



**MINISTRY OF BUSINESS,
INNOVATION & EMPLOYMENT**
HĪKINA WHAKATUTUKI

Growing New Zealand for all

MBIE's economic narrative

May 2017



ISBN 978-0-478-43361-6
May 2017
© Crown copyright 2017

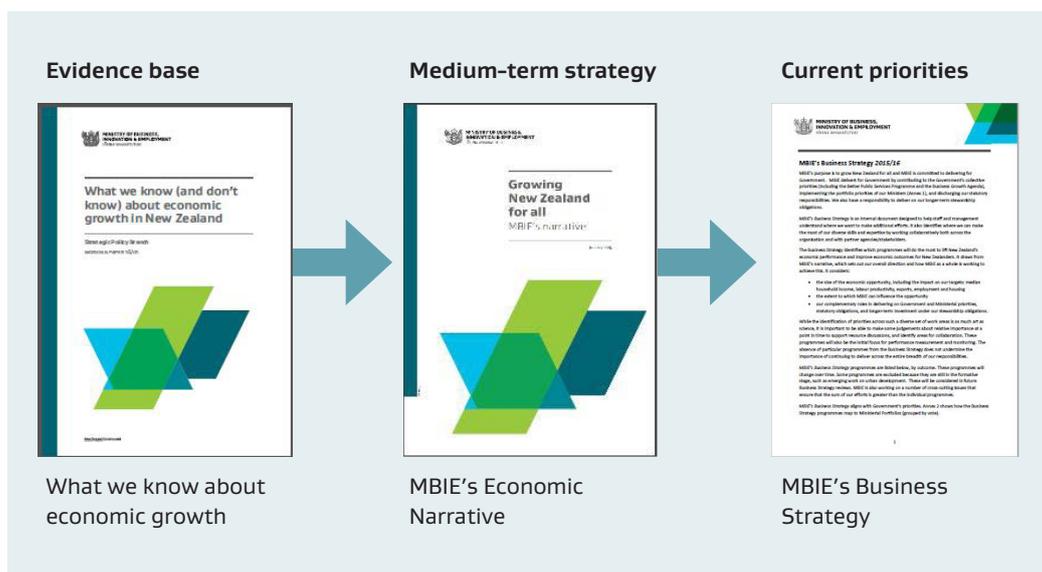
Purpose

The purpose of *Growing New Zealand for all* ('the economic narrative') is to:

- › identify the features of a successful economy
- › provide the context for MBIE teams to identify how their work contributes to achieving MBIE's vision of a successful economy
- › identify areas of focus, and associated activities, that could provide a sustained lift in economic performance.

MBIE's economic narrative, *Growing New Zealand for all*, tells the story of what we think needs to happen for New Zealand to succeed in reaching our economic potential and MBIE's role to deliver this. It is informed by the evidence we have about the conditions for economic growth as set out in *What we know (and don't know) about economic growth in New Zealand*¹.

This economic narrative is part of a suite of strategic documents that helps MBIE to set direction for its advice and to assess its short and medium-term priorities. *What we know (and don't know) about economic growth in New Zealand* provides the evidence base for MBIE's economic narrative. Both documents then inform the *Business Strategy* which identifies the priorities for the coming year. These documents sit alongside other strategic inputs such as environmental scanning work, MBIE's strategic research agenda, and key documents such as the *Statement of Intent* and the *Four Year Plan*.



The primary audience for this document is MBIE staff. The document will also inform conversations with stakeholders to provide them with greater clarity on how MBIE approaches its role in helping to grow New Zealand for all.

The senior leadership team would like to acknowledge the significant contributions made by staff across MBIE and by external stakeholders to the development and revision of this document. This remains a "living" document and will evolve as our knowledge and understanding improves.

¹ MBIE (2016) *What we know (and don't know) about economic growth in New Zealand*, MBIE Working Paper 16/01, August 2016. <http://www.mbie.govt.nz/publications-research/publications/economic-development/What-we-know-and-dont-know-about-economic-growth-full-report.pdf/view>

Contents

Purpose	iii
Contents	v
Executive Summary	vi
1. Growing New Zealand for all	1
2. Dynamic and fair business environment	9
3. Skilled people and innovative firms	17
4. People, sectors and regions	25
5. The built environment.....	31
6. The natural environment	35

Executive Summary

MBIE's purpose is to grow New Zealand for all – to work with our partners to support a better performing economy that delivers a higher standard of living and improved wellbeing for New Zealanders.

This economic narrative tells the story of what we think needs to happen for New Zealand to succeed in reaching our economic potential and MBIE's role to deliver this.

Being a small country, a substantial distance from major world markets presents both challenges and opportunities. It means we have to be very good at what we do to remain competitive. It also means we are an attractive destination for tourists, migrants and investors who bring economic opportunities with them.

We can expect the world to go on changing and evolving. For New Zealand to succeed, we have to improve on what we do now and continue to adapt our capabilities so we are able to take advantage of future opportunities and enhance our resilience.

We play an important role in this process. We have a co-leadership role, alongside the Treasury, on economic matters. We are also the government's lead business facing agency so can provide insights into how markets operate. The breadth of our remit gives us a unique view across a range of economic, regulatory and policy systems. We not only need to ensure each of these systems operates efficiently and effectively but we need to look across the systems to ensure that they are well aligned to achieve the best outcome for New Zealand businesses and households.

We have to be focused on the right things and we need to do what we do well in order to achieve our goal of increasing household incomes by 40% between 2012 and 2025. The economic narrative discusses our focus and activities – grouped into five outcome areas, discussed below.

- 1. More dynamic and fair business environment** – we need market conditions to be supportive of growth for all. The government creates the framework within which market activity occurs and MBIE is one of the agencies that helps to set and enforce those rules across a diverse range of systems. Ensuring the systems operate efficiently and effectively, both individually and collectively, is a priority. There are also other roles we have that can contribute to better business outcomes such as:
 - › supporting consumers through information provision and protection
 - › supporting businesses through education programmes, administering funding options or working with NZTE to attract the right sort of capital
 - › effective procurement and property management
 - › making the most of government data.
- 2. Increased number of highly skilled people and innovative firms** – the effective use of skills, knowledge and capital in firms drives innovation and growth. We expect the interaction between skilled people and innovative firms will be instrumental in achieving growth for all in the future. We need to ensure our labour market settings and the enforcement of those rules reflect the requirements of businesses and workers, and our immigration system brings the best people for New Zealand to prosper. We use a range of levers such as supporting collaboration between academics and businesses and focusing contestable research funds on New Zealand's most pressing research needs to support a well-functioning science and innovation system.

We also work alongside other agencies to support access to international flows of trade, ideas, investment and people to underpin our focus on producing more knowledge intense, high value goods and services, and to grow more businesses of scale.

- 3. More productive and prosperous people, sectors and regions** – Moving to a high-productivity, high-wage economy depends on lifting the performance of all people, sectors and regions. We have work programmes designed to specifically target people, sectors and regions. As part of these work programmes, we have a leadership role in the delivery of the Māori economic development agenda and are working to support Pacific people to reach their potential. We are supporting more productive and knowledge intensive sectors by removing constraints and facilitating opportunities. And we have identified a number of ways in which a regional lens can support region-specific outcomes.
- 4. The built environment better supports a well-functioning economy** – cities are a key engine of economic growth and innovation and they are where the majority of our population live. When they work well, people and businesses can flourish. Housing is a key component of urban life. A focus on ensuring that all contributing markets to the development of housing are operating effectively is the best way of ensuring a responsive supply. We also have a range of responsibilities as regulator to improve building quality and safety. The efficient and timely delivery of infrastructure is an important part of the urban dynamic. We have a role to play in the regulation of some of these key markets like telecommunications, and energy.
- 5. Greater value sustainably derived from the natural environment** – the natural environment underpins much of our economic activity, especially production of primary products and tourism. Natural resources also dominate our energy production with the vast majority of our electricity production coming from renewable sources. While we have some direct responsibilities related to natural resources, such as managing New Zealand's petroleum and mineral resources, we play a supporting role in much of the management of our natural environment. We work with other agencies on issues that are important to our outcomes.

MBIE's economic narrative *Growing New Zealand for all* is a living document. The document will be updated periodically to capture our evolving thinking. The economic narrative is therefore a challenge to all of us to constantly strive to improve and identify new and innovative ways of delivering growth for all.

1. Growing New Zealand for all

MBIE's aim is to grow New Zealand for all

The enhanced wellbeing of New Zealanders is what MBIE and our partner government agencies are working collectively to achieve.

Wellbeing is determined by a broad range of factors including economic factors such as income or GDP, environmental quality, trust, education and health.

Economic success is fundamental to a high quality of life and economic growth delivers higher incomes. Higher incomes allow individuals, families, communities and governments to afford what they value, such as higher quality healthcare or education, improved environmental standards or the ability to consume a wider range of goods and services.

One of the challenges faced by policy-makers is that different groups may have different views about which of the aspects of wellbeing are most important for them. How changes in wellbeing are dispersed across the wider community is also important for assessing the outcomes for different groups.

New Zealand generally performs well on international measures of wellbeing (such as the OECD Better Life index and the Legatum Institute's Global Prosperity Index). Income growth is often a notable drag on our performance on these measures. While income should never be the sole focus, increases in incomes make it possible to sustain performance on other measures of wellbeing such as health and education. For individuals it increases the choices available to them for how they achieve personal wellbeing. MBIE's target is to increase real household income by 40% by 2025 from its 2012 level.

