these issues".[86] Only the state can act to redistribute opportunity for care in an equitable fashion and invest in public goods and services. The market cannot enable the just distribution of resources when the prime beneficiaries of the lower costs -- and lower taxes -- of the re-ordering of health care priorities are members of future generations who have no means to influence today's marketplace. Initiative for change must come from those persons who supposedly represent the best interests of the nation as a whole.[87]

IV) Summary

Treasury's neo-liberal model is based on weak assumptions and fails to prove that health is not a special case that should not be exposed to the vagaries of the unfettered, unregulated free market. Its arguments about constraints -- uncertainty, information, interdependence, incentives, and scarcity and equity -- that

82 Robert Blank, *Rationing Medicine* (New York: Columbia University Press, 1988), pp. 77, 78.
83 Blank, *Life, Death and Public Policy, op. cit.,* p. 133.
84 *Ibid.,* p. 136.
85 *Ibid.,* p. 135.
86 *Ibid.,* p. 135.
87 *Ibid.,* p. 135.

lead it to recommend a greater role for the market in health care can equally serve as arguments why the state should intervene to ensure an adequate level of care for all society's members. Competition does not resolve the constraints of uncertainty, information or interdependence, but may exacerbate them, particularly because of the difficulty patients have in judging quality of care. Incentives may not act as anticipated because cost is an inadequate mechanism by which to make judgments about health provision. The use of incentives such as price signals may increase the problems of scarcity and equity. Treasury's arguments based on these constraints either do not hold up to scrutiny or are equally applicable to an argument for state involvement. If the market cannot be depended on to ensure the provision of efficient, effective and safe health services then the state has a role in doing so.

Applying the neo-liberal model: Education

I) Treasury's view of education

New Zealand's formal education system is predominantly a state system with the direct provision of educational services as the dominant form of state intervention. The state is involved in providing or facilitating provision of education because of the general view that education is a public good that benefits society as well as the individual who acquires it, and that it is a good with such merit that the state is prepared to support its acquisition.[88] State involvement also relates to the problem of inadequate choice or foreknowledge on the part of children, and that education can be a means of improving income distribution and reducing social inequality.[89] Treasury says education performs various functions: it fulfils the individual, integrates the individual within the community and wider society, and prepares the individual for an economic role, either paid or unpaid. The costs and benefits of education accrue to different groups: the individual being educated, the parent or agent of the individual being educated, the community or society as a whole (including the economy), and providers of institutional education: teachers, administrators and support staff.[90] These costs and benefits can take monetary or

88 *Economic Management, op. cit.*, p. 267.

89 *Ibid.*, p. 267.

90 *Government Management, op. cit.*, p. 133.

other forms, and may take effect immediately (consumption) or in the future (investment).

Treasury says the state intervenes in the market provision of education because significant difficulties arise in contracts between providers and individuals or parents seeking private educational provision. It says there are four main reasons for intervention:[91]

Who pays: (equity concerns arising from scarcity) Not all individuals or parents are equally able to purchase suitable education, therefore the net benefits that society and individuals draw from education are not fairly distributed to all.

Who chooses: (the agency problem arising from bounded rationality and information problems) Many of those being educated are children who are not in a position to make strategic decisions about their future or know the consequences; they are exposed to agency failure if their parents do not act in their interests.

Who benefits: (arising from interdependence) Societal costs and benefits may not be fully captured by the individuals being educated or their agents.

Who is accountable: (efficiency concerns arising from the potential for opportunism and uncertainty in relation to the provider) This includes, for example, the risk of the private provider going out of business.

Treasury says these issues raise problems in private provision because of the long-term investment nature of education, as opposed to short-term costs. Potentially, state intervention answers these difficulties because it can redistribute educational and consequent life chances in society in favour of the disadvantaged; assist parents in their role and safeguard children against parental failure; ensure that net benefits to society are maximised; and ensure efficiency in the institutionalised state sector."[92]

However, Treasury then attacks New Zealand's high degree of optimism as to the potential of formal education to contribute to both economic growth and equity, saying that in other OECD countries there is increasing doubt

---

91 *Ibid.*, pp. 133, 134.

92 *Ibid.*, p. 134.

about the role of state education in delivery of these benefits.[93] Each of the four reasons for intervention also brings difficulties. It claims that on equity, there is "evidence" that institutional education makes little, if any, difference to the relative position or life chances of most groups, and some interventions may increase inequity.[94] On agency issues, state intervention may reduce parental responsibility and increase dependence on subsidised institutional provision; on interdependence, intervention runs the risk that benefits will be captured by particular groups of individuals or providers, meaning the cost becomes public but the benefits remain private, and on efficiency, the inefficiencies of the central bureaucracy may reduce the ability of individuals to hold anybody to account. The state thus faces the same four problems as private contractors, and has greater difficulty than the individual or family in measuring the benefits. This has led to inputs being used as measures of success, with the resulting "misapprehension" that more is necessarily better, and has created problems with determining goals and parameters for intervention. Accountability under state intervention is problematic because "consumers" have a common interest in reducing the direct cost of education to themselves and "providers" enjoy greater job security and improved career paths as state support increases. "If decisions are made centrally by the government, both consumers and providers will seek representation and rights at the centre, rather than contracting with each other. Hence, providers cease to be accountable to consumers and accountability becomes lost in the bureaucracy."[95]

Treasury is concerned with these problems because it says a well-performing education system is critical to achieving economic as well as social objectives.

> To secure a high-wage, high-employment economy in New Zealand requires rates of productivity growth comparable to those in the best-performing economies in the world. New Zealanders need to be as well educated and trained as the Americans, Europeans and Asians against whom we compete.[96]

---

93 *Ibid.*, p. 134.

94 *Ibid.*, p. 135. This is another example of Treasury using the blanket term "evidence" to justify its position without giving any references or context.

95 *Ibid.*, p. 134.

96 *Briefing 1990*, *op. cit.*, p. 129. This does not mean that education should be provided by the state, but that the education system -- both state and private elements -- should be performing as well as possible to ensure New Zealanders achieve competitive levels of education.

Poor performance in the education sector adversely affects the labour market, and in turn, the over-all performance of the economy.[97] The link between education and social well-being through the labour market, in particular, is a strong reason why policy review and change in this area is important, it says. Public sector institutions must be efficient and responsive to the demands of "trainees" and employers, offering a range of learning opportunities.

> If they are to boost their contribution to productivity, and improve their ability to raise the skills of low-skilled people, the institutions will need to adjust rapidly to changing labour market needs. The quality of service they provide will be important.[98]

According to Treasury, the difficulties in the performance of the education sector -- for example, the mismatch between school leavers' skills and the demands of the labour market -- reflect underlying problems. These are concerned with the efficient use of resources in an environment where price signals (reflecting consumer demand and resource costs) do not operate to direct resources to the areas of highest return to the community, education suppliers are relatively independent of the need to satisfy consumers in order to obtain funding and so incentives to respond to consumer monitoring are relatively weak, and competitive incentives to minimise costs are also weak.[99] It says the shortcomings of the education system in efficiently achieving appropriate education appear to stem largely from the way in which education is supplied, and substantial improvements in performance may require changes to the nature and concept of education delivery. Treasury identifies the key issues as the extent of government subsidy appropriate to different education sectors (especially tertiary education); the targeting of education resources (in order to equalise education opportunities); and the larger question of the extent to which government should directly provide education rather than subsidise it.[100]

---

97 *Economic Management, op. cit.*, p. 268.

98 *Briefing to the Incoming Government 1993* (Wellington: GP Print Ltd, 1993), p. 86.

99 *Economic Management, op. cit.*, p. 268.

100 *Ibid.*, p. 270.

II) Treasury's market model

Treasury says education is "never free as there is always an opportunity cost to the provider".[101] Formal education is, therefore, "unavoidably" part of the market economy and the state must be as concerned with the effectiveness and "profitability" of its expenditure on education, in relation to its aims, as private providers would be in relation to their expenditures. In discussing education within the market framework, Treasury says the size of New Zealand's fiscal problems means it is no longer possible to spend an ever-increasing amount of money to advance the government's educational objectives. Reforms are needed to get better results from the money invested in education, including reconsideration of the role of the state in the regulation, funding and provision of education services, and a bigger role for parents, students, and competitive private providers.

i) increasing choice and competition

Reforms giving parents more information and more effective choice will strengthen pressure on schools to respond to demands and will yield better educational results, Treasury says. "To take maximum advantage of informed decision-making also requires consideration of the benefits of greater competition between schools in meeting parents' demands."[102] If parents could choose freely, and state funding moved automatically with the child, schools would be put under greater pressure to perform. "The result would, in principle, be that the more responsive schools would attract students, less popular schools would face pressure (as a result of declining rolls) to change. Those which did not change might eventually be taken over by better personnel moving from the successful schools."[103] Treasury attacks zoning and limited subsidy to private schools as "disabling tactics, restricting choice", with zoning as a monopolist practice that restricts choice and competition.[104] It advocates extending the competition for funds to schools currently outside the state system, that is, private schools -- "if access and equity problems could be resolved" --

---

101 *Government Management, op. cit.*, p. 133.

102 *Briefing 1990, op. cit.*, p. 134., and *Government Management, ibid.*, p. 138.

103 *Briefing 1990, ibid.*, p. 135.

104 *Government Management, op. cit.*, p. 141.

saying this would add to parents' ability to pressure for change. It affirms its commitment to choice and competition, saying,

> Choice and competition are each more valuable in the presence of the other. Choice is of little interest if all suppliers are similar or if some suppliers are much more expensive because they are less subsidised. Competition has little value when providers and consumers cannot respond to it. This suggests that movement on both fronts would be more valuable than on only one.[105]

Treasury is convinced that increasing competition will solve the problem of individuals and parents being "rationally ignorant" about education, which it says is caused by the high cost of obtaining information and the limited choice. Individuals will benefit from greater choice and the pressure this exerts for attainment of the standards achieved by the best schools, and individuals will become well-informed "when it is worth-while for them to be so".[106]

ii) tertiary education as a private good

In applying its market model to education, Treasury reserves its strongest criticism for the tertiary sector, saying strong social policy reasons cannot readily be established for the direct, and largely free, state supply of tertiary services.[107] Tertiary education is a "discretionary investment or consumption" decision, making it more a private than a public good because individual users capture most of the benefits of the higher education in their own higher lifetime earnings or increased utility. "Demand for education is substantially derived from the need to acquire labour market skills and because of this individuals have clear incentives to invest in education."[108] Employers benefit because education reduces the transaction costs in hiring staff and may enable them to externalise training costs. While the state may wish to ensure access at tertiary level regardless of ability to pay, "a more selective, targeted approach would meet this objective with least wastage".[109] Problems with tertiary education are associated with relative insulation of suppliers from consumers, low incentives to minimise costs, and sluggish ability to change resource distribution for optimal return.

---

105 *Briefing 1990, op. cit.*, p. 135.
106 *Government Management, op. cit.*, p. 141.
107 *Economic Management, op. cit.*, p. 268.
108 *Ibid.*, p. 268.
109 *Ibid.*, p. 269., and *Government Management, op. cit.*, p. 143.

Treasury says its analysis suggests a relatively strong case can be made for greater use of market processes in the provision of tertiary education, with initial changes including the recasting and reducing of existing public spending. "Significant immediate initiatives could include improving the *pricing* of tertiary services (for instance, more fully charging for the different costs of courses), and implementing *differentiated* government financial support to students (on the basis of need)."[110] Pricing would create greater incentive and ability for optimal use of the resources involved, as it would "improve the responsiveness of tertiary sector supply to consumer monitoring in terms of teaching performance and the range and nature of services."[111] Treasury claims that private suppliers "crowded out" of the sector by the dominance of government provision and a "restrictive regulatory environment" would also be encouraged to participate in the long term.

The productivity of the public and private investment in tertiary education depends on the ability of students to "make the right choices" and on the incentives tertiary institutions have to meet these demands at the least cost, Treasury says.[112]

> Students can better make choices that are in the wider public interest if they face the real costs and benefits of their decisions. That requires labour markets that are able to provide the right signals about the relative rewards and opportunities for different skills. However, it also requires that the costs students face are more closely aligned to the real costs of providing different types of tertiary education.[113]

This suggests a move to allow fees to vary to reflect different course costs, which vary from $7000 for arts to $25,000 for medicine and $40,000 for dentistry. Differing costs mean there are "enormous" variations in the degree of government subsidy, "yet we know of no evidence to suggest that wider benefits to society are generated by the more expensive courses. Indeed, these social benefits are not readily quantifiable."[114] Treasury says "many studies" estimate there are extensive benefits to the individual, notably in the form of improved earnings potential, and those in the most heavily subsidised courses tend to come from

110 *Economic Management, ibid.*, p. 269.

111 *Ibid.*, p. 269., and *Government Management, op. cit.*, p. 144. Treasury's emphasis.

112 *Briefing 1990, op. cit.*, p. 136.

113 *Ibid.*, p. 137., and *Government Management, op. cit.*, p. 144.

114 *Briefing 1990, ibid.*, p. 137.

wealthier-than-average backgrounds. "To the extent that government funding is not related to social benefits, it is a form of income redistribution, possibly from the relatively poor to the wealthy."[115] Treasury claims that if the state did not intervene, information and financial facilities would develop such that a student could borrow against future expected income.[116] It says the flat-fee regime does not encourage tertiary institutions to reduce costs in high-cost courses, and distorts students' choices in favour of expensive courses. Treasury reduces the course argument to one of simple supply and demand.

> "If the supply side is freed up but the demand side is not then all three-year university courses, for example, will cost much the same to the student and hence students will be attracted to 'commercial' courses away from 'non-commercial ones' and differentials in academic salaries will grow wide. The result: inefficiency, over-response to changes in the labour market (because of no feedback through course costs) and a narrowing of study to areas perceived to be commercial. If on the other hand, the demand side is freed up but the supply side is not, the consequent extreme shortages in the supply of some courses will be resolved by non-price rationing methods or by greatly bidding the price up. The result: inefficiency and inequity. By contrast, if both demand and supply sides are freed up, *those courses offering the best job prospects and other advantages will tend to be bid up slightly in price counterbalanced by a reduction in demand.* Hidden cross-subsidisation between commercial and non-commercial courses will be removed. Differentials in academic salaries will be less than in the first case ... and rates of return for students taking different courses will even up, *particularly when aspects such as personal enjoyment are taken into account.* Hence, efficiency and equity are liable to be improved."[117]

Such a system implies minimal state planning, which Treasury approves because it supports its view that "it seems preferable to permit the provision of tertiary education on a more commercial, contestable basis".[118]

III) Critiquing the market model

Treasury's neo-liberal approach to education means its policy framework is based on the notion of rational, self-interested individuals interacting in the market to educate or be educated, with a limited role for the state in overseeing the exchange and providing full funding for education only up to the secondary-school level. Tertiary education is seen as a commodity that individuals have a vested interest in pursuing as it enables them to obtain the skills necessary to

---

115 *Ibid.*, p. 137.

116 *Government Management, op. cit.*, p. 143.

117 *Ibid.*, pp. 144, 145. My emphasis. Treasury does not elaborate on the term "other advantages".

118 *Ibid.*, p. 145.

acquire a job that pays well or is more satisfying than work they could obtain if they did not have these advanced skills. As with health, however, it is not clear that Treasury's application of the market model will have the predicted outcomes, nor that market outcomes will be what society seeks. Like health, education does not fit the model of an ordinary commodity; its provision and outcomes cannot be judged solely in monetary terms. In adopting the economic model, Treasury has once again ignored that it is dealing with "human beings not cans of beans".[119] The following sections will examine the problems of the neo-liberal approach in three areas: that competition may results in education of uneven quality and education that focuses on vocational skills to the detriment of the broader skills necessary for life in a participatory democracy; that parents and students may make "rational" decisions opposite to those that Treasury expects; and that "freedom of choice" in education of the kind envisaged may create more problems that it resolves.

i) market failure

Treasury's pro-market argument emphasises competition, both among state-funded institutions and between state and private providers. It claims competition would increase efficiency in the use of resources and would make educational institutions more responsive to consumer demands. More private sector involvement would increase the quantity and quality of educational provision, mobilise resources that would not otherwise be available, and free some public resources for use by other children. The quality of education would improve, not only from the increased resources made available by those who wished to pay for the education of their children, but also from the efficiency gains arising from exposing the schools to competitive pressures.[120] Leaving aside for the moment the question of whether education should be responsive to individuals or to some wider community goal, a more problematic question is the way in which Treasury anticipates competition will work to bring about "efficiency" and an improved quality of education. Treasury's use of efficiency implies that educational outcomes will be

---

119 Kominik, *op. cit.*

120 Christopher Colclough, "Who Should Learn to Pay? An Assessment of Neo-liberal Approaches to Education Policy" in Colclough, *op. cit.*, p. 203.

judged in terms of how many students can be educated for a given sum, yet the over-all goal in education is that all students are equipped with the skills both to obtain employment *and* to participate fully in society. The desired outcome is not the cheapest education, but the best.

Competition implies that some students will get a better education and others a poorer one while the market finds an equilibrium where the cost of supply of a particular standard of education is met by demand at that price. But the standard of education demanded by society is not set according to price, but according to outcomes. This raises problems for Treasury's argument that private suppliers have been "crowded out" of the education market by a "restrictive regulatory market", and that the removal of these rules would encourage the private sector to enter the education market with a consequent increase in the quality of education for a cheaper price. The competition argument against such rules is not convincing when the regulations are in place to ensure that all students are taught the same basic skills on which they may build their lives. Without state-imposed rules, private suppliers may not have the incentive to provide education of sufficient quality given that such providers are driven by the need to make a profit, and not an altruistic concern that the student get the best education possible. On this point, it is clear that the application of the competitive market model causes confusion about the motive of the education system. Unlike the market for non-human goods and services, the main aim is not to make a profit for producers, but to ensure that all New Zealanders have the skills to participate fully in society. A student or parent may not discover the poor quality of the education in the short term, because education and training, as Treasury says, "often have long pay-back periods".[121] An inadequate standard may not be obvious until after the student has left formal education.

Treasury's focus on the vocational side of education, that is, its ability to train people to get jobs, appears to suggest that efficiency can be assessed by how many students obtain employment at the end of their formal education. Such an

---

121 *Briefing 1993, op. cit.*, p. 85.

assessment ignores what Amy Gutmann calls "functional literacy", or the attainment of skills and knowledge essential for effective functioning in one's society.[122] Education fixated on producing individuals with employment skills creates a situation in which people can make a living, but not understand the political issues that structure their future choices and the future choices of their society.

> Many high-school students -- those who can understand the help-wanted ads but not the text of news stories; who can fill out checks [sic] but understand nothing about the national economy; who have learned how to mail a letter but not how to think about the social choice between a public and a private post office -- lack the prerequisites for effective political participation. ... By democratic norms, they are functionally illiterate.[123]

Education policy needs to encompass what Treasury proposes -- the concern with the ability of students to get good jobs -- but it also needs to include an emphasis on whether students have the capacity to deliberate about the issues that affect their lives. In this sense, education has an invaluable role in ensuring an effective democracy because it "forms the moral character of citizens", and this, along with laws and institutions, forms the basis of democratic government. Education is both cause and effect -- education shapes the moral character of citizens who form a democratic government, which, in turn, shapes the education of future citizens, which then forms their moral character.[124] J. Roland Pennock provides a useful summation of this argument:

> It is not simply that education enables men [sic] to read and comprehend the news, campaign literature, and the like. ... [E]ducation does much more than provide literacy and train people to comprehend the issues of politics and to be effective political leaders and members of the bureaucracy, although these things are of immeasurable importance. ... [Education] helps to break down traditionalism, and to develop new attitudes and values, such as openness to new experience and willingness to participate in civic affairs.[125]

An "efficient" education system is not, therefore, one that produces students trained only for work, but one that inculcates them with the values and knowledge needed for active participation in their society. The quality of outcomes in such a system cannot be measured in terms that can be incorporated into the market mechanism.

