Editorial Note

This issue of *Policy Quarterly* is being published on the eve of one of the most important international conferences in recent history. During 7-18 December 2009, thousands of negotiators and observers will gather in the Danish capital, Copenhagen, with the aim of securing a new global agreement on climate change. A new accord is needed for at least three reasons.

First, in accordance with the Kyoto Protocol negotiated in 1997 under the UN Framework Convention on Climate Change (UNFCCC), Annex 1 Parties (i.e. the 'developed countries' of the OECD and the 'transitional' economies of the former Soviet bloc) agreed to limit their gross greenhouse gas emissions during 2008-12. This is known as the first commitment period (CP1). If the 'top-down' Kyoto mechanisms are to be extended for a second commitment period (CP2) (e.g. another five year period – 2013-17), developed countries will need to agree to new legally-binding targets. These are variously referred to as 'responsibility' targets and quantified emission limitation and reduction commitments (QELRCs). Any agreement on CP2 'commitments', and the rules under which such commitments operate, will be required within the next year or so to provide sufficient time to ratify and implement the new arrangements.

Second, although the US signed the Kyoto Protocol, it did not ratify the agreement (and is never likely to do so). Accordingly, it is not bound by any legal obligations during CP1; nor will it be bound by any CP2 agreement under the Protocol. But without the US 'inside the tent', or at least bound by broadly comparable, economy-wide and legally binding emission reductions, other Annex 1 Parties may not be willing to accept new responsibility targets. Canada has already expressed its reluctance to fulfill its legal obligations under CP1, and may join the US in favouring 'actions' rather than Kyoto-type 'commitments'. But if Canada walks away from Kyoto-type mechanisms, there will be pressure for others to follow – including Australia, Japan and New Zealand. This would leave just the EU, Norway, Russia and Switzerland supporting binding responsibility targets. Such an outcome would almost certainly be unacceptable to the wider international community, undermine the carbon market, increase the risk of protectionism and create huge uncertainties for business.

Third, under Kyoto only Annex 1 Parties have responsibility targets; developing countries do not have legally binding commitments to reduce, or even limit, their emissions. While this sharp differentiation between Annex 1 and non-Annex 1 Parties was broadly acceptable in the 1990s, this is no longer the case. For one thing, a simple Annex 1/non-Annex 1 divide is unfair: numerous non-Annex 1 Parties now have per capita incomes well over those of the poorest Annex 1 Parties, particularly those of the former Soviet bloc. For another, restricting the emissions of only Annex 1 Parties (or even an expanded list of developed countries) will not avert dangerous climate change: the emissions of developing countries now exceed those of the developed world. Indeed, China's emissions are higher than those of the US and are rising rapidly – even though its per capita emissions remain low compared with most developed countries.

Moreover, in the absence of a truly global commitment to addressing climate change, firms in developed countries will lobby for concessions from any domestic measures to reduce emissions in order to protect jobs and minimize carbon leakage. New Zealand's recent experience suggests that such lobbying can be highly effective. Any new international agreement, therefore, requires a more sophisticated and comprehensive approach to the limitation and reduction of emissions.

This is why there is now open discussion about replacing Kyoto with a new and more comprehensive agreement under the UNFCCC. Various models are on offer, including the Australian schedules approach (which would extend legally binding mitigation 'commitments' to certain non-Annex 1 Parties) and the draft implementing agreement proposed by the US (which would require all countries, except the poorest, to specify measurable, reportable and verifiable 'actions' rather than agree to 'commitments').

But the problem will be how to craft any new agreement without unraveling key elements of the global policy architecture so painstakingly negotiated between 1997 and 2005, especially the various flexible mechanisms that form the basis of the international carbon market. To complicate matters, it is not yet clear what the US will be able to offer by way of comparable or parallel domestic policy 'actions'. Unless the Congress enacts satisfactory climate change legislation before Copenhagen, US negotiators will be in a weak bargaining position – reduced to offering a patch-work of federal and state regulations of individual sectors (such as constraints on automobile emissions under the Clean Air Act). Will this be enough to secure anything in December other than a very high-level political agreement on broad objectives? And what then of New Zealand's goal of 'rules before commitments'?