Improving our economic wellbeing

Our economic wellbeing is determined by the performance of the economy – how much we produce and how generated income is distributed. In simple terms this is influenced by the stocks of available resources within the economy and how well they are combined to produce things that people value. These stocks of resources (human capital, natural capital, social capital, physical capital and financial capital) are what the economy draws on to generate income and other flows that make up our wellbeing. Maintaining or growing these stocks is important for future wellbeing. Sustainable improvements in our economic wellbeing will come from:

- › Increased labour force participation – more people working
- › Increased labour productivity – more output per hour worked.

New Zealand already has relatively high labour force participation compared to most other OECD countries. The OECD average for labour force participation in 2015 was 60% whereas in New Zealand over 70% of the working-age population is in some form of employment or looking for work. The participation rate is lower for some age groups, ethnic groups, regions and other categories. While there is the potential to increase the participation of some groups, overall growth in labour force participation will be constrained and may decline in the future as the effects of the ageing population are felt. The focus is on how to increase productivity. How do we produce more with what we have?

What we know (and don't know) about economic growth in New Zealand identified the contributing factors to New Zealand's poor productivity performance:

- › The fact that New Zealand is a small country located large distances from major markets makes it difficult for firms to grow and expand internationally.
- › A larger share of New Zealand jobs are based in industries that tend to have systematically lower levels of productivity.
- › New Zealand has low levels of investment in research and development (R&D).

These factors have also been highlighted by other recent publications focused on understanding our productivity challenge².

While there is little that can be done about New Zealand's physical size and distance from other countries, there are initiatives that can reduce the impact of those challenges and make the most of the opportunities.

Innovation is a key driver of productivity growth. A range of other factors, such as skills development and internationalisation, are also linked with productivity growth.

MBIE's contribution to improved wellbeing

Ultimately progress towards higher productivity is the result of the decisions of people and businesses. However, the regulatory and policy environment that MBIE is responsible for and the way in which it supports those frameworks through enforcement, information provision and other means will influence those decisions.

New Zealand's regulatory and other policy settings are generally seen as supportive of improvements in economic wellbeing. We have strong property rights, flexible labour markets and a dynamic and responsive business population. However, given some of the economic challenges we face in terms of size and distance from major centres of economic activity, we need to ensure our settings are fit-for-purpose and all of our available policy levers are working together to help achieve the outcomes we expect.

The breadth of MBIE's remit provides an opportunity to look across different parts of the economy to ensure there is a common focus and consistent approach.

MBIE's contribution is maximised by ensuring it is clear about its priorities, making links across its areas of responsibility and by operating efficiently. In particular:

- › MBIE is responsible for the provision of a range of front-line services (such as New Zealand's immigration service, consumer protection advice, trading standards services, employment information and much more). Effective and efficient delivery of those functions can reduce costs and complexity for businesses and individuals.
- › MBIE oversees and enforces an extensive set of regulatory processes. Ensuring these processes and the enforcement of them is effective, transparent, unbiased and consistent enables businesses, workers and consumers to engage in economic activity with confidence and ensures the competitive environment is not distorted by non-compliant firms.
- › MBIE plays critical roles in policy development and implementation. MBIE has an opportunity to develop and integrate advice across a number of areas. Having these functions under one roof enables alignment of policy levers which increases the effectiveness and reduces duplication. As well as focussing on the efficiency and effectiveness of individual processes MBIE can also look across a range of systems to ensure they are working harmoniously together.
- › MBIE advises on investments in the economy to act as a catalyst for productivity growth and to encourage firm growth.

² Recent publications include:

- › The Productivity Commission's research paper *Achieving New Zealand's Productivity Potential*, November 2016;
- › Treasury's *He Tirohanga Mokopuna: 2016 Statement on the Long-Term Fiscal Position*, November 2016;
- › Deserres, Yashiro and Boulhol (2014) *An International Perspective on the New Zealand Productivity Paradox*, New Zealand Productivity Commission Working Paper 2014/01

- › MBIE has oversight of ownership interests in a number of business-critical Crown agencies.
- › MBIE's position as the government's leading business-facing agency means we can develop a deep understanding of the challenges and opportunities businesses face.
- › MBIE has a mandate to co-lead the economic policy agenda with the Treasury.

An essential part of the improvement process is monitoring and evaluation of the outcomes.

While MBIE's direct influence is on the decisions that individuals and businesses make, ultimately what we are trying to influence is the broader economic outcomes. Each individual decision adds up to determine an overall economic direction. It is important that MBIE thinks about the cumulative impact of those individual decisions when advising on policy direction and conducting its activity. This is particularly true in the areas of labour markets and housing which are two of the pillars of the broader economy.

How does MBIE's role contribute towards achieving the ultimate goal of increasing real household income?

The MBIE triangle summarises how achieving the MBIE outcomes within the five areas of focus can contribute to meeting the intermediate objectives and ultimately the overall objective of increasing household income by 40% from its 2012 level by 2025.

In setting these goals MBIE has made a series of deliberate choices about what growing New Zealand for all means. The overarching target of increasing real household income by 40% from its 2012 level by 2025 makes it clear that we are not just focussed on growth, but equally concerned that the gains of this growth are realised by New Zealand's households. A target based on median rather than average income ensures that we do not purely focus on achieving growth at the top end of the income distribution – but rather that we move the whole distribution upwards.

Grow NZ for all



In order to achieve the overall household income objective, MBIE aims to shift the economic environment in a way that encourages:

- › more competitive businesses
- › job opportunities for all
- › affordable housing.

MBIE has identified a number of indicators for these objectives and has set target levels for them. While these provide a focus for MBIE's effort, it is important to recognise they are not the only indicators that matter. MBIE uses a range of data to measure different aspects of any issue and looks through different lenses. The ambitious targets provide a clear focus for MBIE's efforts.

More competitive businesses are important for achieving growth and consumer needs. The targets for this objective are doubling labour productivity growth between 2012 and 2025 and increasing exports/GDP ratio to 40%. These two aspects encourage focus on the factors underpinning our productivity performance and international connectedness, both important conditions for growth.

Job opportunities for all recognises not only the contribution of labour force participation to economic growth but also recognises the other aspects of wellbeing that are achieved through work such as enhanced social capital.

Affordable housing recognises the major role that housing plays in the wellbeing of households. The quality, price and location of housing can impact on wellbeing via health and community effects. It can also impact on household incomes through the ability to access the labour market. A lower ratio of housing costs to income will mean households have more of their income to spend on other things that are important to their wellbeing.

What are the features of a successful economy?

Change is inevitable and New Zealand is a small, open economy, affected by global conditions. There are a number of "mega-trends" which influence the way in which economic activity is changing, presenting both challenges and opportunities for countries like New Zealand.

- › **Globalisation** has been a feature of the international environment for decades. Recent geo-political events suggest that attitudes towards globalisation are changing and there is demand for more inclusive distribution of the benefits of growth. While this environment is challenging and is changing the architecture for international trade, this can present opportunities to participate in new markets and global value networks.
- › **Technological change** is likely to increase in pace. It will disrupt many existing markets including labour markets and facilitate significant shifts in the way goods and services are provided.
- › **Demographic shifts** are occurring in most countries due to population ageing. This will continue to bring changes to the size of the workforce relative to the size of the population. Changes to the ethnic diversity of the population will also bring challenges and opportunities.
- › **Urbanisation** is changing the way we view cities as a catalyst for economic activity.
- › **Climate change** and associated mitigation measures has the potential to significantly impact on New Zealand's primary industries and other carbon-emitting firms and sectors.

These changes provide the context which MBIE operates within. MBIE must recognise how these trends affect New Zealand and adapt its response accordingly. New Zealand's distinct economic geography, our small size combined with distance from key international markets, means the scale of the challenges set out above should not be underestimated.

However, the recent geo-political changes underline that at times the challenges of scale and distance can sometimes create opportunities. New Zealand is experiencing strong growth in tourism

and migration as New Zealand is seen as a safe, stable destination. These flows alongside other factors, are underpinning relatively high economic growth at present but they do have implications for other parts of the economy like housing and infrastructure.

To be successful, we need the economy to be able to achieve a sustained lift in per capita incomes. This lift in economic performance could occur in many different ways so it is difficult to predict what the structure of the economy could look like in the future.

The description below identifies the direction of change we can expect for different participants (firms, workers, consumers and government) in the economy. The assumption underpinning this view is that there aren't fundamental shifts in the framework of the economy. There is a risk that some of the trends identified above could result in dramatic shifts in the way goods and services are produced and how the resulting incomes are distributed. The challenge is first of all to identify when changes in the market place are the result of major structural shifts rather than cyclical or other changes. Then to ensure the economic environment is flexible and is able to adapt if significant changes occur.

We would expect that in a successful economy:

■ **Firms will be more productive, innovative and internationally connected**

What this would mean in practice is firms would respond to competitive pressures by innovating or adopting new technology and ways of working. As a result we would expect to see many firms investing in more capital. They would also invest in appropriate levels of training and development for their workers to maximise the output that could come from that capital.