---

122 Amy Gutmann, *Democratic Education* (Princeton, New Jersey: Princeton University Press, 1987), p. 147.

123 *Ibid.*, p. 147.

124 *Ibid.*, p. 49.

125 J. Roland Pennock, *Democratic Political Theory* (Princeton, New Jersey: Princeton University Press, 1979), p. 244.

This raises important issues when examining tertiary education, and its role in society. It is not clear that students will "make the right choices" that are in the "wider public interest" if they are driven purely by price signals and the need to find a job, because the wider public interest cannot be defined merely as "full employment".[126] It may be that society is better served if students and tertiary institutions, especially universities, do not operate with vocational training at the least cost as their main criterion. Gutmann stresses this point, saying that universities are more likely to serve society well "not by adopting the quantified values of the market, but by preserving a realm where the non-quantifiable values of intellectual excellence and integrity, and the supporting of moral principles of non-repression and non-discrimination, flourish".[127] Universities, therefore, have an essential democratic purpose in preserving the tension between social standards and practices, helping citizens contain professional authority within its proper realm. They can serve that purpose, Gutmann says, only if they do not take their cues from the market in an effort to maximise social utility:

> Universities serve democracy best when they try to establish an environment conducive to creating knowledge that is not immediately useful, appreciating ideas that are not presently popular, and rewarding people who are -- and are likely to continue to be -- intellectually but not necessarily economically productive.[128]

Once again, educational outcomes cannot be measured in terms of accepted market mechanisms, which raises questions on whether the supply of education can be left to the market. The focus of Treasury's supply and demand model on courses "offering the best job prospects and other advantages", which are unspecified, does not take into account that the "wider public interest" may be served by students opting for a broader, general education.

This point is particularly relevant to the University of Canterbury, given the criticism of the university's quality assurance procedures in the 1997 audit report. The report's focus on the need for the university to be more "outward looking" in terms of being directly responsive to market and government needs, ignores that one of the functions of a university is to encourage and develop

---

126 *Briefing 1990, op. cit.*, pp. 136, 137.

127 Gutmann, *op. cit.*, p. 183.

128 *Ibid.*, p. 184.

"independent critical thinking and long-term research".[129] In challenging the report's findings, David Novitz says that unless there is an independent source of knowledge and understanding in society, which is what universities are meant to be, then the dissemination of the knowledge and understanding becomes the prerogative of those in power and can be manipulated by them in their own political interests.

> [Universities] are the institutions of learning that are meant to develop a critical understanding of all sorts of problems that affect human beings and their environment, and not just the problems that the market or the government of the day wants to have researched, considered, and taught.[130]

The application of market principles in the education sector may result in education narrowly focused on vocational skills, with a subsequent negative effect on the broader values and skills that citizens need in order to fully participate in society.

ii) rational, self-interested maximisers

The market model may also fail to produce anticipated outcomes because of flaws in its suppositions about how participants will respond to market mechanisms such as price signals. For example, the argument for user charges implies that the increased exposure of the school system to market forces would act to reduce costs because consumers would pressure managers to reduce operating costs or would seek more efficient or cheaper institutions. The argument also assumes that students would work harder because the costs of failing would be higher.[131] However, the truth of these claims "is by no means self-evident".[132] The first implies that the "consumers", that is, the students or parents, are the best judges of efficiency, even though the cheapest education is unlikely to be the best.[133] The second claim also does not follow: students might not work harder, since ability and motivation are not necessarily correlated with ability to pay.

User charges, loan schemes, and private schools and colleges are all seen as ways of inducing the better-off members of the population to pay more for the

---

129 David Novitz, "The deep, fundamental flaws in report on Canterbury University", *The Press* February 5, 1997, p. 11. Novitz is a Reader in Philosophy at the University of Canterbury.

130 *Ibid.*

131 Colclough, *op. cit.*, p. 202.

132 *Ibid.*, p. 202.

133 This argument will be expanded under the section on choice.

educational services their children receive. This expectation rests on assumptions about society's behavioural response to the increase in the price of education. "Specifically, it is assumed that people will choose to pay in sufficient numbers to meet the nation's goals (however defined) and that the changes in the composition of the student population brought about by the change in price would be either positive, or neutral, from the standpoints of equity and quality."[134] However, when examined in terms of the rational, self-interested maximiser, many may choose not to pursue further education. The amount people are prepared to pay towards their education, or that of their children, is calculated by judging the future net earnings associated with that particular level of schooling against the chances of getting a job on completion of the education.[135] On the basis of these calculations, it may be more rational for students and parents to consider alternative, more profitable uses of private funds and student time.[136] Students who are pressured by their parents or economic circumstances to "go out and earn a living" are likely to have less access to higher education than students whose parents are better able or more willing to pay.[137] "It is certain that, under these circumstances, a large number of individuals would change their minds about the wisdom of embarking upon tertiary studies. We should expect such reassessments to be particularly concentrated amongst those in the lower income groups."[138]

The decision by many poorer students and parents not to undertake tertiary education has implications for Treasury's model of supply and demand for courses. Treasury assumes that user charges or price signals will work to even up demand for courses, with those course offering the best job prospects being "bid up slightly in price counter-balanced by a reduction in demand".[139] Once again Treasury

---

134 Colclough, *op. cit.*, p. 203.

135 As previously outlined, Treasury itself postulates that the benefits of tertiary education are a "discretionary investment or consumption" decision because individuals users "capture most of the benefits of higher education in their own higher lifetime earnings or increased utility". *Economic Management, op. cit.*, p. 268.

136 Colclough, *op. cit.*, p. 208.

137 Gutmann, *op. cit.*, p. 222. "As long as less advantaged students are under significantly greater pressure to earn a living rather than continue their education, economic discrimination will be implicit in the institution of higher education."

138 Colclough, *op. cit.*, p. 208.

139 *Government Management, op. cit.*, p. 144.

is equating how much people value something with their ability to pay for it. But it may be that poor students cannot afford to pay, even if they have a strong desire to study in a particular course -- or a natural ability in that area.[140] Treasury argues that student loan schemes resolve this problem, removing some of the risk from the calculation of future returns from the investment in education. Students take out loans to pay for their education, and repay the money only after they start earning above a specified amount. The positive benefits of student loan schemes are that the ability to meet educational costs is no longer a function of household income, and the burden shifts from parents to children, who are the direct beneficiaries of the investment. Loans may also solve the problem of students with "rich but stingy" parents who are unwilling to pay, or pay very much, for their child's education.[141] However, there are also problems with loan schemes, including that the costs of taking out a loan, and therefore its perceived risks, are positive. The poor, being more risk averse, and with higher opportunity costs of participation than the rich, can be expected to use loans the least, which means that even loan schemes have equity costs.[142] Loans do not solve the state's public financing problems in the short term given their long repayment period and other difficulties, as Christopher Colclough explains:

> For example, if loans were typically taken out to cover four years of study, with a 20-year pay-back period, the government would not recover even 50 per cent of the initial generation of student loans until 14 years after the start of the scheme. This calculation ignores any continued subsidy elements in higher education provision, default rates, unemployment of loan recipients, non-participation in the labour market owing to family responsibilities, and the costs of collection of loan repayments. This list may often amount to a substantial proportion of potential revenue.[143]

In New Zealand, more than 220,000 students have borrowed money from the state for their tertiary education since the loan scheme began. They now collectively owe the state $1.6 billion, with the debt expected to climb progressively to $19 billion by

---

140 For example, a poor student may have a strong desire to be a dentist, but the course costs of $18,000-$20,000 a year may be beyond their means. Although they place a high "value" on dentistry as a career, they cannot express this in monetary terms because they do not have the ability to pay. In 1995, 163 students turned down a place on the University of Otago's highly competitive dentistry course, citing costs as the major factor. Cate Brett, "Generation Debt: Our Students' $1.8 Billion Burden", *North and South*, February 1997, p. 39.

141 Gutmann, *op. cit.*, p. 225.

142 Colclough, *op. cit.*, p. 209.

143 *Ibid.*, p. 210.

2024.[144] However, the outstanding students loans are shown in the government's accounts as an asset rather than a liability.[145]

iii) maximising choice

As with health, the issue of choice in education can be approached at both individual and state levels. Treasury claims that increased competition stops parents and individuals from being "rationally ignorant" by allowing them better information and therefore greater choice, but it does not explain the mechanism by which this is achieved. It may be that schools are expected to advertise or display examination statistics or accounts, on which parents and students can base their decisions. But the measurement problems outlined in the section on market failure apply equally here. Neither parents nor students are qualified to judge in the short term what constitutes "good" education. Advertising, as previously discussed, is not an impartial and unbiased source of information; the school with the most impressive advertisement may not be the best. Price is not a useful measure because the school that has the lowest costs may not offer a good education.[146] Examination results are also problematic given the varying talents and abilities of students; a simple pass or fail mechanism may not be an adequate assessment of a student's over-all achievements. Measuring performance by examination results may also lead to schools teaching to produce good test results, thereby neglecting in-depth or longer-term learning for exam-passing skills. "Freedom of choice" in education may cause more problems than it resolves.

Treasury's model also assumes that all parents will be equally interested in their child's education. It is not clear what happens to the children of those who are either too busy to pay much attention or who do not care. Zoning may restrict choice, but given the limited space in each school the only other option available for schools is to select by price or competitive entry competition. A school that takes the best students will, of course, achieve better results and parental

---

144 Lisa Webber, "Student debt soars to $1.6b", *Christchurch Star* February 14, 1997, p. 1.

145 McLouglin, *op. cit.*, p. 50.

146 On the other hand, the school with the best advertisement or the lowest costs might offer a good education, but how is the parent or student to judge?

pressure on the other schools will not be able to challenge this, especially if, under the "bulk funding" of teacher salaries and extra contributions from parents, a school is able to pay wages above the national scale (and thus may be able to employ better qualified teachers) and to purchase other educational aids. This creates a "chicken and egg" situation:

> Selection by entrance examination is likely to improve the school's future public examination results as it admitted more and more pupils with the ability to pass examinations. A reputation of achievement in public examinations would be all the more likely if selection by entrance exam were combined with selection by ability of parents to pay top-up fees, because it would help the school to provide those things that money can buy.[147]

Even if schools could be "pressured to change", such changes cannot occur in the short term, and Treasury does not say what happens to those students caught in the "less efficient" schools in the meantime. If pressure to change is judged, as Treasury says, by a decline in rolls and, therefore, a subsequent fall in resources, then the demand for change comes at a time when the school is least able -- through a lack of resources -- to respond to parents' demands. Disadvantaged schools may not be able to afford to hire as many teachers as the "more efficient" schools, and might have to rely on inadequately trained or less well qualified teachers, and on those teachers unable to get jobs in schools paying higher salaries.[148] "It is not difficult to predict that a free market for education will produce a range of schools closely related to the socio-economic status of their pupil intake, with 'sink' schools at one end of the range and expensive, well-provided ones at the other."[149]

---

147 Jack Demaine, "The Reform of Secondary Education", in Barry Hindess, ed., *Reactions to the Right* (London: Routledge, 1990), p. 85. An exemplary example of this is Christchurch Girls' High School, where intense competition for entry is resolved by an entrance examination and an interview with both the prospective student *and* her parents. The process results in places being offered to the girls with the most talent, and the most articulate parents, which brings good results for the school, which increases demand for places and so on.

148 This creates a difficulty for Treasury's argument that schools that "did not change might eventually be taken over by better personnel moving from the successful schools". *Briefing 1990, op. cit.*, p. 135. Treasury does not explain why the "better personnel" would want to move, especially if the "less popular" school did not have the resources to pay what these personnel would receive at the "more responsive" schools.

149 Demaine, *op. cit.*, p. 86. Demaine says that "if educational research over the last forty years has shown anything at all, it is that there is a relationship between the socio-economic status of children constituting the intake of the individual school and its aggregate performance in terms of public examination results". p. 84. Treasury acknowledges this in its 1993 briefing, saying that children in situations of disadvantage -- poor health, poor housing, low income, and low skills and education -- are, without some assistance, less likely to benefit from growth. "Growing up in such conditions tends to constrain the choices and opportunities available to children. In particular, there appears to be a link between disadvantage in childhood and subsequent unemployment." *Briefing 1993, op. cit.*, p. 14.

Some state involvement may, in fact, be necessary in education. While Treasury argues that its policy prescriptions would increase choice for parents and students and make education more responsive to consumer demands, it is questionable whether all decisions about what could or should be provided by education can be made by individuals. Notwithstanding the problems parents have with judging the quality of education before it is too late to make changes to benefit their own children, a major difficulty is that if parents have control over what their children learn, the children may be denied choice or exposure to diverse thoughts. The question is whether parents should be able to control what children learn if their views are narrowly confined to say, religious or culturally based education. A state committed to freedom from coercion for adults in their personal and political lives may prefer to show the same commitment to children by ensuring their education makes freedom possible and meaningful in the future.[150] Gutmann succinctly makes this point:

> A state makes choice possible by teaching its future citizens respect for opposing points of view and ways of life. It makes choice meaningful by equipping children with the intellectual skills necessary to evaluate ways of life different from that of their parents.[151]

Market mechanisms that respond to parental pressure may eliminate the very outcomes Treasury supposes them to make possible by limiting the freedom and choice of students to make future decisions unaffected by the biases of their parents.

IV) Summary

As with health, Treasury's neo-liberal framework for education is based on flawed assumptions about the results of competition and the way that people act in the education "market". Treasury fails to prove that the "difficulties" of its four main reasons for state intervention would be adequately resolved by taking a more-market approach. On equity, a policy of minimum state intervention in education may create more inequity, despite Treasury's claim to the contrary. On agency issues, parents will not necessarily become more responsible for the education of their children if the state is not involved, nor is it guaranteed that they will make the "rational" decisions that Treasury expects. On interdependence, Treasury's

---

150 Gutmann, *op. cit.*, p. 30.

151 *Ibid.*, p. 30.

assumption that the individual captures all the benefits of education neglects its claim that New Zealand's economic growth benefits when its citizens are "well educated and trained". It also overlooks that New Zealand's progressive tax system means that those who earn more, pay more. On efficiency, Treasury ignores that the difficulties that parents and students face in measuring the quality of education cannot be overcome by equating good education with the cheapest education. Accountability may be more problematic in the market because private providers are driven by the profit motive, not a desire to provide the "best" education. The human factor makes it difficult for Treasury to ethically argue in education that "markets at their best resolve conflicts impersonally and ensure that over the longer term, less efficient producers are penalised and the more efficient rewarded".[152] The "product" in this market is a student's education and "less efficient" producers can have a profound effect on the rest of a student's life. Education is not a "commodity" that responds to competition and choice when the very notion of competition implies that some win and some lose. The aim of education in society is to give all students an education that will enable them to take advantage of opportunities for better lives, but this cannot be guaranteed if a student is consigned to a "losing" or "less efficient" school in a competitive marketplace. Treasury's neo-liberal policy framework for education is unlikely to result in the desired outcome of a quality education for all. Again, as with health, there is a clear role for the state if the market cannot be depended on to ensure the provision of quality education.

Conclusion

In advocating a neo-liberal approach to social policy areas, including health and education, Treasury claims it is responding to growing disquiet over the ability of the welfare state to achieve the goals of New Zealanders. Commenting in *Government Management* (1987) on increasing unemployment, family break-up and crime, it says: "Obviously all is not well with our society. Life is fine for many, but that does not mean that we have a social order which can be sustained with general acceptance by everyone."[153] Part of the problem, it claims, is that there are

---

152 *Government Management, op. cit.*, p. 15.

153 *Ibid.*, p. 397.

"fundamental problems in the social institutions and policies that have been set up to promote a good society", and the "generalised belief that the welfare state is a robust and successful concept is now increasingly questioned".[154] For example, the health system is "showing signs of stress" with more than one million New Zealanders holding private health insurance policies, and education is frequently cited in opinion polls as one of the major problems facing society. Treasury suggests there is a need to recognise the limitations of the state. While the state has a role to play in maintaining an adequate minimum level of well-being for all and promoting the best over-all level of well-being for everyone, this "does not mean that the state is always *(or ever)* the best institution to achieve social aims, or even that the state is capable of success in such areas".[155] Treasury argues that social well-being is essentially a private matter: individuals each have their own, subjective notions of well-being and are in a better position than the state to work to achieve these goals. It therefore argues that the best way for the state to achieve the "fair and thriving society" to which New Zealanders "clearly aspire" is to look to the mechanisms of the market. The state's role should be limited to strengthening and supplementing the market, and individuals should be left free to follow their own preferences.

However, an application of Treasury's pro-market model to health and education reveals that the weaknesses of the underlying assumptions, outlined in chapter three, may result in outcomes that are the opposite of what is anticipated. Despite what Treasury claims, health and education are not typical commodities; their "efficient" production cannot be assessed solely in terms of money. Efficiency judged in terms of the number of people treated or educated for a given financial outlay does not take into account the quality of life patients are left with or how well prepared students are to function in society. The market may fail in both these areas because producers (providers) in a competitive market are concerned more with profit than the provision of quality health and education, where "quality" includes intangible factors such as human emotions and abilities. In a competitive market where service providers are driven by the profit motive, they may be tempted to

---

154 *Ibid.*, p. 397.

155 *Ibid.*, p. 400. My emphasis.

reduce quality in order to lower the cost. The consequences of this can be severe: patients may suffer pain, anguish or even death, while students may be left with a diminished ability to take advantage of life's opportunities. When "inefficient" producers in the health and education "markets" are punished, patients and students also bear the consequences.

The rational, self-interested behaviour assumptions of the market model are also problematic. "Rational" responses to price signals such as user-pays may reduce "consumer" participation in the short term and result in increased costs to the state and society in the longer-term. For example, patients who are not treated early may require higher-cost treatment if their illness becomes more serious, and students who choose not to pursue further education may not attain the skills necessary to obtain work. The specialised nature of these areas means patients and students do not have the knowledge necessary to make informed choices. While they know their interests -- obtaining quality health care or education -- they may not how best to pursue them. For example, in health people do not know whether a particular medicine is effective or safe and must take advice on trust from medical experts; in education, parents do not know the best methods by which children learn to read and must rely on teachers.[156] Both patients and students must be confident that the service they are getting is based on decisions as to quality as well as cost.

Treasury's arguments for an increased use of the market in health and education are inadequate because they fail to acknowledge that health and education are not "preferences" but "needs", without which citizens are unable to fully participate in either public or private life. An adequate income is needed to provide the food, shelter, health, education and so on that are essential to social well-being, but without well-being, individuals are unlikely to obtain the jobs that give them the income to purchase their needs. Research by Harvard Medical School assistant professor Ichiro Kawachi shows a strong correlation between low income, ill-health and low educational achievement.

---

[156] Richard Mulgan, *Democracy and Power in New Zealand* (Auckland: Oxford University Press, second edition, 1989), p. 172.

> If you don't educate disadvantaged people so they can have a meaningful role in society, you will soon be faced with spiralling health, unemployment and crime problems -- all of which will become an increasing drain on society, on the middle classes with jobs that are still paying taxes. Children of the unemployed will become a self-perpetuating underclass.[157]

Treasury acknowledged this problem itself in 1993, saying that children in situations of disadvantage will have particular difficulties.

