

## An incentives approach for NZ's new Prime Minister

Oliver Hartwich | The New Zealand Initiative | 13 December 2016

For all of John Key's achievements, there is one area in which his administration failed miserably – housing affordability. When he became Prime Minister in 2008, house prices were already high. Towards the end of his second term, housing minister Nick Smith called housing affordability a "challenge" but today there is no denying that New Zealand faces a housing crisis of epic proportions.

Fortunately for Mr Key, he does not have to deal with it any more. To clean up the mess in our property market is now the task of his successor, Bill English. And fortunately for the country, English is perhaps the politician best qualified to deal with this crisis. Better than anyone else in his party, the new Prime Minister understands the issues involved. Besides, he has shown a great personal interest in the area – and a genuine curiosity about novel ways of fixing the problem.

When I started my job at The New Zealand Initiative almost five years ago, one of my first meetings was with Bill English, then the Minister of Finance. It was not the usual polite "meet and greet" but quickly turned to policy questions. I had previously worked on housing policy in London and Sydney and English was interested in hearing about it.

To give a bit of context, at the time there was still a debate whether housing could be fixed with demand-side measures or on the supply side. English was firmly on the supply side, and so was I. It was English, of course, who had tasked the newly established Productivity Commission with a major inquiry into housing affordability which focused heavily on construction costs and planning procedures.

The Minister and the Commission were completely correct in their analyses. There is good evidence that construction costs in New Zealand are somewhat higher than in other jurisdictions. We also know how complex, time-consuming and costly planning procedures can be.

Having said that, I felt there was a crucial factor missing from New Zealand's housing debates, and that was the perspective of local government. In my previous jobs, I had researched how local government and planners respond to financial incentives. My observation was simple – in jurisdictions where local decision-makers stand to gain from new development, they will be much more eager to make it happen. Imagine a council that would keep the GST component on any new development. Or a city that would receive a proportion of personal and corporate income taxes generated in its area. It is easy to imagine how such arrangements would tilt the balance in favour of development. Incidentally, the revenues generated could then be used to offer existing residents a better

deal, too. This could mean better infrastructure and public services, lower taxes or indeed both. In this way, we could turn NIMBYs into IMBYs – people who support local economic growth because it benefits them.

As I laid out my thoughts to the Minister, I was not quite sure whether he thought it was an interesting idea or whether I was from Mars. When he asked me what I would do to restore housing affordability and I responded "I would abolish the rates system and give councils a tax base that fluctuates with economic activity", I sensed that he had probably concluded the latter.

Over the past years, the Initiative has produced report after report showing how such a financial incentivisation of decision-making would work towards growth. We did so for housing where we proposed the GST component to be kept by councils. We made similar recommendations for natural resources where we suggested that local communities should gain from minerals exploration and exploitation. We reiterated the theme in our concept of Special Economic Zones, which Mr English publicly praised as novel policy thinking.

What we have achieved with our work is the growing realisation in policy circles that incentives matter. When we started out five years ago, it was an outlandish idea. Today, it has almost become mainstream. You can find it reflected in the Productivity Commission's recent work, in Local Government New Zealand's advocacy for local government finance reform and, of course, in conversations with parliamentarians from across the political spectrum.

Over the years, English has often spoken at our functions and discussed the incentivisation approach with us. It actually fits neatly into his investment approach philosophy, which he pioneered. In both cases, problems are solved at their roots rather than dealing with symptoms later on.

So there is every reason to hope that under Prime Minister English, we will see an "incentives approach" to kick-start housing development. English has rightly been praised for his thorough, long-term and systematic policy thinking as Minister of Finance. Now that he is responsible not just for the nation's finances but the general direction of policy, this is what we can expect in other areas, too.

If Prime Minister wants to leave his mark on the country, and if he wants to differentiate his government from that of his predecessor, he should focus on housing. A change of focus is desperately needed after years of apathy under the previous administration. And, because of his personal interest and indeed passion for housing reform, English could make this field the hallmark of his premiership.

A legacy of housing affordability would be a historic achievement, and it would transform the lives of millions of New Zealanders. Good luck, Mr Prime Minister.



*Dr Oliver Hartwich is Executive Director of The New Zealand Initiative, the Wellington-based think tank formed by the merger of The New Zealand Business Roundtable and The New Zealand Institute.*

*[www.nzinitiative.org.nz](http://www.nzinitiative.org.nz). Dr Hartwich is a member of PortfolioConstruction Forum's core faculty of leading investment professionals.*

---