More firms will have stronger international connections. These connections result in an increase in international trade and investment flows over time. They also use those connections to learn and apply better ways of doing things. More firms will either undertake R&D or be connected to the research infrastructure. Stronger international connections will also allow for greater understanding of foreign markets that our firms are looking to operate in.

Over time, this is likely to result in a shift in economic activity from low productivity sectors to higher productivity, knowledge-based industries.

In a successful economy, firms are aware of their responsibilities to workers and consumers and more of them adhere to those requirements. However, there will remain a role for regulators to ensure compliance through a broad range of enforcement and other activities.

In the future, firms will use natural resources in a way that maximises value but in a sustainable way.

■ **People develop skills and participate in the labour market in a way that grows income levels and also supports firm productivity**

A successful future economy will be one where all New Zealanders have the ability to reach their potential. Skill development is a critical part of this process which will also result in improvements to productivity. Workers will share in the benefits of that productivity through increased wages.

Increasing the skills and the productivity of the workforce is one of the foundations for a successful economy. Achieving this outcome will involve a concerted effort from workers, educational institutions and employers.

Workers will adapt and be flexible as the dynamic business environment shifts resources to reflect the needs of the current market-place. Ideally, they will develop skills that are transferable between a range of different sectors and industries.

In a successful economy, we would expect the location choices of firms and workers to reflect the relative amenity of those areas. Ideally, the built environment will evolve to reflect those location choices.

■ Consumers will make informed choices about spending and saving

Consumers are an important part of the competitive environment for firms. Their choices about the goods and services they purchase, helps to reward firms that meet their needs and send signals to improve to those that don't. In the future, we would expect consumers to be more aware of the options available to them and make informed choices.

The digital economy will create an array of new services and/or a range of different ways of delivering existing goods and services. This new environment will create both challenges and opportunities for firms trying to meet the needs of consumers.

Consumers must also make choices about the balance between consuming goods and services now and saving to enable consumption in the future. The accumulation of these saving choices impacts on the domestic capital available for investment.

■ The government will make decisions consistent with a successful economy

The government plays an important role in the successful economy. It is responsible for the regulatory frameworks and institutions that create the building blocks for economic activity. It needs to ensure that those frameworks and institutions provide an environment consistent with the outcomes we are trying to achieve. It also needs to ensure there is adequate enforcement to make sure businesses adhere to the rules of the game. The government also has a range of other tools such as information provision and funding options which it is able to use to influence business dynamics to improve market outcomes.

The government also provides a safety net via the welfare system and other public spending that supports transitions within the economy by enabling businesses and workers to take risks.

The government also participates in the economy through goods and services it provides and purchases. It will provide goods and services in an effective and efficient manner and will use its procurement to encourage innovation and build business experience and capability.

A stable macro-economic environment is also desirable. The government will make decisions consistent with the desired stability though recognising there are many macro factors outside the government's control.

■ Economic activity is more stable and resilient to shocks

A successful economy will be more diversified in terms of the range of goods and services it produces and the markets in which it sells those goods and services. Such diversification will help to insulate the economy from sector-specific or country-specific shocks.

An important part of this diversification will be growth in more knowledge-intensive sectors.

New Zealand will continue to be exposed to the commodity cycle and future economic shocks are inevitable. Regulatory and policy settings, in a successful economy, enable resources to shift in ways that minimise the economic fallout when shocks occur.

Achieving success will require MBIE to work collaboratively

To enable the changes necessary for achieving a successful economy, MBIE has to work collaboratively not only internally across business areas, but also within the public sector and with businesses, consumers and workers across all sectors and regions.

The following chapters discuss the key focus areas within MBIE's remit that we believe are critical for achieving a strong and sustained lift in New Zealand's economic performance. Each chapter matches to the MBIE outcomes identified in the MBIE triangle (see page 3). A more detailed discussion of the priorities in each of these areas is contained in MBIE's Business Strategy:

- › Dynamic and fair business environment (Chapter 2)
- › Skilled people and innovative firms (Chapter 3)
- › People, sectors, regions (Chapter 4)
- › The built environment (Chapter 5)
- › The natural environment (Chapter 6).

2. Dynamic and fair business environment

What is it?

The business environment refers to the context in which firms operate. It includes the global economic, social, technological and demographic trends discussed in the previous chapter as well as domestic factors such as culture, social norms and more formal influences like legislation.

Why is it important?

All of these factors create the market conditions that will affect the decisions that firms make about what they do and how they do it. Getting these factors right is recognised as being critical to a growing and prosperous economy. The dynamism of the market – the churn of businesses entering markets, competing and growing or shrinking - plays an important role in fostering productivity and economic growth. The process of new or better performing firms taking market share from poorly performing firms is an important way of ensuring resources are allocated to more productive uses. New Zealand has relatively high churn of firm exit and entry, although this rate has been falling.

While firm entry is high, supported by good processes to support business creation, the rate of growth after start-up is low by international standards. New Zealand firms are on average smaller than in comparator countries with relatively few large firms. This may reflect the small size of the New Zealand domestic market and the relatively low participation in global value networks with the result that firms are unable to exploit economies of scale.

Recent literature focussing on high-growth firms suggests that a small number of firms are responsible for a greater than proportionate share of employment growth. These firms are predominantly small, young firms. Understanding these dynamics is important to be able to nurture future high-growth firms.

Competition, more broadly, is an essential ingredient of healthy business dynamics. Competition provides incentives for businesses to be more productive and innovative with the aim of improving the welfare of consumers. New Zealand's small size limits the number of businesses that can efficiently operate in markets and our distance from overseas markets increase the costs of imports. Together this means competition may be less intense than it would otherwise have been.

On a number of indicators competition outcomes seem to be worse for New Zealand than other countries. For example, recent evidence shows that competition intensity has not changed in the majority of New Zealand sectors between 2000 and 2010 and competition is generally weaker in service sectors, particularly the finance and insurance sector⁴.

The Productivity Commission identified weak competition as a result of small, insular domestic markets as one of the four key drivers of poor information diffusion and resource reallocation.

⁴ MBIE, 2016, *Competition in New Zealand Industries*. See also Productivity Commission, 2014, *Boosting productivity in the services sector*.

What is MBIE's role?

The dynamic nature of the business environment means businesses have to constantly adapt to new opportunities and challenges to prosper and ultimately grow New Zealand for all.

Government plays an important role in creating the framework within which market activity occurs. In a sense, government sets the rules-of-the-game and is responsible for enforcing the rules to ensure that the market leads to improvements in welfare. MBIE is responsible for 16 regulatory systems. It is tasked with identifying barriers that the government may create to the efficient operation of the market process and with stopping them being created in the first place.

Sometimes, just setting the rules is not enough. There may be situations where the market doesn't produce the expected outcomes. This may occur for a range of reasons including limited competitive pressure (at the extreme this may be monopoly provision) or information barriers that hinder consumer or worker action, or barriers to investment. In these situations, the Government may intervene to improve the outcomes that would otherwise result from the market. MBIE helps the Government do this in a number of ways for example by:

- › supporting consumers through raising awareness of their rights or requiring business to disclose information to inform consumer choice
- › supporting firms through information provision or directly with business assistance measures
- › advising on specific regulation in situations where competition is likely to be limited
- › advising on how to attract the right sort of investment.

Government also operates directly in the market through its procurement. It needs to ensure this is done effectively.

Clear rules-of-the-game that are enforced consistently are vital for markets to deliver good outcomes

Much of MBIE's work supports the efficient and effective operation of markets. If they are well designed, the rules that governments make help markets to work effectively by defining rights and giving people confidence to trade and invest. MBIE is responsible for many of these functions such as company registration through the Companies Office, intellectual property registration via IPONZ and standard setting through Trading Standards.

Some regulation, such as employment standards and workplace health and safety, protects individuals from serious harm.

Poor-quality regulation can have serious negative effects for firms, workers and consumers for example in New Zealand's recent experience with leaky buildings, failing finance companies and the Pike River tragedy. Other effects of poor regulation also include imposing unnecessary economic costs, inhibiting competition, innovation and investment.

New Zealand does well in international comparisons of how well the business environment supports businesses to operate. For example New Zealand came first on the 2016 World Bank Doing Business Index. However, given the dynamic nature of the business environment, MBIE needs to respond to changing circumstances and ensure that those factors it can influence continue to provide a supportive business environment.

MBIE is aware that regulation can impose costs on businesses and consumers. This means there is often a trade-off between the costs and the benefits regulation brings in terms of fairer and more equitable outcomes for business, workers and consumers.

MBIE has extensive regulatory responsibilities

There are 16 regulatory systems that MBIE has regulatory stewardship obligations for under the State Sector Act 1988. A regulatory system comprises the rules (e.g. statutes and regulations), institutions, and practices which combine to achieve a given set of behaviours or outcomes.

Box A – MBIE's 16 regulatory systems

Accident Compensation	Employment relations and standards	Innovation, science and economic development
Building	Energy markets	Intellectual property
Communication Markets	Financial markets	Petroleum and minerals
Competition	Health and Safety at work	Trade, international and standards
Consumer and commercial	Housing and tenancy	
Corporate governance	Immigration	

MBIE has a stewardship role for its regulatory systems

In August 2016, MBIE published its first Regulatory Management Strategy⁵ which sets out what it is doing to meet its stewardship obligations, the emerging trends that will impact on its regulatory systems, how well these systems are currently performing, and what its priorities are.