> Growing up in such conditions [poor health, poor housing, low income, and low skills and education] tends to constrain the choices and opportunities available to children. In particular, there appears to be a link between disadvantage in childhood and subsequent unemployment.[158]

In order to resolve these problems, rather than limiting the state's role as Treasury suggests, a role for the state can be justified so that people have what they need to take care of themselves. The state may need to provide both health care and education because the market cannot be trusted to ensure their supply in adequate quality and quantity to all.

New Zealanders are clearly concerned about health and education, but the fact that they have registered dissatisfaction with the performance of the health and education sectors does not necessarily mean that they believe the state should not be involved in provision in these areas. In fact, the protests over many of the reforms of the past 12 years, such as the closing of "inefficient" rural hospitals and the introduction of tertiary fees, suggest the opposite. It could be argued that a reason why health and education were issues of primary concern in the 1996 election was that New Zealanders believe that these areas are public goods that the state must ensure are adequately supplied to all citizens. New Zealanders have become accustomed to state supply of "a comprehensive range of social services characterised by underlying notions of egalitarianism, humanitarianism, and a conviction that the state has a responsibility for the health, education and welfare of its citizens".[159] Health and education involve more than just money; they are concerned with intangible, hard-to-quantify factors such as quality of life and future opportunities. The neo-liberal approach does not take into account that society may value health

---

157 Quoted in John Saunders, "The nation with a heart of stone", *Evening Standard* February 8, 1997, p. 12.

158 *Briefing 1993, op. cit.*, p. 14.

159 Task Force on Economic and Social Planning, *New Zealand at the Turning Point* (Wellington: Government Printer, 1976), p. 97.

and education in ways that cannot be reduced to money; they are public goods, and it is in the interests of a better community to have a healthy, well-educated population. Society may therefore have decided to place monetary concerns second to the attainment of these collective goals. Neo-liberals focus on freedom of choice, but this may be of little use if the members of society lack the health and "functional literacy" to assess their choices and participate. The consequences for both individual citizens and society of the inadequate provision of health and education make them political, not market, issues. Questions of how much should be spent, on what and on whom are decisions that must be made by society, not the market.

CHAPTER FIVE

Neo-liberalism and the political community

Introduction

In its briefing papers, Treasury argued from a neo-liberal perspective for policies that limited the role of the state to setting and enforcing rules to allow "free and voluntary" exchange in the market, and shifted into the market or private sector a wide range of decisions previously seen as the realm of the public sector and politicians. Treasury portrayed its recommended policy framework in terms of it being a result of a comparison between the market and the state, claiming this approach was scientific, value-free and neutral, and that the resulting policy plan was the only way for New Zealand to resolve its economic crisis. The catch-phrase of economic policy at this time was: "There is no alternative." The previous two chapters examined this "scientific" claim and discussed the weaknesses of the underlying assumptions, showing the unanticipated outcomes if such policy prescriptions were adopted. This chapter will conclude the thesis by elaborating on the discussion of neo-liberalism and what happens to the political community as the state's involvement in the economy and the provision of opportunities is reduced and the market is extended to cover more and more areas of life. The neo-liberal political framework is likely to change the underlying political culture of New Zealand society and undermine its democratic values.

Treasury's view of market achievements

Earlier chapters detailed Treasury's arguments in favour of the market and its claim that state had caused the economic crisis, burdening the economy with interventions -- rules, regulations, taxes and spending -- that stifled entrepreneurship and decreased the incentives for individuals to use their initiative and take advantage of opportunities available to them. As outlined, Treasury claims a comparative assessment of the state against the market shows that in overcoming constraints on securing an ideal society, the state is subject to the same pitfalls that face private solutions plus other ones, which means that, in effect, it can never produce more efficient outcomes than the market. The solution, therefore, lies in limiting the state's role to setting and enforcing rules of the free market, in which individuals enter into voluntary contracts to obtain the things they need and want. Treasury says there are few areas where the market fails to produce "socially appropriate" outcomes on efficiency as well as equity grounds, and these are mainly confined to goods and services that are of a public nature such as law and order, defence, and street lighting.[1] It claims that even with these goods, however, a case can be made for market-based intervention rather than strict regulation. Efficiently functioning markets maximise opportunities for welfare gains because markets force individuals to make choices about the priorities they have, reconcile the demands of individuals with those of others, and give incentives for individuals to use resources wisely. The results are two-fold: economic growth and individual liberty.

Treasury says growth, which comes from a well-functioning economy, is the only way to resolve New Zealand's economic crisis. Growth contributes to improved well-being for all New Zealanders; it creates jobs, raises the level of income, reduces the number of people dependent on the state, and reduces the level of fiscal expenditure and debt. It yields higher incomes, which enables consumption of more goods and services, greater scope for quality public services, and wider opportunities for people, including the unemployed, to participate more fully in society.[2] Treasury's recommended methods to achieve growth focus on limiting the role of the state and maximising the autonomy of the individual within the market. In this way it hopes to achieve both the efficient use of resources and increased self-reliance and self-responsibility, which will decrease what it sees as ~~a~~ the debilitating burden on the state. Treasury says the market is a non-coèrcive mechanism that allows "free and voluntary" exchange between individuals, which maximises individual autonomy and initiative, whereas state intervention is coercive and interferes with the capacity of individuals to achieve their objectives. The

1 New Zealand Treasury, *Economic Management* (Wellington: Government Printing Office, 1984), p. 297.

2 New Zealand Treasury, *Briefing to the Incoming Government 1993* (Wellington: GP Print Ltd, 1993), p. 48.

market is therefore lauded for its ability to enhance individual liberty, and for being the most efficient and democratic method for transmitting and satisfying individual needs and wants.

Changing state-society relations

According to the neo-liberal philosophy to which Treasury apparently subscribes, the state should intervene in society only to enforce rules protecting "life, liberty, and estate", a limitation that changes the way New Zealanders have traditionally viewed the state and its role.[3] Since the first Labour government of 1935 to 1949, the New Zealand state has had a strong interventionist role in promoting the ability of its citizens to achieve the good life.[4] Policies have combined the principles of individual liberty with principles of collective self-government and egalitarianism, balancing liberty, property, and individualism on one hand, and equality, justice, and self-government on the other.[5] The state aimed to provide good quality public services for all, and levels of aid and income support for those unable to meet their needs were intended to be sufficient to allow participation in society, not simply survival.[6] In reducing the role of the state and limiting what it will provide, Treasury is shifting the balance between principles, emphasising self-reliance and individual responsibility, with individuals providing for the bulk of their needs through the market, their family, or voluntary agencies and charities.[7] State assistance is still available for those unable to meet their basic needs through their own efforts, but it is kept low and "rigorously" means-tested to ensure it does not go to those with incomes or assets above a certain level. "The level of assistance available to those who meet the requirements of the relevant means test is kept to an absolute minimum on the

---

3 David Held, "The Contemporary Polarization of Democratic Theory: the Case for a Third Way", in *Political Theory and the Modern State* (Cambridge: Polity Press, 1989), p. 175.

4 In this context, the good life refers to having those basic needs that allow individuals to pursue a life of quality and value. Ronald Dworkin says a "valuable [life] has to do with how it is lived, the excellences it manifests in responding to the challenges it faces". Ronald Dworkin, "Foundations of Liberal Equality", in Stephen Darwall, ed., *Equal Freedom* (Ann Arbor: University of Michigan Press, 1995), esp. pp. 244-258. This concept will be discussed in later sections of this chapter.

5 Benjamin R. Barber, "Liberal Democracy and the Costs of Consent" in Nancy L. Rosenblum, ed., *Liberalism and the Moral Life* (Cambridge, Massachusetts: Harvard University Press, 1991), p. 55.

6 Jonathan Boston, "Redesigning New Zealand's Welfare State", in *The Decent Society?* (Auckland: Oxford University Press, 1992), p. 4.

7 *Ibid.*, p. 3.

justification of curbing public expenditure and deterring dependence on state handouts."[8]

The relationship between the state and its citizens has shifted from one in which the state helps its citizens to participate fully in life to one where such aid is regarded as creating dependence and a drag on the state and other citizens. Treasury justifies this reduction in the state's role on the grounds that it will help create the conditions for growth by breaking the "vicious cycle" impeding the economy.

> The taxes required to pay for social services create a drag on the economy's ability to create jobs. The resulting unemployment adds further to tax burdens, creating a further drag on the economy. The challenge of reformed economic and social policies is to reverse this into a 'virtuous circle'. As more people are encouraged into jobs, they would reduce the need for welfare payments and would add to tax revenue. This can create a positive impetus which gains momentum over time. Combined with better results from health spending and improved education, the groundwork can be laid for economic growth.[9]

Treasury casts social services, not as a means of ensuring that all citizens have adequate resources to belong and participate in the community, but as an infringement on the liberty of other members of society. "Every time the state provides a social service it must do so by deploying resources which have been taken under coercion from members of society. Taxation implies a compulsory removal of income from those who have worked to earn it."[10] Such a shift in balance between principles governing state action has important implications for the values underlying relationships within society.

Neo-liberalism and collective interests

In shifting the focus to individuals, Treasury is committing itself to the neo-liberal doctrine that the collective good, or the good of all individuals, can be obtained only by individuals acting in competitive isolation and pursuing their aims with minimal state interference.[11] As outlined in chapter three, this is based on the

---

8 *Ibid.*, p. 3.

9 New Zealand Treasury, *Briefing to the Incoming Government 1990* (Wellington: GP Print Ltd, 1990), p. 95.

10 New Zealand Treasury, *Government Management* (Wellington: Government Printing Office, 1987), p. 404.

11 Held, *op. cit.*, p. 175.

notion of individuals being rational actors, and the best judge of their own interests (that is, their own notions of the good), which are subjective and specific to each individual. If left free from interference, individuals will choose according to those interests. Society's over-all well-being, or the collective interest, cannot be organised collectively by the state because it simply accrues from individuals following their own self-interested paths. Neo-liberals claim the free market is the only sufficiently sensitive mechanism for determining "collective" choice on an individual basis and, when it is protected by a constitutional state, the market is more "dynamic, innovative and responsive" than any other system.[12] Voluntary contracting in the free market is presented as superior to the decisions of even the liberal democratic state in achieving individual wants and needs because it allows each individual to exercise choice and initiative in a "daily referendum".[13]

Friedrich von Hayek, one of the leading advocates of this idea, admits -- as does Treasury -- that the free market does not always operate perfectly, but insists its benefits "radically" outweigh its disadvantages. The market ensures the co-ordination of the decisions of producers and consumers without the direction of a central authority; it allows the pursuit by everybody of their own ends with the resources at their disposal; and it allows the development of a complex economy without an elite which claims to know how it all works. "Politics, as a governmental decision-making system, will always be a radically imperfect system of choice when compared to the market. Thus 'politics' or 'state action' should be kept to a minimum."[14] Neo-liberalism thus reduces individuals to rational, self-interested beings driven by monetary incentives and looking only to enhance their own interests. The state is removed from notions of collective good or collective interest because, neo-liberals claim, collective interest is simply an agglomeration of individual notions of the good.

---

12 David Held, *Models of Democracy* (Cambridge: Polity Press, 1996), p. 260. Held is discussing in particular the views of F. A. Hayek.

13 David Green, *From Welfare State to Civil Society* (Wellington: New Zealand Business Roundtable, 1996), p. 35.

14 F. A. Hayek, *The Road to Serfdom* (London: Routledge and Kegan Paul, 1976), p.172.

While an immediate and obvious problem with this view is that a democratically elected state is the result of citizens exercising their choice in a referendum, and therefore its actions could be expected to represent their wants and needs, a more fundamental issue is that visions of the good "cannot be pursued, or even known, by solitary individuals".[15] As argued in chapter three, individuals do not regard themselves simply as solitary, utility-maximising individuals, but as members of collective bodies, including families and communities. Individual are "embedded" or "situated" in existing social practices, therefore notions of the good cannot be formed outside the community of which the individual is a member. This argument reflects the Aristotelian perspective discussed by Taylor that "an essential constitutive condition of seeking the human good is bound up with being in society ... what man derives from society is not some aid in realising his good, but the very possibility of being an agent seeking that good".[16]

> ... [A]n individual is constituted by the language and culture which can only be maintained and renewed in the communities he is part of. The community is not simply an aggregation of individuals; nor is there simply a causal interaction between the two. The community is also constitutive of the individual, in the sense that the self-interpretations which define him are drawn from the interchange which the community carries on.[17]

Individual judgments of the good require the sharing of experiences, and the give and take of collective deliberation. As such, they depend on the collective evaluation of shared practices or they become a matter of subjective and arbitrary whim.[18] The state is, therefore, the "proper arena" in which to formulate visions of the good, because the visions require shared inquiry.[19] The collective good is not the combining of individual preferences, but is a conception that defines the community's

---

15 Will Kymlicka, *Contemporary Political Philosophy* (Oxford: Clarendon Press, 1990), p. 220.

16 Charles Taylor, *Philosophy and the Human Sciences: Philosophical Papers 2* (Cambridge: Cambridge University Press, 1985), p. 292.

17 *Ibid.*, p. 8.

18 Kymlicka, *op. cit.*, p. 220. Kymlicka is outlining the communitarian position.

19 W. Sullivan, *Reconstructing Public Philosophy* (Berkeley, California: University of California Press, 1982), pp. 158, 173., quoted in Kymlicka, *ibid.*, p. 220: "Self-fulfilment and even the working out of personal identity and a sense of orientation in the world depend upon a communal enterprise. The shared process is the civic life, and its root is involvement with others: other generations, other sorts of persons whose differences are significant because they contribute to the whole upon which our particular sense of self depends. Thus mutual interdependency is the foundational notion of citizenship ... Outside a linguistic community of shared practices, there would be biological *homo sapiens* as logical abstraction, but there could not be human beings. This is the meaning of the Greek and medieval dictum that the political community is ontologically *prior* to the individual. The polis is, literally, that which makes man, as human being, possible."

way of life. "This common good, rather than adjusting itself to the pattern of people's preferences, provides a standard by which those preferences are evaluated."[20]

Collective notions of the good may also require shared action to achieve them, in that supporting forms of life the community sees as valuable is a social rather than an individual matter. New Zealanders have traditionally seen voting in this way, turning out in high numbers every three years to cast their vote, although -- as individuals -- their vote may make little difference.[21] They do so because they realise the value of living in a participatory democracy. Collective interests can help to engender community values because "when people engage in political discussion and action with their fellow citizens they not only become more aware of their own needs, but they also come to recognise the interests they share with each other; they thus become, generally, more community-minded."[22] It can also be argued that the use of the notion of individuals as the "best judge" of their interests does not actually preclude notions of collective interest.[23] Some questions cannot be resolved by individuals judging in isolation, and there must be some collective determination and collective embodiment of the conclusions. In such cases, "[j]ust as individuals are the best/only judges of their individual interests, so too are collectivities the best/only judges of their collective interests."[24] Individuals cannot act alone, completely independently of others, because in many areas what affects one will also affect others. "Where there are matters which concern several people, a collective decision will be needed which is binding on all members of the group."[25] For example, collective decisions are needed for the management of

[20] Kymlicka, *ibid.,* p. 206.

[21] Geoffrey Brennan discusses how the standard "homo economicus" model does not work in political contexts, saying that if voters were rational egoists, it seems unlikely that turn-out would be as large in electorates as it is. The probability that a single vote will prove decisive becomes quite small as the voting population increases, so the expected return to voting remains negligible. Also, many voters vote in "a manner they think best for the community as a whole. Few appear motivated predominantly by self-interest, even where there are issues that might affect that interest significantly." Geoffrey Brennan, "Politics *with* Romance: Towards a Theory of Democratic Socialism", in Alan Hamlin and Philip Pettit, eds., *The Good Polity: Normative Analysis of the State* (Oxford: Basil Blackwell, 1989), pp. 57, 58.

[22] Richard Mulgan, *Democracy and Power in New Zealand* (Auckland: Oxford University Press, Second Edition, 1989), p. 169.

[23] Robert E. Goodin, "Liberalism and the Best-Judge Principle", *Political Studies* vol. 38 (1990), pp. 181-195.

[24] *Ibid.*, p. 193.

natural resources because of the impact their use may have on others. A farmer who dams a river to provide irrigation may reduce the water available for others downstream; similarly, too many tourist operators in areas of natural beauty may destroy the resources from which they make a living.

Individual liberty as a primary goal

Neo-liberalism promotes liberty as the key to economic and political life, without which "democracy will have ceased to exist".[26] The basic premise of neo-liberal liberty is that individuals are free from state restraint or interference to pursue their own affairs as long as they do not interfere with the freedom of other individuals to do likewise.[27] In other words, individuals have the freedom to determine their own lives; if someone controls their lives, and makes decisions for them, then they have been deprived of an essential aspect of their humanity.[28] Liberty means a lack of restrictions of individual conduct such that the individual acts with a feeling of freedom and in the absence of coercion: "The individual should be free, other things being equal, to make his own decisions, determine his own actions, seek the satisfaction of his own wants and desires, pursue his own ideals and respond to his own moral imperatives."[29] Such a view rests on the idea that each individual has his or her own notion of the good life, and should have the freedom to pursue it. It is not a good life if society penalises or discriminates against projects individuals feel are the most valuable to them.[30] The functions of the state are therefore limited to setting the rules that govern relationships, preserving law and order and enforcing private contracts.[31]

---

[25] Mulgan, *op. cit.*, p. 165.

[26] J. Roland Pennock, *Democratic Political Theory* (Princeton, New Jersey: Princeton University Press, 1979), p. 240.

[27] Paul Wilding and Vic George, "Social Values and Social Policy", *Journal of Social Policy* vol. 4 no. 4 (1975), p. 374.

[28] Mulgan, *op. cit.*, p. 164.

[29] Pennock, *op. cit.*, p. 85. The notion of liberty is thus linked to a strong notion of individualism in which individuals left free from state restraints will make their own way in the world, independent of outside support. Individuals are thus self-reliant and self-responsible.

[30] Kymlicka, *op. cit.*, pp. 199-205.

[31] The role of the state is thus to "mediate differences among us on the meaning of the rules and to enforce compliance with the rules on the part of those few who would otherwise not play the game". Milton Friedman, *Capitalism and Freedom* (Chicago: Chicago University Press, 1962), p. 12., quoted in Wilding and George, *op. cit.*, p. 374.

By shifting all aspects of life into the private sector and restricting the liberty-inhibiting impact of the state, Treasury claims it is reinforcing the individual liberty of New Zealanders, which it equates with them having maximum freedom of choice. Treasury's focus on this can be seen in its social policy framework, according to which it says the state needs to consider the extent to which proposed policies undermine self-reliance and "reduce the capacity of individuals to make decisions that improve their own earnings potential and health and education status".[32] Thus in health and education, Treasury's goal is not only cost control and efficient use of resources, but the return of choice to the individual. Patients become responsible for choosing between health care alternatives and parents and students become responsible for choosing options for education on the basis that individuals have their own notions of well-being and should be free to follow their preferences. The maximisation of choice leads Treasury to claim that:

> [w]hen the government assumes responsibility for individuals' decisions, an inevitable consequence is the reduction of freedom for individuals to make their own choices -- in fact, society is indicating that it knows better what is good for at least some of its members than they do themselves.[33]

Such a statement attacks notions of collective interest on the grounds that it interferes with an individual's right to be free from coercion of others. On this point, Treasury attacks as coercive the tax needed to pay for social policy, as raised in the earlier section on changing state-society relations.[34] Treasury says tax reduces individual liberty because it involves the compulsory removal of income from those who have worked to earn it, and affects the utility individuals can derive from their employment because it reduces the amount of their own money they can spend on what they want.

> Provided the taxes are spent efficiently on services that are of value to the [individual] then this tax burden is balanced by the social wage. However, given the lack of direct control over publicly provided goods, it is likely that for many [individuals] the value of such goods may be lower than the amount of taxes given up to pay for them.[35]

---

32 *Briefing 1990, op. cit.*, p. 97.

33 *Economic Management, op. cit.*, p. 253.

34 "Every time the state provides a social service it must do so by deploying resources which have been taken under coercion from members of society. Taxation implies a compulsory removal of income from those who have worked to earn it." *Government Management, op. cit.*, p. 404.

35 *Ibid.*, pp. 404, 122.

However, it can be argued that individuals retain their autonomy within collective decisions because the principle of self-determination is not eliminated and each member has a share in making the decision.[36] Richard Mulgan says that if everyone is allowed an equal say in the making of decisions that affect them, they are still free in the sense that they share in the control of their own lives. While the decisions may not always be what they prefer, if individuals have shared in the process of making the decisions then they have not been imposed on them from without. In this way, some freedom is preserved for each individual within a collective as long as each individual is allowed an equal say in collective decision-making. "People may not have as much control over their lives as they would if they were entirely independent of one another, but they certainly have more than if they had no say in making the decisions which affect them.[37]

Treasury's neo-liberal view confines liberty to a narrow notion of freedom from coercion, or the imposition of another's view of the good, rather than a broader notion of the liberty of actually being able to follow one's choice of action, that is, having the capacities and resources to do so. Treasury gives people the freedom to *choose* their goals, without giving them the freedom to *achieve* them. Such a limited notion conflicts with the understanding New Zealanders have had since the welfare moves of the first Labour government in the 1930s, where "to enjoy liberty means not only to enjoy equality before the law ... but also to have the capacities (the material and cultural resources) to be able to pursue different courses of action".[38] New Zealand's Social Development Council, responsible for promoting a high quality of life by focusing attention on social aspects of development, made this point in 1976, saying important aims of social development via social policy were to enhance the dignity, freedom and independence of individuals by ensuring that, among other things, "each person has the maximum freedom of choice and action without encroaching upon the rights of others".[39] It also said there was a need

---

36 Mulgan, *op. cit.*, p. 165.

37 *Ibid.*, p. 165.

38 Held, *Models of Democracy, op. cit.*, p. 263.

39 Task Force on Economic and Social Planning, *New Zealand at the Turning Point* (Wellington: Government Printer, 1976) p. 393.

to share resources fairly by ensuring each person has, among other things, "the opportunity of a *material* standard of living at a level which enables him or her to enjoy a sense of belonging to and participating in the community".[40] In other words, people have to have their needs met in order to pursue their preferences.[41] Assessments of liberty must therefore be made on the basis of liberties that are tangible, or as J. K. Galbraith says:

> There is, first, the absolute, inescapable requirement that everyone in the good ... society has a basic source of income. And if this is not available from the market system ... it must come from the state. Nothing, let us not forget, sets a stronger limit on the liberty of the citizen than a total absence of money.[42]

Collective interest and social justice

A more extensive understanding of liberty may result in a society recognising a commitment to social justice, understood as a redistribution of benefits and burdens throughout society to achieve an allocation of capacities allowing all of its members to pursue tangible outcomes. This means giving people the means to obtain their basic needs -- commodities such as basic food and drinking water, accommodation, primary medical care and education and sanitation facilities, or the "goods that are the means of being able to function, prerequisites of the individual's ability to pursue his conception of the good."[43] The Social Development Council discussed this point, saying it recognised that people are not, and can never be, equal in all respects, but society needs to ensure that each person has a maximum opportunity to achieve self fulfilment: "... the ensuring of maximum opportunity is a goal to which a majority of New Zealanders subscribe."[44] However, Treasury's focus on liberty as freedom from coercion allows it to negate notions of distributive or social justice, which is condemned as imposing on some, another's conception of merit or desert. In this it follows Hayek, who says that social or distributive justice

---

40 *Ibid.*, pp. 393, 394. My emphasis.

41 The difference between needs and preferences was raised in chapter four. Treasury turns all needs into preferences by arguing that they as individuals have their own notions of well-being, all needs are subjective in that they are particular to each individual. The state is therefore less able to attend to these needs than the individual concerned. However, it is hard to see how basic needs, which will be discussed in the next section, can be "subjective" given their role in physical survival.

42 J. K. Galbraith, "The good society", *The Guardian* January 26, 1994, p. 2., quoted in Held, *Models of Democracy, op. cit.*, p. 319.

43 Partha Dasgupta, "Power and Control in the Good Polity", in Hamlin and Pettit, *op. cit.* p. 181.

44 Task Force on Economic and Social Planning, *op. cit.*, p. 392.

requires an allocation of resources by a central authority acting as if it knew what people should receive for their efforts and how they should behave, rather than their being rewarded "according to the value that their services have for their fellows".[45] The argument here is that the value of individuals' services can, however, only justly be determined by their fellows in and through a free market, where there is no interference with the knowledge, choices and decisions of the individuals.[46] If each individual is treated equally, then the state cannot intervene to redistribute unequal outcomes without coercion.[47] Treasury says "[e]xcessive attempts to impose of predetermined concept of justice" are not only coercive, they may suppress economic activity and create disincentives to private and voluntary actions that could promote social well-being.[48]

A difficulty with this claim however, as outlined above, is that individuals cannot formulate or realise their notions of the good outside of their community, and, as members of that community, they may have set distributive or social justice as a goal. In taking action to achieve this goal, the state cannot be seen as coercive because, as a democratically constituted and elected body, it reflects the will of the people. An attack on this notion on the grounds that not everybody votes,

---

45 Hayek, *The Constitution of Liberty* (London and Henley: Routledge and Kegan Paul, 1960), p. 232. "A government which cannot use coercion except in the enforcement of general rules has no power to achieve particular aims that require means other than those explicitly entrusted to its care and, in particular, cannot determine the material position of particular people or enforce distributive or 'social' justice." p. 231.

46 F. A. Hayek, "The Atavism of Social Justice", *Social Justice, Socialism and Democracy* (Turramurra, Australia: Centre for Independent Studies, 1979), pp. 9-11.

47 Hayek, *The Constitution of Liberty, op. cit.*, p. 87. Brennan offers another way of understanding this argument against social justice using the way economists have eliminated the medieval notion of "just price" from the market. "They argue that any *proper* explanation of why prices (and outputs) are what they are must make appeal to the interaction of forces of demand and supply. Whether the price so generated is 'just' or not, or, indeed, what exactly a 'just price' would be, is simply irrelevant." Similarly, it is possible to see public policies emerging from the "interactions of rational agents, all pursuing their particular and partially conflicting goals within the framework imposed by democratic political institutions: 'just policy' is about as relevant in explaining what occurs as the 'just price' is in market interactions". Brennan, *op. cit.*, p. 52. Author's emphasis.

48 *Government Management, op. cit.*, p. 123. It does not define what it means by excessive. Boston has argued that the issue of "too much" social spending immediately raises the question of "too much by comparison with what?" If international comparisons are used as a benchmark, then it is not possible to argue that New Zealand was spending too much on welfare. "If on the hand one is using a different benchmark, namely that any spending is too much, well obviously we'll be spending too much." Boston, speaking to Ngaire Woods, "Analysis: Shrinking the State", BBC News and Current Affairs Department; broadcast on July 13, 1995.

or that majority rule means the views of the minority are over-ruled, is not justified in this instance because voter participation rates are high in New Zealand and voters have traditionally chosen between two major parties who have followed the principles of social justice as a socially desired goal. Social justice may be an attempt by society to enhance the liberty of all of its constituent members, within a notion of the common good, by giving them the resources they need to pursue their choice of a good life.[49] Income redistribution, and access to housing, health-care, and education can be seen as enhancing individual liberty by trying to even out some of the inequalities of the market that prevent people from being equally able to take advantage of opportunities.

Unequal power in the market

Social justice notions recognise that markets are not the "neutral" mechanisms of co-ordination between individuals wanting to engage in voluntary exchange that Treasury's neo-liberal framework projects. This is not to say that Treasury sees actors in the market as having equal power, just that it does not see these power differentials as a problem. Trade, or voluntary contracting, in the market is taken as a situation where someone values a resource more highly than its current owner and is willing to "compensate" the owner in order to transfer ownership.[50] The market disciplines potential "undesirable consequences" such as exploitation, unfair trading and monopoly practices itself through competition, because where such practices give an individual or firm a higher return than that earned elsewhere, there will be incentives for others to enter the market and compete. Competition therefore undermines the longer term survival prospects of such practices, and provides "a check against abuse of power and privilege".[51] This argument is not sufficient,

---

49 A good life here does not refer to an individual's desire to have caviar for breakfast or to own luxury cars, but to have the basic resources necessary to participate in the community's notion of a good life. That is, the community may have a notion of a "common form of life", which "is seen as a supremely important good, so that its continuance and flourishing matters to the citizens for its own sake and not just instrumentally to their several individual goods or as the sum total of these individual goods". Charles Taylor, "Alternative Futures: Legitimacy, Identity and Alienation in Late Twentieth Century Canada", in A. Cairns and C. Williams, eds., *Constitutionalism, Citizenship and Society in Canada* (Toronto: University of Toronto Press, 1986), p. 213., quoted in Kymlicka, *op. cit.*, p. 224.

50 *Government Management, op. cit.*, p. 15.

51 *Ibid.*, p. 16.

however, because it assumes that all goods and services available in the market are preferences or wants, not needs.

Some people, or "consumers" in Treasury's market lexicon, are disadvantaged in real-world markets because modern society is not a world where producers and consumers meet on an equal basis but is, instead, riven with "massive asymmetries of power and resources".[52] Consumers do not have the same power as producers (or the owners of resources), and the market is not neutral between the power differentials.[53] Wealth, or power, accrues to those who already have it to exercise, which means the market is not free and voluntary because the weaker partner often is not free from coercion. This stems partly from the fact that the exchange is not always "voluntary" in terms of being undertaken willingly: market exchange for the purpose of obtaining luxury items may be voluntary, but exchange for the necessities of life -- food, clothing, housing, electricity for cooking and heating and so on -- cannot be seen in the same way. The weaker parties in the latter transactions are vulnerable to coercion because in order to survive they cannot choose *not* to take part in the exchange.[54] On this point, Treasury's insistence on the market as a forum for "free and voluntary" exchange with no acknowledgement of the consequences of power differentials may lead to an unintended, and distasteful, outcome of slavery if an individual desperate to fulfil his or her basic needs has no other way to do so. The state, being limited to setting the rules by which the market operates, has no reason to intervene to stop this because the person has exercised his or her choice to enter the arrangement, and state intervention would be "coercion".

---

52 Held, *Models of Democracy, op. cit.*, p. 260.

53 This argument may not apply in the labour market where the owners of land and capital are the consumers of labour. The problems of power inequalities in this market will be discussed in the next section.

54 This point highlights the weakness in Treasury's argument over the power of poor buyers to effect change in the market. ("Thus no matter how poor a buyer is, if there are many sellers to choose between competition will drive prices down towards a level that reflects all the costs of production, including a reasonable return for capital and risk.." *Government Management, op. cit.*, p32.) Poor buyers can forgo their wants, but have to fulfil their needs in order to survive, therefore they must try to enter the market. However, there may not be many sellers in the market at the price they can afford to pay, which limits their ability to choose among sellers and thus their bargaining power. Treasury's argument confuses wants and needs, and neglects the unequal power of partners to a contract.

The inequality of power coupled with the necessity of meeting one's basic needs in order to survive is particularly important for Treasury's discussion of the labour market, which it says is a market just like any other: "[W]illing sellers (of labour services) trade with willing buyers within the prescribed rules governing the nature of trading."[55] In a consistent theme throughout the briefing papers, Treasury argues for a limited state role in the labour market, calling for labour market regulations "permissive enough to allow arrangements to emerge that are mutually beneficial to workers and employers".[56] It seeks an end to minimum wages, wage-fixing, occupational licensing and rules governing professions on the grounds that labour-market flexibility in both wages and the movement of labour between skills, occupations and activities would, "by facilitating necessary resource shifts", enhance over-all economic growth.[57] It says these will, among other things: allow employment arrangements to reflect the diversity of opportunities and threats facing firms and workers; allow arrangements that lead to the development of productive skills and expertise for workers and managers; ensure that negotiations of employment arrangements are carried out in the interests of firms and workers; and encourage the co-operative element of employment relations while recognising that firms' and workers' interests can diverge.[58] However, it is not clear how these results will emerge in a market where there is a major power differential between employers and employees, and the latter need a job in order to buy the things necessary for survival. Treasury has eliminated the option of the workers staying unemployed and receiving a benefit because benefits are kept low as an incentive to find a job and -- as will be discussed later -- in order to encourage people into employment, Treasury is prepared to make benefits low enough that an adequate living standard is not assured.[59]

---

55 *Economic Management, op. cit.*, p. 235. That is, the mechanisms of supply and demand work the same way in this market as in other markets.

56 *Government Management, op. cit.*, p. 278.

57 *Economic Management, op. cit.*, pp. 234-247., *Government Management, ibid.*, pp. 270-293., *Briefing 1990, op. cit.*, pp. 141-157., and *Briefing 1993, op. cit.*, pp. 75-89.

58 *Briefing 1990, ibid.*, p. 146.

59 *Briefing 1993, op. cit.*, p. 84. "The design of the welfare system needs to ensure that people have an incentive to accept work or undertake training, while still providing an adequate level of income ... These issues ... raise complicated administrative issues, and *trade-offs between encouraging desirable behaviour and ensuring adequate living standards*." My emphasis.

Treasury assumes that workers have some bargaining power because employers need their skills, but in a small economy with high unemployment where competition for jobs is keen, the reverse is true. Treasury repeatedly stresses the need for skills as a means of getting a job, saying that better skills are central to achieving stronger growth in the longer term and to ensuring that the benefits are more widely shared. "Jobs are increasingly knowledge and technology based ... [and] with the prospect of continuing rapid technological change, people can expect to repeatedly train and learn new techniques and approaches throughout their working lives."[60] As outlined in the previous chapter's discussion on "user-pays" in education, Treasury says the returns or higher wages obtained for greater skills give workers the incentive to train. However, the small size of New Zealand's economy means jobs are limited, even for those with skills, and the higher wages for skilled workers may never eventuate. Treasury acknowledges this in the 1993 briefing:

> Despite the sustained economic growth now forecast for the next few years, many people may experience only slow wage growth. This will result from their low productivity (reflecting their work history and low skill levels), and the fact that, *while high unemployment exists, there will be considerable competition for jobs.*[61]

Competition means the bargaining power stays with employers because it is easy to replace from the pool of unemployed any worker who does not accept the wages and conditions offered in the negotiation process that Treasury envisages in a deregulated labour market.

The free market may, in theory, give individuals liberty to pursue their interests, but the serious economic inequality caused by the differentials of power within the market makes this an unlikely achievement in practice. The inequality of ability to obtain wealth from the market "gives a small fraction of men control over the rest. People have vastly different access -- sometimes no access -- to the things necessary to develop human qualities."[62] An outcome of equal liberty, where liberty is understood as the ability to follow and achieve one's preferences as well as one's

---

60 *Ibid.*, p. 77.

61 *Ibid.*, p. 78. My emphasis.

62 Graeme Duncan, "Comments on Some Radical Critiques of Liberal-Democratic Theory", in Pierre Birnbaum, Jack Lively, and Geraint Parry, *Democracy, Consensus and Social Contract* (London: Sage Publications, 1978), p. 64.

needs, is especially unlikely in modern society given the major differences in starting points between classes, cultures, sexes and races. Economic inequality may also affect an individual's freedom from coercion, that is, their freedom from restrictions or interference by others, because a market of unequal power creates the opportunity for the more powerful partner in an exchange to take advantage of the other and impose his, her or its will on the weaker partner.[63] As outlined above, given the necessity of their needs, and not merely their preferences, the weaker partners may not always be able to decline such an exchange. Examples of this abound in the labour market during times of high unemployment, where individuals are faced with accepting the wage offered for their labour or becoming unemployed. It also affects an individual's access to resources to pursue his or her own wants and needs. Individuals whose lives are controlled by the dictates of market forces cannot be said to be truly free because they are not able to determine the conditions of their own lives. As discussed in chapter three, freedom cannot be extracted from its social, cultural and economic context. Simple freedom from coercion may be meaningless if it is not accompanied by the type of freedom that allows some choice of the quality of one's life.

The impact of economic inequality on political equality

Economic inequality may also affect political equality, understood as each member of the society having an equal share in political power with an equal right to participate. Individuals may, of course, choose not to participate, but they have the opportunity to do so. Significant economic inequality may undermine political equality by increasing the ability of the economically powerful to pursue their interests in the political sphere. The more wealth that individuals have, the more resources they can contribute to pursuing their interests, which means those in higher socio-economic groups may wield more power both economically and politically than those in lower groups.[64] As Mulgan points out:

> Superior wealth and education, particularly wealth, are also accompanied by superior political power ... In terms of their numbers, the less well-off make much less effective use of interest groups; they are likely to have less ready access to their MP as an intermediary willing to act on their behalf with government agencies; in local

---

63 "Its" refers to the fact that corporate actors are major players in today's markets.

64 Mulgan, *op. cit.*, p. 125.

> government, they are less commonly found as members of local bodies and, by not exercising their right to vote in sufficient numbers, do not exert much direct or indirect pressure on these bodies.[65]

Political inequality may result in a decrease in collective interests because the rich and politically powerful will argue for policies in their own interest. For example, they may be frustrated at having to pay "twice" for goods and services -- once through tax and once in the market -- and may lobby for lower taxes, which will decrease the amount available for services for the poor. Harvard Medical School assistant professor Ichiro Kawachi says his research shows that the increased stress this places on the poor leads to less participation by them in the democratic process.

> The rich move in the opposite direction. They may still contribute to the democratic process, but their motivation is self-interest. They see the poor as being responsible for dragging the whole system down. So ultimately, the atmosphere of social justice and equality -- under which public health and education systems were first established -- also goes into decline.[66]

This issue will be raised again in a later section.

A related issue here is that society, through the state, has constructed the market, setting and enforcing the rules by which it operates. The rules, however, can be changed through the democratic process, which means those with the most economic and political power will be able to lobby for changes that suit them.[67] Peter Self raises the problem of what might happen if the rules governing the market were continually undermined, saying that without wise and acceptable rules, market freedom would soon degenerate into atomistic chaos.[68] In this sense, a state that does not intervene to alleviate serious economic inequality cannot protect the environment necessary for individual liberty. Access to resources is state controlled, and whatever the state does or does not do will effect the distribution of resources, and consequently individual opportunities to exercise liberty.[69] Economic inequalities

---

65 *Ibid.*, p. 158.

66 Ichiro Kawachi, quoted in John Saunders, "The Nation with a Heart of Stone", *Evening Standard* February 8, 1997, p. 12. Kawachi specialises in the social and economic factors influencing public health.

67 Brian Easton raises this point when discussing the claims of New Zealand Business Roundtable executive director Roger Kerr, who says that businesses should comply with the law because to do otherwise may result in a loss of profit or incarceration. Easton says that in a democracy, "business is entitled to argue for a change of the law (as the Roundtable did over insider trading), no doubt in order to increase their profits, so law is hardly a permanent standard". Brian Easton, "Profit or public good", *The Listener* March 15, 1997, p. 60.

68 Peter Self, *Government by the Market?* (Boulder and San Francisco: Westview Press, 1993), p. 254.

and their subsequent effects on political equality create the risk of seriously undermining both narrow and broad conceptions of individual liberty because excessive concentrations of power, whether political or economic, in the hands of particular actors in the free market restricts what individuals are able to achieve. If people are to be free and equal in the determination of the conditions of their own lives, they need to have the opportunities to do so in both principle and practice.