MBIE's goal is to be a world-leading regulatory steward. There are three dimensions to regulatory stewardship:

- › **An all-of-system view** of each regulatory system and its context
- › **A cross-regulatory systems view** of the regulatory functions that are common across all regulatory systems
- › **A long-term view** to ensure MBIE's regulatory systems are fit-for-purpose today as well as in the future.

MBIE monitoring of Crown entities helps it to take an all-of system view

An all-of-system view means MBIE needs to understand how all the parts of the regulatory system work together and are performing. One of MBIE's roles is to work with Crown agencies and statutory entities, companies, agencies and advisory bodies to ensure they are contributing to the achievement of the system goals. Many of these play important roles in MBIE's regulatory systems and their performance has a significant impact on the performance of the regulatory system.

⁵ <http://www.mbie.govt.nz/about/our-work/roles-and-responsibilities/regulatory-systems-programme/stewardship#RMS>

Building expertise in regulatory functions helps MBIE to take a cross-regulatory systems view

A 'cross-regulatory systems' view means MBIE shares best-practice, knowledge and experiences across its regulatory systems to raise regulatory capability and performance. MBIE's extensive regulatory responsibilities mean it is well placed to play a leadership role across government in developing capability. Some of the initiatives that are underway include:

- › the Government regulatory practice (G-Reg) initiative which is a multi-agency network that collaborates on regulatory practice and capability.
- › the Government Centre for Dispute Resolution, based in MBIE which provides functional leadership and guidance to agencies on best practice approaches for dispute resolution.
- › the MBIE Intelligence Unit (MIU) fulfils a unique integrating function across MBIE, providing a range of decision makers with insights into harm occurring or emerging risks as well as identifying value opportunities.

Assessing the impacts of emerging trends helps MBIE take a long-term view

MBIE's regulatory systems need to adapt over time to respond to emerging trends for example demographic change, technological progress, consumer empowerment or cross-border commerce. New Zealand society is becoming increasingly diverse and different communities may have different understandings and expectations about regulation. It is important for regulators to engage and communicate effectively with a range of cultures in order to ensure regulatory systems achieve the outcomes sought.

An example of how the regulatory system can adapt to opportunities to add value is the New Zealand Space Agency – see below.

Box B – New Zealand Space Agency

The New Zealand Space Agency is the lead government agency for space policy, regulation and economic development relating to space activities in New Zealand. It was set up in April 2016 within MBIE to encourage New Zealand's participation in the global space economy. With New Zealand's first ever rocket launch imminent, the priority has been to implement a regulatory regime – the centre-piece being the Outer Space and High Altitude Activities Bill, which will become law in mid-2017. This will ensure all space activity originating from New Zealand is peaceful, safe, secure and responsible and meets international obligations.

The ability of our regulatory system to adapt to facilitate this new industry has ensured that New Zealand can take advantage of the opportunities that a New Zealand-based space industry provides. Not only are we able to build our capacity and expertise in space activities, but it also provides opportunities to apply the associated advanced technologies to a range of downstream applications as diverse as more reliable telecommunications, more advanced climate data modelling and environmental research and monitoring. These opportunities could feed into other New Zealand high technology businesses, and the development of associated niche hi-tech, high-value manufacturing companies.

MBIE is improving the provision of government services and interactions with businesses

The way Government goes about its provision of services and its interactions with business impacts on business and how they operate. For example, Immigration New Zealand supports two of New Zealand's largest export industries: tourism and export education. Speedy and efficient decision-making are critical for the smooth operation of these industries.

MBIE's role is to improve the efficiency and effectiveness of all of its services and interactions, and there is opportunity to continually improve the services we deliver and monitor. Setting clear objectives for volume, cost and quality of service, and being accountable for this, will help continue to drive improvements and ensure responsiveness to the changing needs of customers. Delivery should reflect the needs of customers, not the structures of government.

MBIE is making it easier for businesses to deal with government

MBIE leads the cross-government partnership, under the Better Public Services Result Area 9: Better for Business, which is making it easier for businesses to deal with government. There are a number of initiatives underway to achieve this. One example is the New Zealand Business Number (NZBN), which provides businesses with a unique identifying number to use when dealing with government and with other businesses to reduce time spent on administration. Another example is the joint government-business accelerator process to jointly develop solutions to main pain points for business.

MBIE uses a range of levers to ensure markets produce better outcomes

In addition to good regulation, the government has a range of other policy levers such as good procurement practice, information provision and various forms of funding.

Role of consumers vital

For competition to work effectively, consumers need to be willing and able to choose between providers. For this to happen, consumers need to be confident and informed. They must have trust in the integrity of the market environment and the firms operating in it.

MBIE, along with other agencies, ensures that firms provide accurate information for consumers to use to make choices and ensure that firms adhere to trading standards. In some situations, like financial advice, some specific information disclosure is required.

Business assistance can reap broader rewards

New Zealand has stable policy settings which enable a positive and supportive business environment. But our lack of large firms combined with small domestic markets and distance from international networks limits competition, hinders the ability of New Zealand firms to grow and makes building overseas connections harder. This means there is a distinct but limited role for government to support businesses to overcome these hurdles. These interventions include:

- › developing capability in entrepreneurs, mentors and investors through intensive accelerator programmes which support the rapid formation of early stage start-ups
- › showcasing entrepreneurs and building international connections through the Prime Minister's Business Scholarships
- › supporting Māori collectives to maximise productivity of their assets through the Māori Innovation Fund
- › lifting management skills of small-medium enterprises and stimulating a private market for business support through the Regional Business Partner programme

- › building skills in exporting and attracting investment through New Zealand Trade and Enterprise (NZTE)
- › stimulating a venture capital market through NZ Venture Investment Fund.

Ensuring high-quality investment

Investment is vital for fuelling growth as it brings the capital businesses need to operate and grow. While more investment is crucial, the skills and knowledge associated with the people who provide that capital is also critical. More investment by businesses can help them to become more productive, grow and export.

Securing better high quality domestic and overseas investment is about maintaining safe, stable financial markets and reducing New Zealand's cost of capital relative to other countries. Reducing the premium on the cost of capital supports New Zealand businesses to invest and grow by lowering the cost of finance. While a multitude of factors influence this premium, MBIE has a role in ensuring stable financial management by improving the functioning of our capital markets. This is both a regulatory function, as discussed above, and an investment attraction function.

While our domestic savings are an important source of funding for investment, New Zealand needs to attract high quality overseas investment to meet our ambitions for growth. New Zealand's rate of business investment is comparable to the OECD median.

MBIE works with New Zealand Trade and Enterprise (NZTE) to attract the right sort of capital and to match investors with the right opportunities. This includes opportunities in the regions, for example, the Regional Growth Programme (see People, Sectors and Regions chapter). MBIE seeks to attract more investors, but also to attract investors with the skills, knowledge and experience to drive change and bring new ideas and practices with them.

MBIE is increasing the value from the business of government

MBIE leads efforts to improve government procurement and property management

The government spends around \$39billion a year on buying goods and services, about 18 per cent of GDP. These goods and services are often critical to the economic and social wellbeing of New Zealanders.

As functional leader for procurement within government, MBIE leads efforts to build procurement capability and improve the practices of government agencies. Given how significant procurement spending is, improvements in the way government agencies procure goods and services can help shape the business environment and bring substantial benefits for firms and the government.

For firms, well-designed and implemented procurement practices encourage innovation, build business experience and capability, and increase business credibility with customers. The potential level of impact varies by market, but is substantial in areas such as infrastructure, health, construction, ICT and education.

In April 2016 MBIE became the functional leader for the management of government property. Agencies are becoming increasingly aware that a good practice approach to property management has a positive impact on their bottom lines, the achievement of strategic objectives and the satisfaction of their staff. Moreover, a standardised approach to property management across government also leads to better engagement with the property industry, including landlords, facilities management providers and other service providers.

There are opportunities to get more value from government data

MBIE has opportunities to increase the value from data held by government by allowing businesses access to this data to create new products and services, through more effective management and governance arrangements.

MBIE's broad scope also provides an opportunity for us to look across a range of related and disparate systems to ensure that they are working together in the most effective way. We need to focus on how we use our data. Among other things, it can help us to understand:

- › more about customer behaviour
- › the response in the market-place to existing policy settings or policy changes
- › how users interact with multiple regulatory systems.

3. Skilled people and innovative firms

What is it?

Skilled people and innovative firms are central to the achievement of our economic goals.

Work done in firms by people is the cornerstone of the economy. This chapter discusses the role of the labour market settings and enforcement, immigration and its link with both formal and informal skills development processes.

This chapter also discusses the process of innovation – one of the most critical factors for future productivity growth – with a focus on how the science system that can support the innovation process.

Why is it important?

The effective use of skills, knowledge and capital in firms drives innovation and growth. This leads to higher productivity, increases in wages and lifts in competitiveness and profitability.

Innovation is a dynamic and uncertain process that leads to firms creating or adapting knowledge to create new products or services or improve existing production or managerial processes. Because ideas can be used over and over again there is the potential for innovation to generate increasing returns on the initial investment. While the conditions for innovation are somewhat uncertain, there is evidence that research and development plays an important role.

People need the skills to maximise their returns from their participation in the labour force. Firms need a skilled workforce to lift performance and profitability and a well-functioning skills and innovation system that helps ensure they have the capability and opportunity to succeed and grow.