Inequality as an "incentive"

Treasury is opposed to intervention to alleviate economic inequality, however, on the grounds that inequality is a positive force in the market. It claims inequality is a motivating force for economic growth, or as former prime minister David Lange explained: inequality of income in New Zealand is "the engine which drives the economy" through the workings of incentives.[70] Inequality provides the incentives that drive people to get jobs, and produce and invest more to achieve greater returns. As raised earlier, Treasury says excessive attempts to impose a predetermined concept of justice might be stultifying of economic activity and act as a "powerful disincentive" to private and voluntary activities that could promote well-being.[71] Like Galbraith, Treasury also sees income "the key to wider participation in society by providing the individual with the opportunity to exercise choice".[72] However, it claims income is an "incentive" for individual action and initiative, and therefore recommends that the state not guarantee an income beyond a minimum to survive. Any more than this reduces the incentives for the recipients to undertake actions to help themselves. "Actions to reduce the scope and magnitude of inequalities in the community may entail efficiency costs, by weakening the incentives the market provides individuals to undertake productive and otherwise profitable activities."[73] Taxing, or taking resources or wealth from some to support others, reduces the individual liberty of those from whom resources are being taken

69 *Ibid.*, p. 255.

70 David Lange, "The New Welfare State" Mackintosh Memorial Lecture, Prestonpans, Scotland, 1986, quoted in Jack Vowles, "Ends, Means, and for Whom?", in Jonathan Boston and Martin Holland, eds., *The Fourth Labour Government: Radical Politics in New Zealand* (Auckland: Oxford University Press, 1987), p. 21.

71 *Government Management, op. cit.*, p. 123.

72 *Ibid.*, p. 169.

73 *Economic Management, op. cit.*, p. 194.

in that the coercive state imposes a conception of redistribution on them. It also decreases their incentives to maintain their efforts.[74]

Leaving aside for now Treasury's understanding of efficiency costs, an immediate problem here is Treasury's interpretation of the motivations of individuals. In presenting a view of monetary incentives as the means for getting people to do things, Treasury portrays people as driven by greed and envy to trade-off anything from their dignity to their participation in society in return for greater material assets. Again, leaving aside for the moment Treasury's use of "trade-offs", the difficulty here is that Treasury does not recognise that people may respond to other motives or that other factors may constrain an individual's option to respond to the "incentive". For example, Treasury moots the use of incentives in the form of "partial user charges" in health to encourage individual behavioural changes such as "avoiding accidents", improving diet, and drinking and smoking less.[75] In other words, being made to pay for the results of risky behaviour encourages people to take responsibility for their own risks, such as being hurt on a sports field or being stricken with heart disease. This ignores that reasons such as avoiding pain, anguish and discomfort may be equally effective -- or equally ineffective -- motives.[76] Similarly, Treasury wants stand-down periods and increased margins between benefits and wages as incentives to encourage people to take jobs, which implies that there are many jobs available and people are simply choosing not to take them. In periods of high unemployment, this is not true, and creates serious difficulties for Treasury's argument for a trade-off between "adequate living standards" and keeping benefits low as an incentive for people to accept work or undertake training to enable them to get work.[77] Nor is it

---

[74] "... it may seem easier to try to redistribute income through taxation ... However, any large-scale tax-based redistribution programme that significantly raised the income of low-income working families would impose very high costs. The costs include not only the fiscal value of the transfer payments, but also the demotivating effect that high marginal taxes has on efforts to acquire skills or to work long hours." *Briefing 1993, op. cit.*, p. 83.

[75] *Briefing 1990, op. cit.*, p. 98.

[76] While Treasury's use of the term "avoiding accidents" is unusual, given that accidents by definition are *chance* events bringing injury, loss or distress that people do not choose to have happen, its use is understood here in the broader context of people choosing not to take part in risky activities.

[77] *Briefing 1993, op. cit.*, p. 84. "The design of the welfare system needs to ensure that people have an incentive to accept work or undertake training. This involves consideration of eligibility criteria, obligations placed on recipients, the levels of assistance and abatement rates, and the duration of assistance. These issues in turn raise complicated administrative issues, and trade-offs between

necessarily true that people will work less hard or acquire fewer skills if they have to pay tax. Gerald Cohen has successfully debunked this claim in an argument built on the notion that in order for a social policy or institutional arrangement to be justified, it must be capable of being justified interpersonally, by members of society speaking to each other. He says the issue of lower tax as an incentive for the employed to produce more is not about whether those paying higher tax would be *able* to work to the same degree without incentives, but whether they would be *willing* to do so. If they are not, then they have to be able to justify their behaviour -- and their larger shares -- to other community members, which Cohen claims they are not able to do.[78]

Another difficulty with the neo-liberal argument for inequality as an incentive is raised by Partha Dasgupta when he criticises the claim that the market mechanism allows even a person possessing no physical assets to join the labour force, and thereby step on the escalator to possible future success.[79] This does not recognise that at systematically low levels of nutritional intake a person's capacity for work is affected adversely. Workers require guaranteed access to certain essential commodities, or basic needs, in order to obtain "productive work, and thus access to further commodities".[80] Associated with this is that without an adequate living standard, the problems of those on benefits and low incomes will be exacerbated, and may eventually be more costly to society in terms of higher mortality rates, higher crime rates and so on. Treasury acknowledges this problem in its 1993 paper, saying that some people face multiple difficulties such as limited work or social skills, poor health and housing, low income, and poor attitudes to works and acquiring skills.

> While better growth will help to some extent because it will then be easier to obtain a job, their problems are likely to limit their ability to share in growth. Furthermore, their problems may be passed on from one generation to another, within families or social groups. The problems will be particularly acute for children in these situations. If the problems are not addressed early these children will find it difficult to acquire skills, which will adversely affect their life chances. Long-term child development studies in New Zealand have found links between some early childhood experiences, teenage mental health and behavioural problems, and unemployment.[81]

---

encouraging desirable behaviour and ensuring adequate living standards."

78 Gerald Cohen, "Incentives, Inequality, and Community", in Darwall, *op. cit.*, pp. 331-397.

79 Dasgupta, *op. cit.*, p. 183.

80 *Ibid.*, p. 184.

81 *Briefing 1993*, *op. cit.*, p. 80.

The issues raised in this statement would seem to suggest an argument in favour of social justice to alleviate inequality in the market place and break the cycle, but Treasury opts to retain faith in the "trickle down" theory, under which the rising tide of economic growth raises all boats. "The stronger growth is ... the greater will be the benefit to these groups through increased employment opportunities."[82] This means that while growth is supposed to provide jobs to help the disadvantaged out of their plight, in fact, unemployment will in the foreseeable future remain about the same. A major difficulty with this argument is that Treasury has already admitted that under its latest economic forecasts, "while economic growth will be stronger than in the past, unemployment is expected to decline only gradually", with about 20,000 to 25,000 newly created jobs each year being sufficient only to cover growth in the work force.[83] Such a contradiction seems to confirm Kawachi's research results that "the rising tide will in fact drown up to 20 per cent at the bottom".[84]

The costs of inequality in the market are therefore borne continually by those with the least amount of resources and power. Inequality leads to an inability on the part of the weaker members of the society to purchase private goods, even those that may be necessary to their survival, and creates the possibility of coercion by the stronger, more powerful actors in the market. Notions of social justice are eliminated as not only infringing individual liberty, but acting as an impediment to the operation of incentives encouraging self-reliance and self-responsibility. Consequently no market actor is pursuing the public good because, as an aggregate of individual notions of the good, it is not seen to exist, and individual actors driven by self-interest have no incentive to care about what happens to others within the market. As New Zealand Business Roundtable executive director Roger Kerr recently said: "The social responsibility of business is to increase its profits."[85] Social justice and collective interests have been eliminated from both the public and the private sectors, being outside the realm of a limited state confined

---

82 *Ibid.*, p. 77.

83 *Ibid.*, p. 13.

84 Kawachi, *op. cit.*, p. 12.

85 Roger Kerr, "Social responsibility a case of corporate versus personal role", *The Press* January 11, 1997, p. 19.

to enhancing the pursuit of individual notions of the good and being of no interest to powerful actors in the market because there is no profit to be made.

Profit as the market's motivating force

In shifting more and more areas of life into the private sector, Treasury is assuming that the market has the same motives as the state -- facilitating the free and voluntary conditions that allow individuals to pursue their own notions of the good. In reality, the market follows the motives of its most powerful actors: achieving the highest possible profits. Michael Parenti offers particularly strong criticism of the market on this point, saying that labour, skills, technology, and natural resources are not used for social needs and egalitarian purposes in the market because they are used for corporate gain. "The corporations cannot build low-rent houses and feed the poor because their interest is not in social reconstruction but in private profit."[86] The neo-liberal response to this is that increased profits are returned to the market in the form of investment, which creates new jobs, employs more people and so on. For example, Kerr, who is a former assistant secretary to the Treasury vehemently denies that business has any social responsibility, quoting Adam Smith and the Pope to justify his position in a syndicated newspaper article attacking society's negative attitude to profit:

> The business of business is business -- using economic resources efficiently to provide the goods and services that consumers want. Those that do the best job for consumers make the most profits. ... When businesses are diverted from their main function, they falter and the whole nation is denied the benefits that profitable economic activity brings.[87]

But the inequality of power in the market means that the benefits do not accrue to the whole nation, but to those with economic power. This "trickle down" theory is weak for the reasons previously outlined -- with profit as a motivating force and no concept of social justice, the market has no incentive to look out for those with little economic power. The bottom 20 per cent remain trapped in a vicious cycle, and may indeed drown in the "rising tide".

---

86 Michael Parenti, *Democracy for the Few* (New York: St Martin's Press, fifth edition, 1988), p. 305.

87 Kerr, *op. cit.*, p. 19.

Many goods and services, if left to the market, would not be supplied despite their benefit to society because it is not profitable to do so. For example, accident and emergency care is of value to the community in saving lives after accidents that may or may not be the fault of the person involved, but the private sector is not interested in supplying services in this area because trauma medicine tends to be high-cost, and there is little or no profit to be made. Services that meet the needs of the poor and are affordable to them, such as low income housing or affordable urban transport, are also unlikely to be unprofitable, and therefore under-supplied by the market. Treasury argues against subsidised state provision of urban transport, saying it "may lead to inefficient processes, and services that are not directly responsive to the needs of the users".[88] It also may not generate gains equivalent to the taxes used in the subsidy. These arguments ignore that the benefits of urban transport accrue to others besides the direct users in terms of both decreased traffic congestion and lower pollution levels. The difficulty for Treasury is in measuring these benefits because they are not readily reducible to quantifiable units. It also neglects that the reason why some services are provided by the state is that they are inherently unprofitable, but society recognises that their provision is of value to the well-being of the community. As will be discussed in a later section, society is therefore prepared to underwrite the cost of the services.

Commodification of values and feelings

So far, discussion has focused on the fact that the organisation of society according to free-market principles eliminates notions of collective interest and social justice, and elevates liberty or freedom from interference in individual choice above all other considerations. The result is a breakdown in the underlying values of the community. Compounding this is that the market mechanism, by its very nature, only works with tangible commodities that individuals can trade or exchange. Treasury's neo-liberal model therefore reduces needs and wants to those goals that can be treated as commodities to be bought, sold and traded off against one another. Intangible values are seen as the same as tangible values, which allows

---

88 *Government Management, op. cit.*, p. 123.

Treasury to shift their provision and support into the private sector. Human relations are seen as purely market or economic relations, which means that individuals, as rational self-interested maximisers, will accept monetary incentives in exchange for their formerly intangible values and feelings. Those values that cannot be reduced to a monetary value, such as respect for others, altruism, and a public spirit, are not recognised by the market, which encourages selfish behaviour by rewarding only those actions for which people are paid. This has implications for Treasury's emphasis on the role of voluntary groups. It repeatedly claims that as state support is decreased, individuals will either become more self-reliant or will be helped by voluntary and charity groups.[89] Charity work, however, does not have a monetary value, and people are not rewarded in monetary terms for their voluntary contributions. In a market system of rational, self-interested maximisers, there is no incentive -- and arguably a strong disincentive -- for people to have the attitudes necessary to engage in charitable work.

The absence of values such as respect, altruism and a public spirit, which some may argue are essential to the functioning of a good society, combined with the lack of any ameliorating input from the state, results in an increase in negative individual behaviour such as theft, vandalism and violence as the gap between rich and poor in the market widens.[90] Kawachi says the evidence of the poor outcomes of pro-market policies in the United States should be a warning to New Zealand:

> As the gap increases, frustration increases. Most homicides [in the United States] are white on white, they're killing each other as a result of economic hardship, deprivation, a rising hostility and frustration against those who they see as being successful, as having all the material possessions. New Zealand has a very high homicide rate, so it would be foolish to imagine this country is not on that same path.[91]

Those doing well from self-interested behaviour in the market have no incentive to be altruistic or generous to those not doing well, because this behaviour is not rewarded by the market or by the negative responses of the less fortunate. Any social justice or

---

89 See *Economic Management, op. cit.*, p. 257., *Briefing 1990, op. cit.*, pp. 96, 97., and *Briefing 1993, op. cit.*, p.22.

90 "Religious decline linked with change in society", *The Press* February 28, 1997, p. 7.

91 Kawachi, *op. cit.*, p. 12.

egalitarian notions are eliminated as the values needed for their survival are destroyed. At this point, it appears that Treasury has created a self-fulfilling prophecy. It says in *Government Management* (1987) that "[t]he organisation of society towards the achievement of social goals would be immensely easier if individuals were always generous, altruistic, honest and forgiving. When they are selfish, jealous and spiteful then the costs of social organisation are raised."[92] Treasury's promotion of market mechanisms that reward only the latter behaviour has resulted in the very situation it claimed the market was better than the state at resolving.

Trade-offs and cost-benefit analysis

The conflation of tangible and intangible values allows Treasury to discuss trade-offs between efficiency and such values as equity and participation and feelings such as pain and anguish. A trade-off implies an initial cost-benefit analysis, where the costs of an action or a commodity are weighed against the anticipated benefits of the action or purchase. If the gains do not outweigh the costs, then the action or exchange may not take place. Treasury's use of the term, however, does not acknowledge that its weighing of costs and benefits do not always relate to the same groups of people -- those who bear the costs do not necessarily gain the benefits. This affects the supposed gains from efficiency, because those bearing the costs of creating efficiency are not necessarily those who gain from it. For example, when attacking redistribution policies on the basis of the need to maintain incentives for effort and to encourage "employment and independence", Treasury says that the costs associated with income redistribution suggest there are limits to the amount of redistribution that should be undertaken. "Determining the appropriate level of redistribution thus involves a difficult *trade-off* between the equity values of permitting participation in society and the equity value and important efficiency questions of retaining incentives for effort for both beneficiaries and taxpayers."[93]

---

92 *Government Management, op. cit.*, p. 12. It repeats this argument in 1990: "In determining benefit levels and eligibility criteria, difficult judgements are unavoidable. Trade-offs must be made between fiscal and social objectives, between short-run adequacy concerns and long-run effects on participation and growth." *Briefing 1990, op. cit.*, p. 108.

93 *Government Management, ibid.*, p. 170. My emphasis.

But those who pay the costs of a low income and limited participation in society are beneficiaries and the unemployed while those who gain from limits and incentives are taxpayers, who already have jobs. The "incentive" to a beneficiary of a low benefit only works if there is a job to be had, an outcome that highlights Treasury's mistaken assumption that all unemployment is voluntary.

In arguing that there are trade-offs between "encouraging desirable behaviour and ensuring adequate living standards", Treasury may be perpetuating both economic and political inequality. As discussed in chapter four, people have to have their basic needs met in order to then be able to provide for their own well-being. Without an adequate living standard, they may not be able to respond to incentives for "desirable behaviour". If they cannot participate in the market, then their ability to participate politically may also be limited. An important problem here is that Treasury is prepared to assign a monetary value to participation, and accept that some people will be able to participate in society less than others. People are therefore not being treated as though they had equal human rights, which Treasury says "express relationships between individuals ... with respect to each another", as Treasury is prepared to trade the rights of some in order to obtain benefits for others.[94] Similarly, when setting up its market versus state model, Treasury discusses the use of public morals and the maintenance of human dignity as an objective or criterion that guides decision-makers, and challenges the claim that the loss of dignity or alienation has important social consequences that mean it cannot be left as a private concern. Treasury says that the loss of dignity is likely to be more important for some than others, and "it is important therefore both to employ careful analysis of individuals' need for dignity and evaluate what *trade-offs* alternative institutional structures may involve".[95] Again, while some individuals may lose their dignity, it is a different group of individuals that get the benefit of the state's withdrawal of support of dignity for all. It is arguable whether a democratic society would accept either of these "trade-offs" if, as will be discussed in the next section, it has decided

---

94 *Ibid.*, p. 13.

95 *Ibid.*, p. 34. My emphasis.

to bear the cost of ensuring all of its members have an adequate standard of living in order to gain the benefit of having a particular type of community.

Efficiency as the penultimate aim

This discussion highlights one of the major problems with Treasury's argument throughout its briefing papers: that its notion of efficiency is confined narrowly to a concept that is amenable to a cost-benefit analysis. Treasury says efficiency is "concerned with achieving the greatest level of national income for a given quantum of resources" because the basic constraint that society faces is the scarcity of resources relative to the demands that are placed on them.[96] "There is a need to use physical and human resources efficiently, to make them go further, and to ensure that the use to which they are allocated are those that are most highly valued."[97] Efficiency, therefore, is judged in terms of the allocation of resources so that they are not "wasted", and that they are employed in their most "socially valued use", generating the maximum gain for a given supply of resources.[98] The market is seen as the best mechanism for the efficient allocation of resources because prices convey to market participants information about competing claims to resources and the costs of production. Individuals use prices to make production and consumption decisions in a way that incorporates wider social claims on resources. "Through changes in price, changes in demand and supply are signalled to resources owners and resources are guided to more high valued uses", a process that "assists growth and improves the welfare of all".[99] "Efficient markets force individuals to make choices about the priorities they have, reconcile their demands with those of others, and further provide incentives for individuals to conserve the use of resources wisely."[100] All of which, Treasury says, are socially desirable outcomes.

---

96 *Economic Management, op. cit.*, p. 296.

97 *Government Management, op. cit.*, p. 11.

98 *Ibid.*, p. 30. "If in any sense then efficiency can be used as a guide for social decision making it probably implies a concern for the maximisation of wealth in a society. It involves concern for ensuring valuable resources are not wasted and are allocated to their most socially productive uses, and it implies evaluating alternative institutional options according to these concerns."

99 *Ibid.*, p. 33.

100 *Ibid.*, p. 15. Also *Economic Management, op. cit.*, p. 297. The market is "a highly efficient method of generating and passing on information in that each transaction acts as a signal to those involved and forms the basis of further decision. Only the most essential information is passed on, and only to those concerned."

An immediate difficulty with this notion is how Treasury defines "highly valued", "socially valued", "socially productive" and "socially desirable" outcomes. In linking efficiency to the price mechanism, Treasury is equating "efficiency" solely with money and the maximum price that can be obtained for a resource -- "resources are guided to more highly valued uses". This eliminates from "efficient" use all those who may value the resource, but who cannot afford to pay for it. Demand within the supply and demand price mechanism is made effective only by those with money. Treasury's use of efficiency as improving the "welfare of all" can only be understood if "welfare" is confined to notions of wealth or money rather than a broader definition of social well-being, and "all" is understood as an aggregate measure, rather than a measure of the welfare of every individual.[101] "Socially desirable outcomes" have been defined narrowly as those that maximise wealth to the individuals and corporations who have control of the resources. Given that market exchange is not between free and equal partners, but often massively unequal ones, an efficient outcome may be far from "socially desirable" if this is understood in a broader sense that includes notions of equity or fairness. Efficiency in terms of "highly valued" resource use, where value is judged by price, may therefore be an insufficient allocation mechanism if society has social justice goals such as ameliorating the inequality of power and control of resources in the market.