The interaction of skilled people and innovative firms provides considerable scope for economic growth. Firm growth provides further job opportunities, and supports productive employment relationships. We also know that skilled people experience better social and economic outcomes, and are more resilient in periods of change.

Many interactions between people and firms in New Zealand take place within an international network of firms, people and the goods and services that they produce. Firms need access to international flows of trade, ideas, investment and people to support the production of more knowledge intensive, high value goods and services.

What is MBIE's role?

MBIE has a role in developing skilled people and innovative firms through our levers and influence in the following areas:

- › **Labour market policies, including skills and migration systems.** MBIE is responsible for providing information about the functioning of the labour market as well as setting a framework for the labour market that helps maximise employment and social and economic outcomes in New Zealand. MBIE advises on and enforces requirements that employers must meet. MBIE plays a direct role in the skills system through its role in setting and administering the immigration system but also influences outcomes through its work focused on specific groups such as youth not in employment, education and training (NEETs).
- › **The science and innovation systems.** MBIE advises the Government on the design and operation of the science system and uses a variety of funding levers to maximise public benefits from the science system. We aim to build a highly dynamic science and innovation

system that enriches New Zealand, making a more visible, measurable contribution to our productivity and wellbeing through excellent science and high-value, knowledge intensive businesses.

- › **Enabling international integration.** MBIE has a role in creating and maintaining appropriate access to international markets for example through immigration settings and assisting with free trade agreement negotiations. MBIE also helps to manage some of the risks through product or labour market standards.

These roles are discussed in more detail in the sections below.

The labour market is a key driver of New Zealand's economic growth

Making the most of people's talent, skills and energy is a key platform for New Zealand's economic success. For most firms, workers are crucial to the firm's performance, and for most people, participating in work will be the main way that they benefit from economic growth. In addition to a source of income, work can provide people with a sense of purpose and develop skills, experience and social connections.

The effective operation of the labour market contributes to MBIE's overarching goal of increasing real median household income by 40 per cent from its 2012 level by 2025 through:

- › more people to participate in the labour force
- › increases in productivity.

Our challenge is to raise productivity while keeping participation high. We also need to ensure that everyone can benefit, through people having jobs that provide good outcomes, and having the ability to move into other suitable employment over time. MBIE's target is to double the rate of labour productivity growth between 2012 and 2025.

We need to ensure our policy and regulatory settings remain fit for purpose

The global trends identified in the introductory chapter (globalisation, technological change, demographic shifts, urbanisation and climate change) have the potential to dramatically affect the nature of work, the workforce and workplaces. We need to ensure that our systems are flexible enough to manage any transitions smoothly.

New Zealand's employment regulation is flexible, facilitating considerable job mobility and different types of employment arrangements while ensuring that workers have the protection of a package of minimum standards. In light of an expected increase in non-standard employment (i.e. not permanent, full-time), we will need to ensure that employees continue to receive appropriate protections. There is also a risk that workers in non-standard employment get left behind when it comes to in-work skill development.

Employment regulation has important connections with welfare, particularly in a future where people may make more transitions between jobs and have periods of unemployment. There is also an overlap with immigration and taxation, in that non-compliance in one area tends to be associated with non-compliance in others. This suggests the potential for greater information sharing and joint enforcement actions, particularly through the Labour Inspectorate and Immigration New Zealand.

Other key regulatory settings include:

- › **Health and safety:** the Government has enacted reform of New Zealand's health and safety system, which is expected to result in fewer workplace injuries and deaths. If implemented successfully, this should lead to greater employee engagement and firm-level productivity improvements.
- › **Accident Compensation:** New Zealand's Accident Compensation scheme plays an important role in preventing and reducing the impact of accidents, and rehabilitating people who have suffered accidents.
- › **Occupational regulation:** MBIE regulates around 40 of the close to 100 regulated occupations in New Zealand. This can be an important protection for consumers, but can also restrict the supply of workers.

The New Zealand economy has been successful at absorbing labour

Workforce participation rates are relatively high in New Zealand. In the December quarter 2016, the overall participation rate was 70.5% up from 68.3% in December 2014. OECD data showed New Zealand's participation rate was the fifth highest among its members in 2015⁵. Our flexible policy and regulatory settings contributed to unemployment remaining lower in New Zealand than many other countries during the global financial crisis. The unemployment rate peaked at 6.7% in September 2012 and in the December 2016 quarter was 5.2%. Despite this improvement in the overall rate, unemployment rates for Māori and Pasifika (11.9% and 9.7% respectively in the December 2016 quarter) remain persistently higher than other groups. MBIE's target is to reduce unemployment below 4%.

Our labour market has also been absorbing an increasing pool of migrant workers, including a significant number of temporary migrants with work rights.

The government has set a challenging target to reduce benefit numbers. This will need welfare and tax settings that incentivise work, and the appropriate use of active labour market policies to overcome barriers to beneficiaries moving into and staying in work.

We have a highly skilled workforce

New Zealand generally performs very well in international comparisons of rates of education and training and our levels of workforce qualifications and basic skills. For example:

- › participation and completion rates in tertiary level education are relatively high
- › workforce literacy and problem solving are high internationally, and numeracy skills are above average
- › the level of training in our workplaces compares well internationally
- › New Zealanders born overseas have higher literacy and numeracy skills than equivalents in any other OECD country.

However, there are also some areas where we could improve our performance:

- › match New Zealand's strong performance in primary education with stronger performance in international tests among secondary schools
- › lift tertiary education attainment and employment outcomes for Māori and Pasifika, as discussed in the Sector and Regions chapter
- › more collaboration on research and development between businesses and higher education institutions
- › make the most productive use of people's skills and qualifications.

To ensure that the labour force of the future contributes to higher productivity, responding to the opportunity to lift performance in the areas above will be important.

⁵ OECD rates are for 15-64 year olds. For this age range, the New Zealand rate is 79.0%.

But we need to find ways to improve labour utilisation and matching

In a well-functioning labour market, employees and employers are able to quickly and efficiently make job matches, and employees are able to move around freely. There will always be some frictions in the labour market – workers will not necessarily be willing or able to immediately change their skill set or location to respond to changes in labour demand, and employers may face competitive pressures that make it difficult for them to easily change the nature of their work or the conditions they offer to fill a labour or skill shortage. There is also evidence of mismatches between skills, qualifications and jobs.

If employees do not have the skills employers want, giving employers more voice in the education and training system may be one way to respond. Alongside this we need to ask what responsibility employers should bear for developing these skills in work. It may also be that some employers would benefit from lifting their management capability and ability to utilise their employees' skills.

Improving labour utilisation and matching requires understanding the perspectives of different labour market agents (workers, employers, sector and regional representatives, government agencies, local government) and coordinating actions. MBIE has been increasingly working in partnership with regions and sectors to identify labour needs and identify agreed solutions to addressing them (e.g. Sector Workforce Engagement Programme, Regional Economic Action Plans). This may require policy and operational solutions targeted to different sectors and regions.

Attracting and selecting migrants with high levels of human capital will continue to be important

We need to continue to ensure that immigration is part of an integrated system response to human capital shortages, alongside welfare and tertiary education. This encourages employers to take responsibility for workforce development. This also provides opportunities to domestic workers, with higher wages or improved working conditions where appropriate, and could incentivise greater capital intensity, innovation and productivity.

With a clear purpose to bring the best people New Zealand needs to prosper, Immigration New Zealand (INZ) plays a critical role in this process. INZ has completed a significant business transformation (Vision 2015), which has shifted from a "bricks and mortar" model to a largely online, distributed one. The next phase, Vision 2020, is putting renewed focus on partnering with industry and business to meet their needs and to ensure migration has positive impacts on communities. Actions are also underway to enhance the security dimensions of immigration flows, and ensuring better outcomes for refugee migrants.

The science and innovation systems create new knowledge and supports businesses to grow

In addition to a skilled workforce, a well-functioning innovation system will lift New Zealand's productivity and build a diversified and resilient economy. Innovation can lead to businesses using new technologies and new processes and offering new products to consumers. It creates new business models and opens up new markets, and it allows New Zealand businesses to compete on the world stage. This process not only benefits businesses through increased productivity and profitability but it also benefits consumers by enabling a greater range of products that better meets their needs. Science and innovation also drive environmental, social and health outcomes.

The private sector is the main channel by which science and innovation yields economic benefits. However, the government has a role in supporting businesses. MBIE is responsible for advice on supporting and building New Zealand's innovation system, including:

- › commercialisation of knowledge for innovation
- › infrastructure to lift innovation potential, including support for incubators and start-ups
- › innovation skills and entrepreneurship
- › global integration and international connections, such as attracting multi-national investment in R&D.

Creating knowledge is a key part of the innovation system

Investment in knowledge-based capital such as science, research and development (R&D), is a key input to the creation of new products and services. Encouraging businesses to conduct more R&D is therefore an important part of MBIE's role in building New Zealand's innovation system. New Zealand has one of the lowest rates of total R&D in the OECD, driven by one of the lowest shares of private R&D. The OECD estimates that New Zealand's weak R&D investment could account for around 40 per cent of the productivity gap between New Zealand and the OECD average (de Serres et al. 2014).