Treasury's stance on this is somewhat contradictory. It acknowledges that society may have equity and social justice concerns, saying there is no reason to presume that an "efficient" distribution of income and wealth would be regarded as socially desirable, nor that society would be unwilling to trade a reduction in aggregate income for a more equitable outcome.[102] "Some government action to redistribute income in favour of less advantaged members of the community may strengthen social consensus and democratic processes and allow incentives to the improvement of individual welfare to operate with less resistance."[103] But Treasury's neo-liberal stance repeatedly rejects intervention for these reasons, returning time and

101 In other words, the income of some may rise while that of others falls or stays the same, but if the over-all income level rises, Treasury considers the "welfare of all" to have improved.

102 *Economic Management, op. cit.*, p. 296.

103 *Ibid.*, p. 296.

again to efficiency and cost concerns. It says that in order for the state to intervene, there needs to be a clear balance of benefits over costs from the proposed action, taking into account both equity and efficiency considerations. The opportunity cost to the pursuit of an equitable set of social outcomes means the "efficiency cost of complete equality would be prohibitively expensive" and "by interfering too much in the income received by [resource] owners, the government may adversely affect incentives to efficiently allocate and use resources. The necessity to evaluate trade-offs between efficiency and equity cannot be over-emphasised."[104] With this argument, Treasury is using an extreme position of "complete equality" to negate arguments for any redistribution, even though few, if any, New Zealanders would claim that the state's role is to provide "complete equality". What New Zealanders do appear to want, as previously outlined, is that resources be shared fairly with each person having a maximum opportunity to achieve a standard of living that enables him or her to belong and participate in the community.[105]

Treasury's use of the term trade-off is problematic because the costs and benefits of the trade-off between equity and efficiency do not apply to the same groups of people. Treasury says "trade-offs imply a perfect world may not be possible", although "in many areas of existing policy it may be possible to improve both equity and efficiency".[106] Where this is not possible, however, Treasury appears to be prepared to sacrifice equity for efficiency, ignoring that by their very nature, social justice objectives are those for which society has placed cost considerations behind other motivations such as security or justice. That is, in order to achieve a given outcome -- a particular type of community -- society is prepared to sacrifice wealth because the outcome is not judged solely in terms of money, but in the broader sense of social well-being.[107] For example, in the provision of public

---

104 *Government Management, op. cit.*, pp. 123, 33. Treasury does not elaborate on how much interference is constituted as "interfering too much".

105 Task Force on Economic and Social Planning, *op. cit.*, p. 392.

106 *Government Management, op. cit.*, p. 33.

107 This highlights the incongruity of Treasury's inclusion of, and emphasis on, efficiency as an objective or criteria for making social choices in its discussion on the role and limits of government in *Government Management*. Treasury devoted the first five pages of its discussion to efficiency, two pages to equity, a third of a page to liberty and a page to public morals and human dignity. *Ibid.*, pp. 25-34. A society that has broader social objectives in mind may not agree with that order of priority.

services, the state is providing goods and services society has deemed it wants all of its members to have, regardless of their ability to pay. Society has recognised that, if left to the market, where allocation is determined by price, not everyone who needs these goods may obtain them. It therefore accepts the cost of providing the goods, in return for the social justice of their provision to all. Treasury is critical of many of these attempts to correct "perceived social problems", claiming that the state's failure to achieve these objectives arises because it has focused on desired results or outcomes, and "the question about what is the most efficient means of achieving desired outcomes has not been addressed sufficiently".[108] But efficiency in process when judged in terms of cost may not bring the anticipated results. For example, Treasury condemns the "waste" of holding the price of public services below resource costs, saying that holding down these prices for "social" reasons would seem to be a "sure recipe for widening inequalities" because such subsidies are delivered to all users, "irrespective of need".[109] But if these were provided "efficiently" on Treasury's terms, that is, the users were charged the full cost of the resources, then the social objective -- provision of services to all, regardless of ability to pay -- would not be met. Supplying the services to all "irrespective" of need may be the only way society can ensure they are provided to those who need them the most.[110]

The weakness of Treasury's narrow conception of efficiency can be seen in its discussions on state spending, when the scarce resource being allocated is state funds, and efficiency is interpreted as the desire to get the highest return in terms of goods and services for the least outlay. Treasury's focus again is on cost, and obtaining the most for the least cost, which means that it again has to reduce all intangible feelings and values to tangible commodities that can be quantified and assessed via their price. It attacks state spending across the board, saying resources

---

108 *Economic Management, op. cit.*, p. 252.

109 *Ibid.*, p. 198.

110 A related, but important, point here is that the "efficiency" of achieving "socially desirable" objectives cannot always be judged in terms of money. Raising the price may not result in an allocation society prefers. For example, society may deem it desirable for all New Zealanders to be able to communicate by post. Rural mail delivery costs more than urban delivery, and an "efficient" system in monetary terms would be to charge users according to where they lived. However, this may not result in the desired outcome if rural residents could not afford to have their mail delivered. An efficient allocation in this case is achieved by the larger number of urban residents subsidising the rural service.

have not been put to their "best use", that is, their most efficient use, because the provision of services at no charge to consumers removed the role of price signals in ensuring the amount and quality of services reflected as closely as possible consumer demands and the costs of supplying them, and provision via state-funded institutions reduced the incentive for suppliers to provide services at the least cost.[111] For example, it says that in health, previous forms of organisation have made it difficult to ensure that an "adequate level and quality of service" is provided for the money spent in the public-hospital system.[112] "Increasing the effectiveness of spending requires increased efficiency in the production of services, and increased efficiency in funding. Efficiency in funding involves paying the lowest price for a given level of service, and funding those services which best meet the needs and preferences of the community."[113] This statement shows that in assessing the "effectiveness of spending", Treasury has equated "effective" outcomes with "efficient" outcomes, which means that non-tangible considerations have been eliminated from performance assessments.

A major difficulty with using the price signal as a gauge to control consumer demand by showing them the cost is that it ignores that in many areas the state has undertaken supply because the true cost of the resource is too high for most people to pay, but the outcome of having the good or service is seen as socially desirable. The state undertakes the provision of particular goods and services because society recognises that many people would not get them if they had to pay for the goods and services themselves. A 1976 government-appointed Task Force on Economic and Social Planning found that there was a "strong desire to maintain New Zealand's reputation for social 'pioneering' and social justice".[114] It said New Zealand had "progressively developed a comprehensive range of social services characterised by underlying notions of egalitarianism, humanitarianism, and a conviction that the

111 *Economic Management, op. cit.*, p. 271.

112 *Briefing 1990, op. cit.*, p. 118.

113 *Ibid.*, p. 123.

114 Task Force on Economic and Social Planning, *op. cit.*, p. 55. This thesis uses the Task Force report as a guide to what New Zealanders want from social policy rather than the later, more comprehensive 1988 Royal Commission on Social Policy because the latter was not in existence when Treasury was formulating the ideas contained in its briefing papers.

state has a responsibility for the health, education and welfare of its citizens", and New Zealanders wanted it to stay that way.[115] If "price signals" are used to measure how much of a good or service is supplied, it is not clear how this is "efficient" if it reduces consumer demand for goods and services society has deemed desirable for all. For example, in health, the use of the price mechanism may produce distasteful outcomes if the price of treatments, say radiotherapy for cancer patients, is raised until demand from patients is reduced. The result may be efficiency in process in terms of an artificial equilibrium, where demand has been driven down by price until it equals what Treasury wants to the state to pay, but this is not efficiency in outcome when judged in terms of how well the use of resources has met society's desires -- equal access to certain goods and services. These goods and services can be seen as "merit goods" or those that are "often publicly provided to ensure that access to them is not hindered by the potential user's inability to pay", and for which economic efficiency is not considered to be the most important criterion of their provision.[116] Society has made a political decision to provide these goods because of their role in creating the kind of community in which members of society have decided they want to live. It these goods and services must be rationed, then it must be a *political* decision for society to resolve, not the market.

This argument leads to difficulties for judging efficiency in "funding those services which best meet the needs and preferences of the community".[117] In some ways, this contradicts the aim of buying a service at the least possible cost, given that the services that meet the needs and preferences of the community may not

---

115 *Ibid.*, p. 97.

116 Stuart Birks, "The Public Sector: An Overview", in Stuart Birks and Srikanta Chatterjee, *The New Zealand Economy: Issues and Policies* (Palmerston North: Dunmore Press, 1992), p. 279.

117 It is not clear how the "needs and preferences of the community" are decided, but presumably it is through demand expressed in marketplace exchanges. However, the market may not be the most appropriate mechanism, given that needs and preferences can be shaped by what is supplied in the market, as well as propaganda and advertising. That is, as new goods and services become available on the market, they shape consumer preferences. This means it is not possible to measure market efficiency in terms of satisfaction of existing demands because the market has an effect on preferences and choices. As David Hogan aptly points out: "The very idea that one can independently measure the level of exchange efficiency in a market in terms of the satisfaction of existing preferences is at best nonsensical and at worst, a wilful sociological deceit." David Hogan ,"The Social Economy of Parent Choice and the Contract State: Some Theoretical Issues". Paper presented at the Conference on "The New Contractualism", Griffith University (November 1995), p. 21.

necessarily be those that cost the least. For example, Canterbury people would prefer a cardiac surgery unit was established in the public sector, at Christchurch Hospital, but the Southern Regional Health Authority does not want to pay for it, saying that the most cost-effective public provision for heart surgery in the South Island is using the cardiac unit already set up in Dunedin Hospital. Arguments advanced in favour of a Canterbury unit include that the costs in terms of patient pain and anguish at having to travel away from their families, and the risk of travel at a time when patients are very sick, are too high. Efficiency in terms of the trade-off between tangible (money) and intangible (human feelings, values and life itself) is not easily judged. Returning to the earlier point about cost-benefit analysis and trade-offs, those paying the costs of more "efficient" resource use in social policy are not necessarily those who are gaining the benefits. For example, patients bear the costs of "efficient" health care that limits the number of hospital beds and restricts the amount of surgery performed.[118] However, taxpayers gain the benefits of the lower cost of public health services with a reduction in the amount of tax they pay. Those with the highest incomes gain the most; the costs are confined to those needing, rather than "wanting", the service. The costs and benefits of the alleged better use of resources are thus unequally distributed across society.[119]

Citizens as clients and consumers

As human values and feelings have been transformed into commodities and shifted into the private sector, so Treasury's pro-market model also

---

[118] A similar argument can be made in education. Students and parents bear the cost of a decentralised, "user-pays" education system, both in financial terms and in terms of the new demands on their time (serving on school boards of trustees and so on). The benefits are distributed across taxpayers. The poor may bear more costs for several reasons, including that schools in lower socio-economic areas are unlikely to have the resources of schools in wealthier areas. See the extended discussion on this issue in chapter four.

[119] Private insurance is not an adequate response to this cost-benefit problem in health, because those who can afford it are generally those who have already gained the benefits of the increase in "efficiency" of the public health system. It may also create a new problem, as outlined by Birks: "If individuals have to pay for health care, many choose to take out insurance. this has two advantages, first payments can be made when convenient, not when someone is unable to earn, and second major expenses are avoided due to the cover. Markets are considered to operate efficiently if the value of the additional benefit from the last unit consumed by an individual equals the additional cost incurred in making that unit available. The addition cost to an insured person of a visit to the doctor, say, is less than the true cost. To follow this up one state further, premiums will rise to cover the extra cost, and some individuals may decide not to take out insurance cover. In other words, markets, even with insurance, are unlikely to satisfactorily, allocate health care." Birks, *op. cit.*, p. 268.

transforms citizens into consumers or clients whose needs and wants are simple matters of commodity exchange either in the market (the private sector) or via market mechanisms in the public sector. The distinction is important because it changes the relations between state and society, and what members of society can expect from their state. Treasury uses the terms "consumers" and "clients" interchangeably with "individuals", "people" and occasionally "citizens" throughout its briefing papers, without acknowledging that the terms are not synonymous. Tim Lang and Colin Hines say the difference between the terms is "critical":

> The consumer chooses between products on the shelf, designed, built and profited from by others; the consumer is an end-user. In contrast, the citizen is actively involved in all stages of a process, directly or by representation. The word consumers indicates at worst a passive role and at best someone who can only act in the market through their purchasing power.[120]

As Lang and Hines observe, this is not an argument against consumption, but against reducing the capacity of citizens to decide "what *sort* of consumption, how extensive it is, its impact on the environment and social equity, how many goods are consumed, how long goods last and what effects the decision-makers have over the processes which make the goods".[121]

Linda McGuire explains the importance of the distinction between consumers and citizens when she examines Australian public services and their performance.[122] She uses the term "customers" to distinguish the relationship between citizens and the public sector services, saying citizens can be seen as the "customers" of the services because customers by definition pay for services while clients or consumers are more often those that meet eligibility criteria.[123] Public services therefore have "multiple stakeholders with conflicting goals".[124] Citizens as taxpayers own the services and want economy and efficiency, where -- as will be discussed in a later section -- these are defined in broader terms than simply achieving economic efficiency. Citizens as clients want reliable, quality services.

---

120 Tim Lang, and Colin Hines, *The New Protectionism: Protecting the Future Against Free Trade* (New York: The New Press, 1993), p. 109.

121 *Ibid.*, p. 114.

122 Linda McGuire, "Service Delivery Contracts: Quality for Customers, Clients and Citizens". Paper presented at the Conference on "The New Contractualism", Griffith University (November 1995).

123 *Ibid.*, p. 15.

124 *Ibid.*, p. 15.

Public management reforms in Australia have, like those in New Zealand, aimed to make more efficient and effective use of resources in delivering public services by increasing productivity and improving service quality. As in New Zealand, the new distinguishing characteristic of public services is a focus on clients. Management strategy is now aimed at improving responsiveness to clients and encouraging their active participation in service delivery by introducing direct accountability to clients of public services.[125] However, the new accountability appears to be limited to *delivery*. Clients can demand better delivery of that particular service, but cannot demand more than that, such as what sort of service is provided, how much, for how long and so on. These questions are decided, as Lang and Hines argue, by citizens, who are different to clients, consumers or "end-users" because they are "actively involved in all stages of a process, directly or by representation".

By implication, consumers are not producers and initiators, yet people participate in democratic decision-making as citizens, not as direct users, consumers or clients of the state's services. The key term here is participation. Citizenship, or the "sense of community membership based on loyalty to a civilisation which is a common possession", can be seen to involve the ability to participate more or less equally in the social life of society.[126] However, as discussed in previous sections, Treasury is prepared to trade off participation in society in order to create incentives for increased self-reliance and decreased dependence on the state. Consequently, it appears to be prepared to accept that some New Zealanders will not be full citizens, given that a lack of resources means the poor will not be able to participate in the civilisation that others enjoy as "a common possession" and are thus deprived of an essential component of citizenship.[127] Disenfranchising the poor from citizenship may reinforce both economic and political inequalities, which has implications for the provision of future public services. Citizens as "customers" pay for services while

---

125 *Ibid.*, p. 3. Mechanisms to increase responsiveness to clients include the use of customer surveys and customers councils to find out customers' views, and customer-service training for public servants.

126 T. H. Marshall, *Citizenship and Social Class* (Cambridge: Cambridge University Press, 1950), discussed in Barry Hindess, *Freedom, Equality and the Market* (London and New York: Tavistock Publications, 1987), p. 37.

127 *Ibid.*, p. 38.

"clients" use services; if the poor are not counted as citizens then they become only clients, who do not have the power to decide what services will be provided or how extensive or equitable they will be. Those who do count as citizens -- the wealthy -- may not be interested in paying for public services used by the poor. As previously discussed, when the economically powerful become politically powerful, they can use their power to pursue their own interests, which may result in the elimination of notions of collective interests.

Consumers and collective interests

Public services by their very nature are collective services, with "public" signifying that the services have social objectives as well as objectives for individual clients.[128] Effectiveness in public services means meeting service standards and producing outcomes for clients, as well as meeting the goals of citizens in providing the type of community in which they want to live. In this sense, the provision of public services is based on social justice notions of redistribution and is a political, not just managerial, process because defining effectiveness (outcomes) is inherently political.[129] Through the political process, society sets what outcomes it wants and places them in order of priority; in doing so, it may place provision for all above economic efficiency. This creates a problem for the market model because its notion of efficiency rests on the measurement of outputs, that is, on quantifiable outcomes such as the number of clients seen in a given time period and so on. Society's goals (outcomes), such as equity or the provision of a service to those who need it, may not be so easily measured. Restricting performance evaluations of public services to how well they satisfy client requirements ignores the intangible aspects of public service provision, including citizens' social justice objectives, which are hard to specify and evaluate, and therefore may not be realised.[130]

The use of market mechanisms such as a funder-provider split may exacerbate measurement difficulties, given that it puts an extra step between the

---

128 McGuire, *op. cit.*, p. 20.

129 *Ibid.*, p. 18.

130 *Ibid.*, p. 18.

consumers and the public managers responsible for allocating resources. Accountability becomes more difficult because clients are in contact with those providing the service, not those deciding which services to fund. It is not clear how the wants and needs of consumers will be transmitted to decision-makers. For example, heart patients and their families seeking a public-sector cardiac unit in Canterbury tell their providers (general practitioners and hospital doctors) of their preferences for care, but the Southern Regional Health Authority, which controls the funds, makes the decision. The authority's output is economically efficient in that patients still have their surgery -- in another province -- and costs are controlled, but the service provision is not effective in that the outcome is not what the community wants.

The fact that not all outcomes can be measured in quantifiable terms means it is not possible to confine performance evaluations to measurable indicators such as economic efficiency, that is, achieving the same with less or making the same produce more. The argument here is not that economic efficiency is not desirable or necessary, but that performance indicators need to include public interest and community service objectives as well as client service and efficiency.[131] Public services must include service standards and measures that reflect collective objectives in performance evaluation. Repeated claims that public services are not "efficient" when that judgment is confined to economic terms may eventually undermine that their primary reason for existence may never have been to make money, but to fulfil community goals. Citizens are born into, and spend their lives, in communities that shape their interests, and have collective as well as individual goals. They want the state, as an embodiment of their collective will, to be driven by broader motivations than simply providing an "efficient" service.

Restricting performance evaluation to economic efficiency has another important effect in that it allows citizens and their wants to be removed from consideration when setting efficiency criteria for public services. Examples of this

---

131 *Ibid.*, p. 18.

can be seen in the arguments made to "corporatise" some of New Zealand's state-owned enterprises. "Corporatisation" meant private sector business principles were applied to public enterprise management. The new philosophy was that the corporations were to be "as profitable and efficient as comparable businesses that are not owned by the Crown", that is, they were required to accept the responsibility of operating at a "reasonable" profit.[132] They were also supposed to "exhibit a sense of social responsibility by having regard to the interests of the community in which it operates and by endeavouring to accommodate or encourage these when able to do so".[133] It could be argued that these aims conflict, as evidenced by the example of the Forestry Corporation, which in the first six months of its existence (April-September 1987) recorded a cash surplus of $24 million compared with the cash deficit of $35 million in the six months before it was corporatised.[134] Labour finance minister of the time, Roger Douglas, has since lauded the turnaround, saying that

> [w]ithin 12 months, the number of employees, including contractors, had been reduced from 7000 to 2600 without loss of output. The cash surplus rose steadily to reach $150 million during the year to March 1990.[135]

But the aim of state ownership of forests was never solely to make a profit. As Bob Gregory argues,

> Many [state-owned forestry] planting, logging and processing activities have, over the years, been dictated by political and social concerns (particularly job creation and maintenance) rather than purely commercial considerations.[136]

In running forestry as a commercial venture, with its primary goals efficiency and profit, the social reasons for the state's intervention were lost. A similar argument could be made for other nationalised industries privatised or corporatised during the reform period. Many of the reasons for state ownership could not be quantified in purely monetary terms. The application of free-market practices has eliminated many -- if not most -- of the goals of collective ownership and neglected that a reason for state ownership and intervention is that it ensures the achievement of community objectives that members of society have decided cannot be entrusted to the market.