Business expenditure on R&D (BERD) is the R&D performed by business, of which 87% is funded by business itself or overseas. BERD has increased significantly (+52% in real terms between 2008 and 2016) and was 0.64% of GDP in 2016, up from 0.54% of GDP in 2014. The Government has set a goal of increasing business expenditure on research and development to 1% of GDP. New Zealand faces some challenges to achieving this. We have few multi-national companies, which tend to do the most spending on R&D. Attracting more multi-nationals to undertake R&D in New Zealand is one way to address this.

MBIE advises the Government on the design and operation of the science system. Our aim is to increase the value of science to New Zealand.

Co-funding arrangements between government and the private sector help to leverage private sector involvement. Callaghan Innovation administers the R&D Growth Grants, a key mechanism for lifting BERD.

Overtime, more investment in high value science is likely to see more government investment in ideas-led discovery research, to generate new ideas - particularly in ICT, health sciences and the primary sector.

MBIE also administers a range of grants and funds that invest directly in science and innovation in New Zealand. These funds include:

- › contestable research funding, including the Endeavour Fund and the Catalyst Fund
- › Strategic Science Investment Fund
- › National Science Challenges.

The science system must be transparent, high performing and well connected internationally

Strong and easily accessible information is vital to the operation of the science system. This means having information about the performance of people, institutions and systems. This information will be used to guide future investment and drive performance. The recently launched Domain Plan establishes a data infrastructure that can be used for a variety of purposes, including generating performance measures for New Zealand research, and the science and innovation systems. The new annual Science and Innovation System Performance Report supports this approach by beginning to assemble the comprehensive evidence base needed by researchers, investors and other stakeholders.

Science is an international endeavour. Knowledge flows easily across borders and international collaboration is common. New Zealand needs to be able to access the best science from overseas.

Box C – The application of digital technologies can add to innovation, lift skills and make business more resilient, productive and internationally competitive.

Digital technology will play an important role in the development of a prosperous New Zealand economy. The digital technology sector is an important driver of innovation and job and export growth.

MBIE has stewardship of the Digital Economy Programme. The aim of the Programme is to ensure that government as a whole is focusing on the right areas to enable New Zealand to become a leading digital nation – a nation with a thriving digital sector, where our businesses, people, and government are all using digital technology to drive innovation, improve productivity, and enhance the quality of life for all New Zealanders.

MBIE is also directly supporting the growth of a thriving digital sector and technology-enabled digital businesses through a number of initiatives, including coordinating the Digital Technology Skills Forum and extending broadband infrastructure through the second phase of the Ultra-Fast Broadband Programme. We are also focusing on the critical elements of the digital skills eco-system including the pathways into the sector via the education system, the immigration system and professional career development.

Successful economies need to be well integrated internationally

In order to create lasting prosperity New Zealand's economy needs more firms producing more knowledge intense, high value goods and services, and to grow more businesses of scale.

Access to the international flows of trade, ideas, investment and people is a necessary condition to support this shift, because New Zealand does not produce enough of these inputs domestically. Our home market lacks the scale necessary for sustainable growth, and this is exacerbated by our distance from large foreign markets.

Many successful economies and firms are well integrated into "global value networks". These networks are complex cross border interactions between firms where multiple exchanges of value occur both within the network and with end consumers. Inputs from firms in multiple countries now contribute to the final good or service that eventually reaches the consumer. New Zealand is not currently well integrated into these global value networks and ranked lowest out of 38 countries in terms of its participation in global value chains in a recent study (OECD, 2013d, cited in de Serres et al. 2014).

To be successful in the future, we expect that as well as exporting high value goods from New Zealand, our firms will increasingly need to do business via establishing offshore presence. This includes through outward direct investment and partnerships with foreign firms, internet based business models, and provision of services.

As New Zealand firms increasingly participate in the global trading environment, the importance of ensuring that international rules reflect New Zealand's interests also increases.

MBIE can help facilitate the flows of trade, ideas, investment and people within these global networks. Across MBIE we have a number of policy levers which we use in partnership with other agencies to:

- › create and maintain appropriate access (such as immigration settings, negotiating Free Trade Agreements (FTAs), international science strategy and multinational investment attraction)
- › ensure the economy can effectively capture the benefits and increase prosperity (such as enterprise or innovation policy, or providing a dynamic business environment)
- › manage any risks of international connectedness (such as product or labour market standards).

One of the challenges for MBIE and other agencies is ensuring that all of these levers are providing consistent signals to firms to maximise the potential for growth.

4. People, sectors and regions

What is it?

Moving to a high-productivity, high-wage economy depends on lifting the performance of all people, sectors and regions. It also requires the New Zealand economy to diversify and transition to more knowledge and export intensive industries. In this chapter we outline three cross-cutting perspectives on MBIE's work: people, sectors and regions.

Why is it important?

Each of these perspectives provides an additional lens to analyse the economy in a more granular way. This better enables MBIE to:

- › identify where the greatest opportunities and constraints to future economic growth are
- › target effort on groups of people, sectors or regions with the greatest potential or distinct need
- › tailor policy to address people, sectoral or regional-specific contexts to improve effectiveness.

What is MBIE's role?

There are two aspects to MBIE's role with respect to these cross-cutting perspectives:

- › MBIE has work programmes designed to specifically target people, sectors or regions – or sometimes all three such as the Regional Action Plans (see below)
- › MBIE also integrates demographic, sectoral and regional perspectives into our policy development across all of our business.

Leveraging the potential of all people

Demographic trends influence economic activities and performance. New Zealand is beginning to experience the effects of two significant demographic trends: structural ageing which is initially being felt in rural regions, and significant ethnic diversity which is concentrated in urban centres, particularly Auckland. MBIE has begun assessing how these trends may impact national and regional economic growth.

Structural ageing will increase the ratio of people over 65 years old to those of working age and will eventually reduce the working age population thereby creating an additional need to improve long-run labour productivity. It will stimulate growth in some industries (e.g. aged care) and may reduce growth in others. Most studies show that structural ageing is likely to have a net negative impact on national economic growth.

Parts of New Zealand are becoming increasingly ethnically diverse. For example Auckland is one of the world's most ethnically diverse cities with 44 per cent of its workforce born overseas. This creates a very complex environment for MBIE's services and regulatory settings to operate within. It also creates potential dividends (e.g. international connections), which need to be actively leveraged as well as challenges to be managed (e.g. pressure on shared values and institutions). It is important that MBIE's policy advice, regulatory practice and services reflect the changing nature and needs of New Zealand and are designed to leverage potential 'diversity dividends' and address challenges. Our assessments should recognise that common ethnic categories e.g. Māori, Asian and Pacific, are not homogenous groups of people. Very different cultural contexts exist within each broad ethnic group due to individual factors that include place of origin, gender, age and socio-economic status.

Adopting a perspective on people also enables MBIE to identify those groups with significant potential and/or specific challenges in achieving good economic outcomes. When people are unable to reach their full potential it is a loss to individuals, their communities and to New Zealand's

broader capacity for growth. Māori and Pacific people have experienced persistently poor socio-economic outcomes whilst holding significant potential to lift their own and New Zealand's broader outcomes. That potential will only increase as New Zealand gains from proactively investing in the youthful Māori and Pacific population (the median ages of Māori and Pacific populations are 24 and 22 years respectively compared to 41 years for the New Zealand European population). To realise this potential, MBIE has developed targeted programmes for each group which are outlined below.

Facilitating Māori economic development

The Māori economy has huge potential to lift the New Zealand economy, by building the skills of a young and growing population, participating in future focussed industries like the digital economy, improving the productivity of Māori primary sector assets, and supporting improved performance and innovation of Māori firms.

Barriers to leveraging this potential require specific government intervention. Barriers include poorer educational outcomes for Māori compared to most other ethnic groups, poorer economic growth in regions where the Māori population is concentrated and low uptake of business support services by Māori SMEs.

MBIE has a leadership role in the whole of government delivery of the Māori economic development agenda. Together with Te Puni Kōkiri, economic agencies, and working with Māori and the private sector, we implement and monitor He kai kei aku ringa (HKKAR), the Māori economic growth strategy.

We are currently refreshing the HKKAR Strategy and Action Plan and cementing its role as:

1. An overarching strategy to tell the story of Māori economic development across the system including government, whanau and enterprise.
2. A vehicle to stimulate innovation and collaboration to influence government policy and significantly improve Māori economic outcomes.
3. A voice for the economic aspirations of Māori.

The cross-agency Māori economic development work programme will focus on five themes: employment, enterprise, education, rangatahi (Māori youth) and regions. It will involve:

- › improving Māori skills and vocational outcomes to create a highly literate, numerate and adaptive workforce. We are future proofing this by matching skills development to future skills needs for Māori groups.
- › accelerating Māori enterprise performance and innovation, especially exporters and SMEs, by strengthening the business pipeline, capability and connectivity of the enterprise support eco-system. This includes attracting capital to Māori enterprise and investment readiness.
- › improving the productivity of Māori primary sector assets and leveraging opportunities that emerge through the Regional Growth programme so that iwi and Māori can be leaders in regional economic development.
- › supporting rangitahi to define and pursue their economic aspirations.

Supporting Pacific people to reach their potential

MBIE's role in realising the potential of Pacific people is guided by the Pacific Economic Strategy launched in 2015. MBIE seeks to improve Pacific people's involvement and contribution to New Zealand's economy through:

- › increased participation of Pacific people in higher-skilled work in growth industries
- › more Pacific people owning sustainable businesses
- › increased number of Pacific people living in affordable, quality and suitable homes
- › supporting the development of economic institutions within the Pacific region.

MBIE has a role in ensuring that employers are ready for a diverse future workforce. Recent research in South Auckland (The Attitude Gap) has highlighted a significant misalignment of expectations, cultures or values between employers and employees, which can hinder employment opportunities for groups from diverse backgrounds. In partnership with other government agencies we support employers to identify ways to better engage, recruit and retain Pacific people particularly in areas of high Pacific populations and high unemployment rates, such as South Auckland.

MBIE has also been developing networks that support more sustainable Pacific businesses and which help identify new business opportunities that best utilise Pacific community resources and competitive advantage.

The social and economic welfare of New Zealand's domestic Pacific population has a significant ripple effect within the Pacific region through remittances, migration, technology sharing and labour mobility. In this way, MBIE's Pacific Economic Strategy is one component of MBIE's broader work to support the Pacific region's economic development.

Supporting more productive and knowledge intensive sectors

Why knowledge and export intensive sectors are important

MBIE is focussed on improving productivity across all sectors and transitioning to a more knowledge and export intensive economy. Increasing knowledge intensity builds capabilities that allow firms and sectors to move into new and more valuable products and services. These innovations can be more difficult for other (lower-cost) economies to copy, providing the ability to maintain an ongoing comparative advantage in these specialist areas.

Increasing success in international markets is important for several reasons. First, it exposes firms involved to knowledge generated in those markets, enabling them to more quickly put that knowledge to use. Second, it exposes firms to international competition forcing them to continually innovate to stay competitive, adding to overall productivity growth. Finally, it provides firms the opportunity to develop genuine scale which is often not possible when focussed solely on New Zealand's domestic market.

Our scale and distance to markets requires additional government intervention

Alongside government's broad responsibilities that touch all sectors in the economy (discussed earlier), MBIE also has a role in more targeted sector policy. This includes removing constraints and facilitating opportunities in high-value export sectors with strong growth potential.

New Zealand sectors face the challenges of a small domestic market, small firm size and a greater physical distance from other markets compared to other countries. This can require a more active role for government, often at an earlier stage in sector development than that which occurs in other countries.

As illustrated in figure 1, MBIE starts working with targeted sectors by gathering evidence to identify any gaps that warrant government intervention within the broader eco-systems of these industries – particularly industries in early stages of maturity. Producing even simple products and services requires a complex web of knowledge, institutions (such as trade bodies, research establishments, and training institutions), skills, regulatory frameworks and other capabilities for their production.

Figure 1. MBIE's engagement process with a specific sector



MBIE has been working with several high value sectors including ICT, Screen, and Innovative Food. Common activities MBIE undertakes include information provision, addressing skills shortages, R&D support, and facilitating links between industry and government. MBIE also reduces the risks for firms in the early development of new products, for example, through funding open access infrastructure (e.g. the New Zealand Food Innovation Network).

MBIE's activities vary depending on each sector's needs. For example, MBIE is working with the ICT sector to address skills issues while we are focussed on science investment and removing regulatory barriers for the innovative foods sector. Policies need to be designed in order to minimise potential risks such as rent-seeking behaviour or supporting firm activities that may have occurred anyway.

MBIE also targets large mature sectors and lower productivity sectors that provide significant employment and growth opportunities. The policy objective for these sectors is to lift productivity and transition sectors to higher value goods and services. For large sectors of the economy, even a small gain in productivity can have a big impact on New Zealand's overall productivity. For example, MBIE is working with the tourism sector to increase productivity and lift the value derived from international visitors. MBIE is also supporting the tourism sector to address infrastructure pressures in tourism hot spots through targeted funding, addressing seasonality issues and encouraging more tourism in underutilised parts of the country.

MBIE can also take an active role with sectors which contribute to broader economic outcomes. For example MBIE is addressing regulatory, skills and productivity challenges in the construction sector in order to support better functioning housing markets and the Christchurch rebuild.

Regional economic development

The Regional Growth programme

Different regions face different circumstances and have different assets which mean the effectiveness of national policies or the impact of national factors such as the exchange rate varies across regions. National policy frameworks can overlook important characteristics of a particular place. Accordingly, region-specific or regionally tailored policies can be effective in raising wellbeing in those areas.

A number of key international policy organisations (including the OECD) encourage policy makers to use a place-based lens when considering policy problems. The key rationales for doing this are:

- › local actors are often closer to the problems
- › they can see solutions that central government is unable to see, and
- › they have a range of different levers available to them.

The Government's Regional Growth Programme, set up in 2014, uses a place-based approach to increase resilience to shocks and help local people create more employment opportunities and improve their standard of living. The programme identifies and helps leverage short and medium term sectoral growth opportunities. The programme initially focussed on East Coast, Northland, Bay of Plenty, Manawatū-Whanganui and the West Coast and has broadened to work with Taranaki, Canterbury, Southland and Waikato over the last year.

MBIE is working with stakeholders and other government agencies to apply learnings from its experience and sharpen and extend the programme. Extensions include increasing the linkages between economic and social policy, ensuring we effectively leverage opportunities for Māori and potentially increasing our presence in regions. The Regional Growth Initiative Fund has also been established to support the programme.

In order to maximise value at both a regional and a national level, MBIE is facilitating engagement for investment opportunities to ensure that foreign direct investment and high net worth individuals are integrated effectively into the New Zealand economy.

We will also work to ensure that earthquake recovery investments in Kaikoura are designed to stimulate longer-term local economic outcomes.

Auckland and major urban centres

Well-performing cities play a key role driving economic growth nationally. Our major urban centres have been experiencing rapid growth but they are not performing as well as they could. Most critically, Auckland has been experiencing:

- › lower productivity than international comparators
- › high housing costs
- › pockets of under-performance in education, employment and health outcomes (specific employment interventions are discussed in Skills Chapter 3).

The challenges facing our major urban areas are discussed further in the Built Environment chapter.

5. The built environment

What is it?

The built environment includes urban environments, which are crucial hubs of economic activity, as well as the connecting infrastructure such as transport, water, energy and communications.

Why is it important?

The quality of our urban environments and infrastructure directly affects our economic growth potential, the success of our businesses and the wellbeing of the population. Well-functioning urban areas attract talented people, support flourishing communities, and improve productivity and prosperity. Cities are key engines of economic growth and innovation, making them critical to our economic development goals.

One important element of that urban performance is ensuring there is an adequate supply of affordable, quality housing. MBIE's target is to lower the ratio of housing costs to income. It is also recognised that other factors outside MBIE's influence have a direct bearing on housing affordability – such as interest rates. Affordability pressures have direct impacts on people via choices about housing and can also have broader economic impacts such as decisions about job location and/or labour force participation.

Affordability pressures have particularly high impacts on people with lower income – so we also need to consider how affordability impacts different groups and wider economic development goals. For example, access to affordable housing in Auckland is a key issue for Pacific and Māori economic development.

What is MBIE's role?

MBIE has lead responsibilities for housing and construction markets, and the building regulatory system. MBIE's also works alongside our central and local government partner agencies on wider urban policy issues.

In the infrastructure space, MBIE has a lead role in the energy and communications networks through regulation and monitoring of telecommunications, oil and gas security and supply, and electricity markets. MBIE also recognises the importance of other infrastructure elements and works with other agencies to ensure those interests are taken into account.

Improving New Zealand's urban performance

MBIE has recently established an urban performance team and programme to increase our focus on urban issues. MBIE applies an economic development perspective to our urban work, which envisages the city as an integrated social, economic and physical system. We also take into consideration the role good urban design plays in generating agglomeration benefits and environmental and social outcomes.

Work on urban performance in New Zealand is focused particularly on Auckland, given it is projected to account for 60% of New Zealand's long-term population growth.

MBIE also has had a significant role in the rebuilding of Christchurch and the longer-term recovery of the Canterbury economy – for example, involvement in the Christchurch innovation precinct. With the economy in transition and with growth rates declining as the rebuild nears completion, the Canterbury region will remain an important priority.

Housing supply has been a focus of recent urban policy work, particularly given the increase in Auckland house prices. It is important, however, to recognise that housing is just one part of the complex urban eco-system and consideration also needs to be given to the provision of water

infrastructure, transport links and access to amenities. A focus solely on housing supply to the exclusion of the future development of these other matters could lead to poor outcomes. For example, we also need to consider whether the city has adequate future business land supply for high-value industries and whether planned developments provide employment accessibility.

Tackling the issues facing urban centres will require us to take a multi-portfolio approach across MBIE, and across central government, and helping to develop a more collaborative relationship between central and local government in urban areas.

The Productivity Commission points to the challenges of rapid population growth in urban areas and how it can potentially slow productivity in cities. How cities plan for and manage growth and the quality of planning and resource management rules matter for firms and households. MBIE can play a role to support economic and other outcomes through engaging with local government on the levers MBIE and central government can bring to bear on shaping city growth and infrastructure (for example through the refresh of the Auckland Plan) and working with other agencies to provide advice on how to improve planning and resource management.