---

132 Clause 4(1)(a) of the State Owned Enterprises Bill introduced into Parliament on September 30, 1986, quoted in John Roberts, "Ministers, the Cabinet and Public Servants", in Boston and Holland, *op. cit.*, pp. 101, 102.

133 *Ibid.*, clause 4(1)(c).

134 Roger Douglas, *Unfinished Business* (Auckland: Random House, 1993), p. 180.

135 *Ibid.*

136 Robert Gregory, "The Reorganisation of the Public Sector", in Boston and Holland, *op. cit.*, p. 126.

CONCLUSION

The most important implication of Treasury's neo-liberal framework appears to be that the emphasis on growth, and neo-liberal methods to achieve it, comes at the expense of the collective notions behind New Zealand's traditional welfare state. New Zealanders have long believed that they lived in a "quarter-acre, pavlova paradise", where every New Zealander had the opportunity to buy a quarter-acre section and live well for the rest of their lives. From the 1930s and the introduction of the Keynesian welfare state, a comprehensive range of social services had been established, based on underlying notions of egalitarianism, humanitarianism, and a conviction that the state had a responsibility for the health, education and welfare of its citizens. Such services were built on a particular type of life being available to all New Zealanders; that there were certain goals that each New Zealander was entitled to reach for, and the state was there to ensure that all New Zealanders had an equal chance of achieving those goals. For example, for a long time home ownership was considered to be a priority and goal that every New Zealander should -- and could -- have a chance to achieve. The state therefore provided low-cost housing, low-interest mortgages and tax rebates for first-home owners. New Zealanders had come to expect the provision of these types of support as part of what it meant to be a citizen of New Zealand. More important, perhaps, was that it was available to all New Zealanders equally.

The 1976 Task Force on Economic and Social planning found New Zealanders had firm notions of what they wanted from the state, and a strong desire to maintain social justice. It told the government that while economic objectives must be given a "very high" priority in the "foreseeable future", it was not enough to concentrate planning on economic issues:

> Planning for social justice, for a positive reduction of social problems, for a greater sense of community, for a pleasant environment, and for cultural and recreational activities which both refresh us and develop our national identity, is not only important in its own right, but also an essential element in any scheme to

> overcome our economic difficulties, while keeping New Zealand a place were both young and old will wish to live.[1]

New Zealanders were prepared to accept economic growth as a desirable policy objective "*provided* growth is intelligently directed to minimise the social and environmental costs and maximise the benefits".[2] In other words, they were prepared to sacrifice efficiency or wealth in order to achieve a better community.

However, Treasury's neo-liberal framework does not allow for such collective notions because it has commodified privatised notions of social well-being. Individuals are seen to have their own notions of well-being, which can be reduced to goods and services that can be exchanged in the market, and the collective good is simply an aggregate of individual good. In reaching this conclusion, Treasury compared the state's ability to achieve social goals with that of the market, and ruled in favour of the latter. It says that in dealing with the constraints on achieving social objectives -- scarcity, interdependence, uncertainty, information and opportunism -- the state faces the same difficulties as the private sector, plus other ones. This means that, in effect, the state can never be as proficient as the market in providing for the wants and needs of New Zealanders. In this it is following the neo-liberal philosophy that the individual is the best judge of his or her own interests and should therefore be left free from interference to pursue those interests. The best mechanism for meeting those preferences is the market, where willing buyers and willing sellers engage in voluntary contracts so that each is better off through the exchange than they were before. State intervention decreases this individual welfare and leads to inefficiency because it distorts the market signals and disrupts competitive equilibrium.

Treasury is concerned with efficiency because the efficient use of resources is one of the means to ensure the economic growth that it claims will solve New Zealand's economic crisis. Another means of achieving growth is to decrease the "burden" on the state by increasing individual self-reliance and self-responsibility, thereby also encouraging individual initiative. This is consistent with Treasury's

---

1 Task Force on Economic and Social Planning, *New Zealand at the Turning Point* (Wellington: Government Printer, 1976), p. 45.

2 *Ibid.*, p. 34. Authors' emphasis.

notions that individuals should be given freedom to pursue their own notions of the good. The state has to take into account that when it intervenes, it is decreasing the incentives for individuals to provide for the bulk of their needs through the market, their family, or voluntary agencies and charities. Treasury claims that a decrease in state support will put the responsibility for help for the needy back on the community.

This is similar to the views of David Green, which were widely promulgated in New Zealand in 1996 after his book, *From Welfare State to Civil Society,* was published by the New Zealand Business Roundtable.[3] Green's arguments are analogous to Treasury in that he argues for a radical reform of the welfare state on the grounds that it causes a decrease in self-reliance and self-responsibility and, more importantly, a decline in civil society. He claims excessive intervention by the state has replaced the older tradition of personal duty for others' welfare, and the marshalling of individual resources to develop solutions to shared problems, with a propensity to look to the state to act. The solution to social problems lies, not in more state spending, but in the return of welfare to being the primary responsibility of the "individual and his (sic) family", supported by the community in the form of voluntary associations and with the state in the background "ready to help but within proper limits".[4] To achieve this,

> governments should, first, step back to create the space for a renewal of public but not political action, and, second, they should refrain from actions that undermine personal responsibility, the family and voluntary associations. The rest is up to us.[5]

By "us", Green means a revitalisation of civil society, and a return to the "philanthropic ethos" of the past.[6] Green's work takes a similar approach to Treasury in that he contrasts the abilities of the market and the state in providing for citizens, concluding that if state intervention were decreased in favour of the market,

---

3 David Green, *From Welfare State to Civil Society* (Wellington: New Zealand Business Roundtable, 1996).

4 *Ibid.*, p. 111.

5 *Ibid.*, p. 98.

6 *Ibid.*, p. 111. Green says there were two elements to this philanthropic ethos. First, the "community without politics", or the sense of solidarity with others that is based on an obligation to help each other without degrading the recipient. Second, the sense of "duty without rights". "Everyone, and especially the wealthy, had a duty to help but no-one had a right to receive assistance. Giver and receiver were both expected to take pains to show mutual respect."

individuals would freely interact to achieve their preferences in everything from health and education to pensions. Those temporarily unable to support themselves would be aided by voluntary organisations of their fellow citizens, because a decreased state fosters an enhanced sense of community.[7]

Treasury has also put forward these arguments, which are based on the assumption that the free market enhances the conditions to maintain a successful democracy by encouraging self-responsibility and a commitment to the welfare of others. However, it is not clear that neo-liberal policies and attitudes will result in the community values envisaged because weaknesses in the underlying "scientific" assumptions may lead to weaknesses in the expected outcomes. The mechanisms of the market, and the rational self-interested maximisers acting within it, may undermine the very political values neo-liberal policies need in order to operate. For example, Treasury wants to break the "vicious cycle" of welfare dependency and to decrease the role of the state, moving many functions back on to the individual, the family, and community and voluntary groups, but to do this it needs the notions of collective interest and community values -- that is, that members of society have a responsibility to other members of society -- that self-interested behaviour in an unequal market eliminates. This thesis has argued that people are not the rational, self-interested maximisers that neo-liberalism postulates. But the implementation of neo-liberal policies is likely to turn people into such creatures, at the same time eliminating the "public spirit" that neo-liberalism needs in order for voluntary groups to take on some of the former functions of the state. In reducing individuals to rational self-interested maximisers, neo-liberalism accentuates individual responsibility and self-help measures so that there is likely to be less collective

---

7 *Ibid.*, pp. 29, 30. Green says community rests on a view of human character that "sees people not as innately good, not infinitely malleable through education, but which emphasises our mutual interdependence. It goes without saying that the coercive power of the state should not be employed to produce a particular character, but that supporters of liberty should in their private lives do their bit to maintain the existence of institutions that bring out the best in people -- above all the traditional family, but also the voluntary associations for helping one another which historically were part of the fabric of society. The reason for reducing the scope of the welfare state, therefore, is not only that private organisations will provide better services, but also that it will restore the role of voluntary associations whose task is character building as well as service provision."

responsibility in the future. The emphasis on self-interest decreases collective interest.

Neo-liberalism rejects social justice, saying it is coercive in that it involves taking from some in order to give to others. It is also portrayed as a disincentive for individuals to look after themselves because they can rely on the state (and the work of others), and it is stultifying of the economy in that it involves regulation and tax that restricts free and voluntary exchange and discourages people from working harder because they would have to pay more tax. Treasury recognises that some people may be disadvantaged in the market, but accepts this inequality saying that it provides an incentive for the unemployed and low-income earners to obtain jobs or further education and new skills. The problem is that at low levels of income people may be unable to provide for their own well-being and may be caught in the poverty trap that Treasury says it is anxious to avoid. It may also result in more state intervention as people suffer multiple disadvantages and need more help than if the state had intervened earlier. For example, poor health and low education creates a situation where income is likely to be low. With a low income, people are less likely to eat well, which may lead to poor health, and are less likely to take part in education. They are caught in a poverty cycle that may result in their needing more state resources.[8] Economic inequality may also result in an increased need for law and order as poverty brings an associated increase in crime.[9]

The ultimate effect is a prisoner's dilemma in which, based on selfish interests and actions, the outcomes are worse than if people had taken a more

---

8 As discussed earlier, Treasury acknowledges that "a group of people" experiencing multiple disadvantages, including poor health, poor housing, low income, and low skills and education, will be less likely to benefit from growth "without some assistance". Children in these situations will be particularly affected, because "there appears to be a link between disadvantage in childhood and subsequent unemployment". New Zealand Treasury, *Briefing to the Incoming Government 1993* (Wellington: GP Print Ltd, 1993), p. 14. Arguably, early intervention would break this cycle.

9 This raises an interesting dilemma for Treasury given its recently publicised 1994 report urging that the state not employ more police officers because this would increase the costs in the justice system as the enlarged police force caught more criminals. In this it appears to be arguing to limit the state's role beyond the generally accepted parameter of neo-liberalism, which is that the state's role be restricted to enforcing law and order. Diane Keenan, "Plan aims for lift in police strength", *The Press* April 11, 1997, p. 3.

public-spirited stance.[10] The "dilemma" is created because individuals believe they will be disadvantaged when others act selfishly -- that is, in Treasury's lexicon, they believe they will suffer from the opportunistic actions of others -- so they also choose selfish behaviour. The result is a downward spiral, in this case leading to a decrease in collective actions and a decrease in political equality as the poor are no longer able to participate in society, and ultimately in politics. Treasury is prepared to trade off participation by the poor in return for the incentives of obtaining skills or work, but this only succeeds when there is low unemployment and jobs are plentiful. When this does not happen, the result may be that the political system becomes the realm of the rich, who will use it to pursue their own interests. Treasury's use of incentives is based on a bleak view of individuals driven by envy and greed, which is likely to become a self-fulfilling prophecy under these conditions. If individuals are not "unencumbered selves" but are shaped and formed by their community, then a selfish community will create selfish individuals. A mechanism that Treasury does not acknowledge exists -- that the community shapes individuals -- will contribute to the creation of the very type of people on which Treasury has based its model.

Unfortunately, this may bring the negative, opportunistic attitudes that Treasury warns of when setting out its market versus state model.

> The organisation of society towards the achievement of social goals would be immensely easier if individuals were always generous, altruistic, honest and forgiving. When they are selfish, jealous and spiteful then the costs of social organisation are raised.[11]

In assuming people exhibit only the latter characteristics, and framing policy accordingly, Treasury may eliminate the former, positive behaviour. It can be argued that this is already evident in New Zealand after 12 years of neo-liberal inspired

---

[10] The dilemma is commonly framed as two prisoners sitting in separate cells, with each being urged to confess and help convict the other. The pay-offs are that if a prisoner confesses (defects) and the other does not (co-operates), she receives a lighter sentence than her partner in crime. If both confess (defect) then both receive long jail terms, while if both stay quiet (co-operate) then both receive short jail terms or go free. Each prisoner reasons that if she defects and the other prisoner stays quiet, she will get the best result. If, however, she stays quiet and the other defects, then she will get the worst result. Because she cannot trust that the other will not defect while she confesses, then the dominant selfish strategy prevails. Both defect, which lands both with a substantial jail sentence. Both could have achieved a better result by tacitly co-operating and staying quiet. Peter Self, *Government by the Market?* (Boulder and San Francisco: Westview Press, 1993), p. 11.

[11] New Zealand Treasury, *Government Management* (Wellington: Government Printing Office, 1987), p. 12.

reforms. For example, reducing "welfare dependency" has become a hot issue for the government, and the National government, when introducing a tax-cuts package in February 1996 justified its decision not to apply the cuts to those on benefits because it wanted to give beneficiaries the incentive to get back to work.[12] The implication was not that society has a collective interest in looking after all of its members, but that individuals who have "chosen" not to work should be encouraged to change their minds. Similarly, one of the first major policy initiatives of New Zealand's first coalition government was the introduction of legislation that from April 1, 1997, all domestic purposes beneficiaries whose youngest child is 14 or older will have to go into work or training -- or lose their benefit. A $1500-a-head conference for senior members of government, state agencies and businesspeople was held in Auckland in March 1997 to canvass ways of getting beneficiaries back into paid work, and one of the major topics was investigating ways to create a "paradigm shift" in public attitudes in favour of a tougher "throw the bums off welfare" response to beneficiaries.[13] The new Treasurer, Winston Peters, wants welfare reform to reduce the state's role and strengthen "family responsibility", while Social Welfare Minister Roger Sowry claims "tolerant social attitudes allow people to malinger". Sowry says welfare reform is about "making sure people in receipt of a benefit do have -- and acknowledge -- a responsibility to society".[14] He does not appear to consider that traditionally New Zealanders have always believed that the reverse was also true -- that society has a responsibility to all of its members.

Neo-liberalism changes the relationship between state and society, moving from positive notions of state support for those who need help to negative

---

12 Michael Rentoul, "Changes give gains to workers", *The Press* February 20, 1996, p. 1. A related point here is that the way in which the National government justified the tax-cuts package reflects the degree to which the "neutrality" premise of Treasury's discourse has been absorbed into everyday discourse. Politicians now claim that economic policy is free from politics, and the policies chosen are selected for what they can achieve for economic growth and thus the good of the country. When National announced the tax-cuts package in February 1996, at the beginning of an election year, it argued that the package was "less about politics than creating the incentives to ensure ... further economic growth". After 12 years of economic reform in the name of "economic growth", New Zealanders were asked to believe that what was done for the economy was politically neutral rather than an election-year bribe. Peter Luke, "Tax cuts favour middle-income NZ", *The Press* February 20, 1996, p. 1.

13 Gordon Campbell, "Benefits for whom?", *The Listener* March 8, 1997, p. 34.

14 *Ibid.*, p. 37.

notions of dependence and being a burden on others. The market model supposes that the relationship between citizens and the state is the same as those of parties in the private sector. The result is a new relationship that limits the ability of citizens to exert control over the types and amount of goods and services the state supplies to meet their needs and wants. Social service provision is stripped of its human factors and commodified (given a monetary value), and is thus reduced to purely economic or market relations.[15] The emphasis on citizens as consumers highlights the individual and the individuals needs and wants, and how these can be met by the individual interacting with others in the market. The state's role is diminished from facilitating the achievement of the community's collective goals to setting the rules of the market within which individuals act to achieve their individual goals.

When the state's role is limited in this way, political action is confined to setting and enforcing the rules of the game while all the actions within the game are left to individuals or corporations in the private sector. State intervention becomes viewed as coercive, with a subsequent decline in collective interests. As Phillips observes:

> Governments are now judged primarily in terms of how well they serve our material interests and how careful they have been to leave us in peace. The idea that politics is about the pursuit of *public* happiness or the taste for *public* freedom has been tossed aside as an archaic ideal.[16]

The implications of this for the political community are broad, especially if democracy is understood, as C.B. MacPherson suggests, as "the equal effective right of individuals to live as fully as they may wish", with a democratic system providing "the conditions for the development of human capacities, and to do this equally for all members of society".[17] Neo-liberalism does not allow the state to provide the conditions for the development of human capacities, because it claims the market is

---

15 "Witness the renaming of people as 'resources' and university graduates as 'product'." Peggy G. Koopman-Boyden, "Social Policy: Has There Been One?", in Martin Holland and Jonathan Boston, eds., *The Fourth Labour Government: Politics and Policy in New Zealand* (Auckland: Oxford University Press, Second Edition, 1990), p. 228.

16 Anne Phillips, "The Classic Debates", in *Engendering Democracy* (Pennsylvania: Pennsylvania State University Press, 1991), p. 47. Author's emphasis.

17 J. Roland Pennock, *Democratic Political Theory* (Princeton, New Jersey: Princeton University Press, 1979), p. 5., and Graeme Duncan, "Comments on Some Radical Critiques of Liberal-Democratic Theory", in Pierre Birnbaum, Jack Lively, and Geraint Parry, *Democracy, Consensus and Social Contract* (London: Sage Publications, 1978), p. 64.

better able to achieve this than the state. However, the market's ability to provide the opportunities for all members of society equally cannot be guaranteed, which may be a reason why the community is prepared to accept state intervention. Notions of a "fair and thriving" society are defined by the community through a political process; the state, as an embodiment of the collective will, is entrusted with intervening to secure these aims because society's members do not trust the market to do so.

Soon after the 1996 election, National member of Parliament Simon Upton wrote in one of his fortnightly newspaper columns that politics was "back with a vengeance" in New Zealand after a 12-year hiatus.[18] He claimed that from 1984 to 1996 New Zealand had been ruled by a single government that "masqueraded under two different political banners" as it embarked on an ambitious reform programme that transformed the country into a bastion of free market economics. Both Labour and National governments "drank at the neo-liberal well because the old one had quite simply dried up". The new MMP environment, which brought more parties and the prospect of coalition governments to Parliament, returned politics -- or a plurality of policy ideas and options -- to centre stage, "and there's nothing in Treasury's tool kit about how to deal with it". Upton's linking of Treasury to the neo-liberal reforms of this period states plainly what many people believed; that Treasury adopted one policy framework to the exclusion of other options, which it then applied to all areas of New Zealand life, both economic and social. Such a claim is worth investigating because the adoption of a single policy stance contravenes what is commonly accepted as the role of a state agency that has to serve governments of all political hues; that policy advice be neutral, presenting a range of options from which the ruling party can choose a programme that reflects its election pledges or policy goals.[19]

As raised in the introduction to this thesis, public servants may not find this an easy task. They have to seek effective action from within "a range of

---

[18] Simon Upton, "Without a crisis looming, reform in New Zealand is going to be much harder", *The Press* November 5, 1996, p. 11.

[19] The term "or policy goals" is used here to reflect the claim that recent governments have not fulfilled their election pledges. A discussion on the truth of this claim is outside the scope of this thesis.

values and constraints that conflict in differing ways under differing circumstances". The policy options offered to ministers have to reflect public concern that authority exercised in its name, and using its resources, is both efficient and economic, yet socially responsive. In this, Treasury is no different to any other department. It is the government's main adviser on economic and financial affairs, and is expected to offer advice on macroeconomic matters, supply-side issues, and social policy.[20] It could therefore reasonably be expected that such advice should include the setting out of the pros and cons of a range of options along with their costs and benefits. However, Treasury became synonymous with the economic, administrative and social reforms of 1984-1996, being widely identified as their "leading advocate, and prime architect". Jonathan Boston, one of the most prolific writers on Treasury and its role, says Treasury has become so closely identified with the "radical, often controversial" reforms that opponents of the policies of both the Labour and National governments of this period have vented much of their anger on Treasury. "Some, in fact, have assumed that it is the Treasury which now dictates the policy agenda in New Zealand, the government having become a mere pawn and mouthpiece, 'ensnared in the Treasury's line'."[21] Other commentators on New Zealand economics and politics reinforce this claim.[22] Treasury is therefore not seen as a politically neutral public sector body, but is linked to a particular ideological stance that resulted in reforms that transformed New Zealand from a Keynesian welfare state to a bastion of the free market.

This thesis is not interested in whether it is right or wrong for Treasury to take a consistent policy stance; such a claim is beyond the scope of this thesis and involves consideration of the role of government departments and constitutional

---

[20] Jonathan Boston, "The Treasury: Its Role, Philosophy and Influence", in Hyam Gold, ed., *New Zealand Politics in Perspective* (Auckland: Longman Paul, Third Edition, 1992), p. 196. Boston says macroeconomic matters include monetary, fiscal, exchange rate, and incomes policies; supply-side issues include trade, tax and employment policies, industry assistance and labour market regulation; and social policy includes education, health, housing and social welfare.

[21] *Ibid.*, p. 195.

[22] See especially Shaun Goldfinch and Brian Roper, "Treasury's Role in State Policy Formulation during the Post-War Era", in Brian Roper and Chris Rudd, eds., *State and Economy in New Zealand* (Auckland: Oxford University Press, 1993), pp. 50-73., and Len Bayliss, *Prosperity Mislaid* (Wellington: GP Publications, 1994), pp. 75-78.

concerns.[23] Instead, it has focused on the political philosophy underlying this consistent policy framework, and what outcomes may result from assessing and setting policy through this particular ideological stance. It has used the briefing papers to incoming governments because these can be seen as the most "politically neutral" of Treasury's papers in that they are not ordered by or for a particular minister of finance, but are prepared as information documents for new ministers of any party. As such they are statements of the department's views on the state of the New Zealand economy and what should be done. An analysis of these papers shows that Treasury's political philosophy fits comfortably within neo-liberal ideology, and it can therefore be argued that Treasury did "drink at the neo-liberal well", taking a neo-liberal framework and applying it broadly across all sectors of economic and social policy. In *Government Management*, Treasury says New Zealanders "clearly aspire to secure a fair and thriving society" judged by goals and values including equity, efficiency and freedom.[24] An analysis of Treasury's briefing papers, however, does not provide convincing evidence that its neo-liberal prescriptions for social policy will achieve this. In fact, given the effect of limiting the role of the state, which has in the past guaranteed New Zealanders the opportunity to secure a life that is both fair and thriving, in favour of the unfettered workings of the free market, which offers no guarantees, an argument can be made that Treasury's policy framework will produce the opposite result.

---

23 General comments on this point have been made by others. For example, Bayliss says a competent Treasury not a policy eunuch, and should not sit perpetually on the fence. "It is quite legitimate for Treasury to express its support for a particular option. It is, however, a gross abuse of power for Treasury to make the option it supports the only choice by denigrating or by ignoring the alternatives." Bayliss, *ibid.*, p. 77.

24 *Government Management, op. cit.*, p. 9.

BIBLIOGRAPHY

Aimer, Peter. "The Rise of Neo-Liberalism and Right Wing Protest Parties in Scandinavia and New Zealand: The Progress Parties and the New Zealand Party", *Political Science* vol. 40 no. 2 (December 1988), 1-15.

"Air New Zealand credits Kiwi with holding down airfares", *Evening Post* February 21, 1997.

Amsden, Alice; Kochanowicz, Jacek; and Taylor, Lance. *The Market Meets Its Match.* Massachusetts: Harvard University Press, 1994.

Barry, Norman P. *The New Right.* London: Croom Helm, 1987.

Bayliss, Len. *Prosperity Mislaid.* Wellington: GP Publications, 1994.

Begg, David K. H.; Fischer, Stanley; and Dornbusch, Rudiger. *Economics.* London: McGraw-Hill, Second Edition, 1987.

Birks, Stuart, and Chatterjee, Srikanta. *The New Zealand Economy: Issues and Policies.* Palmerston North: Dunmore Press, 1992.

Birnbaum, Pierre; Lively, Jack; and Parry, Geraint, eds. *Democracy, Consensus and Social Contract.* London: Sage Publications, 1978.

Blank, Robert H. *Life, Death and Public Policy.* DeKalb, Illinois: Northern Illinois University Press, 1988.

Blank, Robert H. *Rationing Medicine.* New York: Columbia University Press, 1988.

Bloxham, Les. "Tickets to Australia soar 32%", *The Press* January 14, 1997.

Bollard, Alan, ed. *The Influence of U.S. Economics on N.Z.* The Fulbright Anniversary Seminars, N.Z.-U.S. Education Foundation, N.Z. Institute of Economic Research, Wellington, 1988, N.Z.I.E.R. research monograph no. 42.

Bollard, Alan. *Economic Liberalisation in New Zealand.* N.Z. Institute of Economic Research, Wellington, working paper 91/5 1991.

Bollard, Alan. *The Political Economy of Liberalisation in New Zealand.* N.Z. Institute of Economic Research, Wellington, working paper 93/2, 1993.

Boston, Jonathan, and Holland, Martin, eds. *The Fourth Labour Government: Radical Politics in New Zealand.* Auckland: Oxford University Press, 1987.

Boston, Jonathan. "Thatcherism and Rogernomics: Changing the Rules of the Game -- Comparisons and Contrasts", *Political Science* vol. 39 no. 2 (1987), 129-152.

Boston, Jonathan. "Redesigning New Zealand's Welfare State", in Boston, Jonathan, ed. *The Decent Society?.* Auckland: Oxford University Press, 1992.

Boston, Jonathan. "The Treasury: Its Role, Philosophy and Experience", in Gold, Hyam, ed. *New Zealand Politics in Perspective.* Auckland: Longman Paul, 1992.

Boston, Jonathan, ed. *The State Under Contract.* Wellington: Bridget Williams Books, 1995.

Brett, Cate. "Generation Debt", *North and South* February, 1997.

Campbell, Gordon. "Benefits for Whom?", *The Listener* March 8, 1997.

Castles, Francis; Gerritsen, Rolf; and Vowles, Jack, eds. *The Great Experiment.* Auckland: Auckland University Press, 1996.

Cohen, Ronald L. *Justice: Views from the Social Sciences.* New York: Plenum Press, 1986.

Colclough, Christopher, and Manor, James, eds. *States Or Markets?.* Oxford: Clarendon Press, 1993.

Crocombe, Graham T.; Enright, Michael J.; and Porter, Michael E. *Upgrading New Zealand's Competitive Advantage.* Auckland: Oxford University Press, 1991.

Dalziel, P.C. "The Rhetoric of Treasury: A Review of the 1990 Briefing Papers", *New Zealand Economic Papers* vol. 25 no. 2 (1991), 259-274.

Dalziel, P.C. "The Rhetoric of Treasury: Reply", *New Zealand Economic Papers* vol. 27 no. 1 (1993), 91-99.

Darwall, Stephen, ed. *Equal Freedom.* Ann Arbor: University of Michigan Press, 1995.

Davidson, Greg, and Davidson, Paul. *Economics For A Civilized Society.* London: MacMillan Press, 1988.

Deeks, John, and Perry, Nick, eds. *Controlling Interests: Business, the State and Society in New Zealand.*
Auckland: Auckland University Press, 1992.

Douglas, Roger. *Unfinished Business.*
Auckland: Random House, 1993.

Easton, Brian, ed. *The Making of Rogernomics.*
Auckland: Auckland University Press, 1989.

Easton, Brian. "Government Management: A Review of it's Political Content",
Political Science vol. 42 no. 2 (December 1990), 35-42.

Easton, Brian. "Ignoring the Critics",
The Listener February 15, 1997.

Easton, Brian. "Profit or Public Good",
The Listener March 15, 1997.

Eatwell, John; Milgate, Murray; and Newman, Peter, eds. *The New Palgrave, A Dictionary of Economics*. vol. 2: *E to J.*
London: MacMillan Press, 1987.

Franks, Stephen. "The New Zealand Experience",
Columbia Journal of World Business (Spring 1993).

Freeden, Michael. *Rights.*
Minneapolis: University of Minnesota Press, 1991.

Goodin, Robert E. "Liberalism and the Best-Judge Principal",
Political Studies vol. 38 (1990), 181-195.

Gorringe, Peter, and Bushnell, Peter. "The Rhetoric of 'The Rhetoric of Treasury' ",
New Zealand Economic Papers vol. 26 no. 1 (1992), 127-142.

Gray, John. *Beyond the New Right: Markets, Government and the Common Environment.*
London and New York: Routledge, 1993.

Green, David G. *From Welfare State to Civil Society.*
Wellington: New Zealand Business Roundtable, 1996.

Gutmann, Amy. *Democratic Education.*
New Jersey: Princeton University Press, 1987.

Hamlin, Alan, and Pettit, Philip. *The Good Polity: Normative Analysis of the State.*
Oxford: Basil Blackwell, 1989.

Hayek, F. A. *The Constitution of Liberty.*
London and Henley: Routledge and Keegan Paul, 1976.

Hayek, F. A. *The Road to Serfdom.*
London: Routledge and Keegan Paul, 1976.

Hayek, F. A. *Social Justice, Socialism and Democracy.*
Turramurra, Australia: Centre for Independent Studies, 1979.

Held, David. "The Contemporary Polarization of Democratic Theory: The Case for a Third Way", in *Political Theory and the Modern State.*
Cambridge: Polity Press, 1989.

Held, David. *Democracy And The Global Order.*
Cambridge: Polity Press, 1995.

Held, David. *Models of Democracy.*
Cambridge: Polity Press, 1996.

Hindess, Barry, ed. *Reactions To The Right.*
London: Routledge, 1990.

Hindess, Barry. *Political Choice And Social Structure.*
Aldershot: Edward Elgar, 1989.

Hindess, Barry. *Freedom, Equality and the Market.*
London and New York: Tavistock Publication, 1987.

Hindess, Barry. "Neo-liberalism and the National Economy" in Dean, M., and Hindess, B. eds. *Governing Australia.*
Cambridge: Cambridge University Press, 1997.

Hoadley, Steve. *The New Zealand Foreign Affairs Handbook.*
Auckland, with the Institute of International Affairs, Wellington: Oxford University Press, 1992.

Hogan, David. "The Social Economy of Parent Choice and the Contract State: Some Theoretical Issues".
Paper presented at the Conference on "The New Contractualism", Griffith University (November 1995).

Holland, Martin, and Boston, Jonathan, eds. *The Fourth Labour Government: Politics and Policy in New Zealand.*
Auckland: Oxford University Press, Second Edition, 1990.

James, Colin. *New Territory: the Transformation of New Zealand 1984-1992.*
Wellington: Bridget Williams Books, 1992.

James, Colin, and McRobie, Alan. *Turning Point: The 1993 Election and Beyond.*
Wellington: Bridget Williams Books, 1993.

Jesson, Bruce; Ryan, Allanah; and Spoonley, Paul. *Revival of the Right: New Zealand Politics in the 1980s.*
Auckland: Heinemann Reid, 1988.

Keenan, Diane. "Plan Aims for Lift in Police Strength",
The Press April 11, 1997.

Kerr, Roger. "Social Responsibility a Case of Corporate versus Personal Role", *The Press* January 11, 1997.

King, Desmond S. *The New Right.* Hampshire: MacMillan Education, 1987.

Kominik, Anna. "Health Care Still Sick After Radical Cure", *The Dominion* August 9, 1996.

Kymlicka, Will. *Contemporary Political Philosophy: An Introduction.* Oxford: Clarendon Press, 1990.

Lang, Tim, and Hines, Colin. *The New Protectionism: Protecting the Future Against Free Trade.* New York: The New Press, 1993.

Luke, Peter. "Tax Cuts Favour Middle-Income NZ", *The Press* February 20, 1996.

McAllister, Ian, and Vowles, Jack. "The Rise of New Politics and Market Liberalism in Australia and New Zealand", *British Journal of Political Science* vol. 24 (1994), 381-407.

McGuire, Linda. "Service Delivery Contracts: Quality for Customers, Clients and Citizens", Paper presented at the conference on "The New Contractualism", Griffith University (November 1995).

McKenna, Edward J., and Zannoni, Diane C. "Philosophical Foundations of Post-Keynesian Economics". *Journal of Post Keynesian Economics* vol. 15 no. 3 (Spring 1993), 395-407.

McLennan, Catriona. "Trade Policy for the 1990s", *The Press* May 24, 1993.

McLoughlin, David. "New Zealand at the Crossroads: MMP Election Special Issue", *North and South* July, 1996.

MacPherson, C.B. *The Rise And Fall Of Economic Justice.* Oxford: Oxford University Press, 1987.

Mansfield, Andrew W. *The Power Elite: the Treasury and N.Z. Business Roundtable's Power in the Formation of the Privatisation Programme 1984-1987 - A Theoretical Analysis.* M.A. Thesis, University of Canterbury, (1990).

Miller, David; Coleman, Janet; Ryan, Alan: and Connolly, William, eds., *Blackwell Encyclopedia of Political Thought.* Oxford: Blackwell, 1987.

Mulgan, Richard. *Democracy and Power in New Zealand.* Auckland: Oxford University Press, Second Edition, 1989.

Nagel, Jack H. *Market Liberalisation in New Zealand.*
Paper for delivery at the 1994 annual meeting of the American Political Science Association.

New Zealand Treasury. *Economic Management.*
Wellington: Government Printer, 1984.

New Zealand Treasury. *Government Management.*
Wellington: Government Printer, 1987.

New Zealand Treasury. *Briefing to the Incoming Government 1990.*
Wellington: GP Print Ltd, 1990.

New Zealand Treasury. *Briefing to the Incoming Government 1993.*
Wellington: GP Print Ltd, 1993.

Nixon, Chris. *New Zealand's Economic Environment.*
N.Z. Institute of Economic Research, Wellington, working paper 94/32, 1994.

Novitz, David, and Willmott, Bill, eds. *New Zealand in Crisis.*
Wellington: GP Publications Ltd, 1992.

Novitz, David. "The deep, fundamental flaws in report on Canterbury University", *The Press* February 5, 1997.

Nozick, Robert. *Anarchy, State and Utopia.*
New York: Basic Books, 1974.

Parenti, Michael. *Democracy for the Few.*
New York: St Martin's Press, Fifth Edition, 1988.

Patten, Alan. "The Republican Critique of Liberalism", *British Journal of Political Science* vol. 26 (1996), 25-44.

Pennock, J. Roland. *Democratic Political Theory.*
Princeton, New Jersey: Princeton University Press, 1979.

Phillips, Anne. "The Classic Debates", in *Engendering Democracy.*
Pennsylvania: Pennsylvania State University Press, 1991.

Pinfield, C.N. *Equity and Economic Policy.*
Discussion Paper no. 42 June 1987, Victoria University of Wellington, Department of Economics.

Pitkin, Hanna Fenichel. "Justice: on Relating Private and Public", *Political Theory* vol. 9 no. 3 (August 1981), 327-352.

Polanyi, Karl. *The Great Transformation.*
New York: Farrar & Rinehart, 1944.

Polanyi, Karl; Arensberg, Conrad M.; and Pearson, Harry W., eds. *Trade and Market in the Early Empires: Economies in History and Theory.*
New York: The Free Press, 1957.

Rawls, John. *A Theory of Justice.*
Oxford: Clarendon Press, 1992.

Rawls, John. *Political Liberalism.*
New York: Columbia University Press, 1993.

"Religious decline linked with change in society",
The Press February 28, 1997.

Rentoul, Michael. "Changes Give Gains to Workers",
The Press February 20, 1996.

Roper, Brian . "Business Political Activism and the Emergence of the New Right in New Zealand 1975 to 1987".
Political Science vol. 44 no. 2 (December 1992), 1-23.

Roper, Brian, and Rudd, Chris. *State and Economy in New Zealand.*
Auckland: Oxford University Press, 1993.

Rosenblum, Nancy L., ed. *Liberalism and the Moral Life.*
Massachusetts: Harvard University Press, 1991.

Ross, Frances. "Salvaging the System",
The Dominion January 13, 1997.

Ross, Frances. "So Much Promised, So Little Delivered",
The Dominion January 16, 1997.

Rutherford, Donald. *Dictionary of Economics.*
London and New York: Routledge, 1992.

Saunders, John. "The Nation with a Heart of Stone",
Evening Standard February 8, 1997.

Scitovsky, Tibor. *The Joyless Economy.*
New York: Oxford University Press, 1976.

Scollay, Robert; St John, Susan; and Horsman, John. *Macroeconomics and the New Zealand Economy.*
Auckland: Longman Paul, 1989.

Scott, Graham. "The New Institutional Economics and Re-shaping the State in New Zealand",
Paper presented at the conference on "The New Contractualism",
Griffith University (November 1995).

Self, Peter. *Government by the Market? The Politics of Public Choice.*
Boulder and San Francisco: Westview Press, 1993.

Sen, Amartya. *Choice, Welfare And Measurement.*
Oxford: Basil Blackwell, 1982.

Sen, Amartya. "Markets and Freedoms: Achievements and Limitations of the Market Mechanism in Promoting Individual Freedoms",
Oxford Economic Papers no. 45 (1993), 519-541.

Sen, Amartya. "Rationality and Social Choice",
American Economic Review vol. 85 no. 1 (March 1995), 1-24.

Sharp, Andrew, ed. *Leap Into the Dark - the Changing Role of the State in New Zealand*
Auckland: Auckland University Press, 1994.

Shim, Jae K., and Siegal, Joel G. *Dictionary of Economics.*
New York: John Wiley and Sons, 1995.

Statistics New Zealand. *New Zealand Official Yearbook 1996.*
Wellington: Statistics New Zealand, 1996.

Task Force on Economic and Social Planning. *New Zealand at the Turning Point.*
Wellington: Government Printer, 1976.

Taylor, Charles. *Philosophy and the Human Sciences: Philosophical Papers 2.*
Cambridge: Cambridge University Press, 1985.

Upton, Simon. "Without a crisis looming, reform in New Zealand is going to be much harder",
The Press November 5, 1996.

Webber, Lisa. "Student debt soars to $1.6b",
Christchurch Star February 14, 1997.

Whalen, Charles J. *Political Economy For The 21st Century.*
New York: M. E. Sharpe, 1996.

Wilding, Paul, and George, Vic. "Social Values and Social Policy",
Journal of Social Policy vol. 4 no. 4 (1975), 373-390.

Williams, Sharon. "Airfare rise no surprise",
Evening Post January 16, 1997.

Wolff, Jonathan. *Robert Nozick: Property, Justice and the Minimal State.*
Stanford, California: Stanford University Press, 1991.

Woods, Ngaire. "Analysis: Shrinking the State",
BBC News and Current Affairs Department; broadcast on July 13, 1995.