Focus on improving housing and building markets

The housing and building market faces four connected long-term challenges. All four need to be addressed to ensure housing supply and construction is safe and produces quality buildings:

1 Increasing housing supply

MBIE is working with other agencies on interventions to improve the operation of the housing market. The key focus to date has been enabling more supply, through a range of regulatory reforms including changes to the Resource Management Act, Special Housing Legislation and direction to councils through the National Policy Statement on Urban Development Capacity. MBIE also operates the Crown Land Development Programme and has led the creation of the Housing Infrastructure Fund.

Increasing supply means not just building more houses, but building houses of the right type, in the right locations, and at a range of price points matching demand. Several markets must operate efficiently together to achieve this – failure in any one can negate gains made in the others:

- › land markets – land is available for development, appropriately priced and zoned
- › development markets – there are commercially-attractive opportunities for urban development
- › infrastructure markets – water and transport in particular are provided efficiently and in time to support development
- › construction markets – labour, capital, skills and innovation combine efficiently to deliver efficiently priced and safe buildings and infrastructure.

We are putting increased focus on the efficient operation of these four markets. This includes work with the building sector on workforce requirements and infrastructure needs.

As home ownership rates decline, many households are likely to spend longer periods in the rental market. In line with this, MBIE is implementing Ministers' proposals to improve the quality of rental housing – for example, through regulations to improve insulation and ensure smoke alarms are fitted in rental properties.

2 Smoothing the boom/bust cycle

Building firms can lack incentives to invest in skills, capital and innovation both during a boom (when competitive pressure is weaker) and during a downturn (due to the uncertainty of future work covering costs).

Sound macroeconomic policies help to reduce volatility across the economy, and within the construction sector. MBIE is also working with the sector to give greater certainty on future demand

for construction work and employment (e.g. through the National Construction Pipeline Report and through procurement of construction). Greater certainty of demand, which can also improve productivity, complements the work of the National Infrastructure Unit.

3 Boosting productivity through skills and innovation

New Zealand's construction sector has a large number of small firms and makes extensive use of subcontractors. There is a concern this results in a general reluctance of firms to invest in capital, skills and innovation.

MBIE is looking at how to boost productivity, through means such as creating more transparency around longer-term labour and skills demand and supporting increased uptake of new technologies and practices (e.g. through the National Science Challenge).

4 Improving building quality and safety

As the central building regulator, MBIE is focussed on ensuring the New Zealand building and construction sector is productive, efficient, focussed on quality, customer centred and accountable.

Improving building quality and safety has particular significance for New Zealand's natural disaster resilience, especially earthquake resilience. Following the Kaikoura earthquake of November 2016 MBIE worked closely with our local and central government colleagues to support earthquake response and recovery. We continue to contribute to cross-government work on resilience to future events.

To help the sector overcome those four challenges MBIE has identified four levers for action: people, regulatory and commercial processes, building products and systems, and performance requirements.

A work programme based on these four levers has been developed to enable MBIE to improve the operation of the regulatory system and building safety and quality in a strategic and proactive way.

Ultimately, focussing on the four challenges together have a major impact on the affordability and quality of housing. MBIE is working broadly across government, with local government, developers and the construction industry to address all four.

The importance of infrastructure

Infrastructure investment must anticipate New Zealand's future needs

The infrastructure needs of a modern economy are complex and create many challenges. Technological change and disruption may have significant implications for the future shape of New Zealand's infrastructure. This creates challenges when infrastructure is expensive and takes a long time to build, but relevant technologies can change quickly. For example, energy infrastructure will be affected by any shift towards distributed energy generation and micro-storage (discussed further in chapter 6). The telecommunications infrastructure of the future could take quite different forms depending on the technologies used (e.g. wired vs mobile transmission). The requirement for longer-lived 'bricks and mortar' assets such as transport infrastructure will be influenced by long-term trends such as remote working or public transport options.

These changes present opportunities as well as risks – technological changes may increase the efficiency and effectiveness of future infrastructure. We need to consider how infrastructure networks can remain resilient in the face of natural hazards such as earthquakes and floods, or cope with the long-term effects of climate change. In undertaking its regulatory role, MBIE has to be aware of those challenges and opportunities, and have a flexible approach in dealing with a fast-changing world.

Given the importance of infrastructure to achieving MBIE's outcomes, we will continue to work with and influence relevant central and local government agencies. For example, in Auckland we are working closely with central and local government on transport and housing infrastructure.

6. The natural environment

What is it?

The natural environment includes the land, freshwater and ocean used to produce New Zealand's primary products. It also includes the conservation estate and other natural features which makes New Zealand such an attractive place to live and visit. Our natural resource base also includes petroleum and minerals reserves.

Why is it important?

Natural resources are central to our economic prosperity, especially in our regional economies. A large proportion of New Zealand's export income comes from primary products. New Zealand's highest export-earner, tourism, is also reliant to a large extent on the attractiveness of the natural environment and our "100% Pure" reputation.

As well as underpinning our economy, NZ's natural environment is integral to our sense of national identity and has great cultural and recreational significance. It is an important part of the attractiveness of New Zealand as a destination for migrants.

Natural resources are also the key sources of energy for New Zealand – with the vast majority of our electricity supply coming from renewable sources including hydro-generation, geothermal and wind.

What is MBIE's role?

MBIE plays a supporting role in much of the management of our natural environment. Our key natural resources, such as agricultural land, freshwater or fisheries, are managed by other agencies, and MBIE works with them on a case by case basis as required.

MBIE has two main responsibilities in this space:

- › managing New Zealand's petroleum and mineral resources, ensuring they are developed in a responsible manner to deliver for the benefit of all New Zealanders; and
- › monitoring and advising on electricity, gas and fuel markets. We work to ensure accessible, secure and environmentally responsible energy is delivered to the country's businesses and residents, effectively utilising our renewable advantage.

MBIE also plays a lead role in developing the settings to support the transition to a low-carbon economy while maintaining secure and affordable energy for New Zealanders.

Transition to a low-carbon economy: risks and opportunities

The next decade is critical for lowering greenhouse gas (GHG) emissions in order to reduce climate change. Despite global efforts (such as the recent Paris Agreement), there will still be significant climate change in the future. New Zealand will need to adapt to these impacts. For example, we must factor in the impacts of climate change to planning and policy decisions at all levels. Infrastructure needs to be more resilient to extreme weather events expected to result from climate change.

The climate change challenge is not simply about a transition to lower emissions, but about achieving a smart energy economy and maximising the economic benefits. New technologies, behaviours and business models are bringing opportunities which offer the potential to reduce emissions and further improve energy productivity over time.

These new technologies will also have significant transition issues for existing infrastructure networks. For example, smart metering and solar generation at point-of-use may lead to major change in the economics of electricity generation and distribution.

Given energy is 42 per cent of our emissions, energy policy and climate change are inextricably linked. Our energy intensity has improved – electricity demand is now growing at a slower rate than the economy – and we are getting more of our electricity from renewable sources due to increased geothermal and wind resources. However, energy sector emissions continue to be well above 1990 levels.

Transport remains a particular challenge as transport fuel use contributes to over 40 per cent of energy sector emissions, and is forecast to increase. The development of alternative fuels, modes and vehicle technologies offer the potential for changes in energy demand patterns over time. Fuel switching in industrial heat applications also provides an opportunity to reduce emissions.

Our on-going goal is to balance the transition to a low-carbon economy while maintaining secure and affordable energy for all New Zealanders.

Making the most of our resources during the transition to a low-carbon economy

New Zealand has abundant renewable and non-renewable resources. We have one of the highest (and growing) proportions of renewable electricity generation in the world, and our forestry resources are a potential source of biofuels. We also have a multi-commodity minerals sector with many sedimentary basins known to have working petroleum systems, only one of which is currently in production (Taranaki).

There are significant opportunities to derive more value from our natural resource base while preserving the values New Zealanders place on the natural environment. Providing an efficient, predictable and fair regulatory system, is critical for development. Over the long-term there will be a tension between maximising the value from our carbon-based natural resources while anticipating the transition to a low-carbon economy but while economic opportunities exist and their use is compatible with our goals around transitioning, it is appropriate for New Zealand to take advantage of them.

MBIE (as New Zealand Petroleum and Minerals) has statutory responsibility for managing New Zealand's petroleum and minerals portfolio. We work with other government agencies as required – for example the Ministry for the Environment and Environmental Protection Authority have important policy and regulatory roles relating to petroleum and minerals.

There is strong competition between countries to attract investors and competent operators in the petroleum and minerals sector, and New Zealand is a small player. Regulatory reform in recent years has strengthened the development requirements on the industry and the management of risk (health and safety, and environmental). The key challenge now is to ensure a nimble and responsive system able to respond to shifts in the commodity cycle.

Looking to the future, we will need to consider potential gas supplies (and required infrastructure) as production from the Taranaki basins wind down in the next decade. The pending closure of some oil and gas fields also raises questions of how infrastructure should be decommissioned when no longer in use.

Other natural resources

Biophysical constraints, such as water quality, should influence how growth in some sectors is managed. There are significant stresses on our lands, waters and resource base, and on the regulatory and management systems governing them.

Reforms to freshwater management are currently underway, and their outcomes (particularly in relation to water allocation) will have significant implications for economic development.

Responsibility for natural resources management (other than petroleum and minerals) falls to other agencies – such as local government, Ministry for the Environment and Ministry for Primary Industries. MBIE therefore has an influencing (rather than lead) role. A key focus for the future is to determine which projects we get involved in, and what value we can add to other agencies' work.