With the Copenhagen conference in mind, this issue of *Policy Quarterly* includes three articles on climate change or related matters: first, Peter Wilson outlines why New Zealand should not harmonize its emissions trading scheme with Australia's pending scheme; second, Philippe Boncour and Bruce Burson address the relationship between climate change and migration; and third, Alana Cornforth reviews the implications of social psychology and behavioural economics for the design of environmental policies.

Reflecting the plethora of policy issues currently on the international and national agenda, this issue of *Policy Quarterly* also contains five articles on other important matters: David Bromell discusses the complex and controversial relationship between diversity and democracy; Bob Buckle reflects on the origins and implications of the recent global financial crisis; Mike Reid questions the idea of defining the 'core' services or functions of local government (an idea once promoted by Rodney Hide, the Minister of Local Government, but now, thankfully, abandoned); Len Cook and Robert Hughes advance the case for improving the efficiency and effectiveness of our public services by focusing on the most critical 'value chains'; and Andrew Butcher highlights the need for New Zealand to bridge the gap between its foreign polices and the burgeoning field of international education.

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Peter Wilson[1]

To Harmonise Or Not To Harmonise, Should That Be The Question?
Emissions Trading Schemes
in New Zealand and Australia

An Anzac approach?

The governments of New Zealand and Australia are proposing to implement greenhouse gas emissions trading schemes (ETS) to help drive down carbon pollution within their borders. Although both countries enjoy a political consensus in favour of emissions trading, the Parliament of each country is deeply divided along party political lines about the appropriate design of their respective schemes.

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Following calls from certain sectors of New Zealand industry to harmonise the two schemes, a trans-Tasman working group of New Zealand and Australian officials was established in March 2009 to consider the question of harmonisation. Apparently in advance of this group concluding its work, in September 2009 the New Zealand government announced a series of unilateral amendments to the New Zealand ETS, designed in part to align the New Zealand ETS more closely with Australia's.

This article examines the case for harmonisation – defined as making regulatory requirements or government policies of different jurisdictions identical or at least similar (Leebron, quoted in Quigley, 2003, p.3) – along with the legal and institutional issues that arise. It concludes that the economic case for full harmonisation is not made, although linking the two schemes – allowing emissions units issued by one country to be used to comply with the scheme operated by the other – might provide some economic benefits. Notwithstanding these benefits, the legal and institutional issues involved with linking mean that even that level of harmonisation will be difficult to achieve in the short term, particularly in the midst of contentious political debate occurring on both sides of the Tasman.

Accordingly, I question whether it is the right time to be considering harmonisation, and posit that both countries should focus on designing and implementing their respective schemes first.

The article firstly outlines why Australia and New Zealand are undertaking action to reduce greenhouse gas emissions and what they have done to date. It then summarises the emissions trading schemes proposed in both countries, and in the following section discusses the principles underlying cross-border policy cooperation and applies those principles to emissions trading.

The context: why Australia and New Zealand are both proposing emissions trading schemes

Because greenhouse gases emitted from one point are quickly and evenly mixed through the atmosphere, there is no direct link between local actions (which can incur costs) and local impacts. This means that any benefits of mitigation are always shared globally. This disjuncture between costs and benefits makes climate change a diabolical policy problem (Garnaut, 2003, p.xviii). The world as a whole will be better off if there is significant mitigation of the harmful effects of climate change, but every individual country also has a clear incentive to let others bear the burden of that mitigation, while reaping the benefits.

Overcoming these sorts of diabolical policy problems is difficult and to date the world has not 'solved' the problem of climate change. But we do have some experience in dealing with complex international problems, which suggests that communication and undertakings to share the gains, all undertaken repeatedly, with slow steps forward, building trust and cooperation, are important parts of the process.

When viewed outside the context of a global negotiation, an individual country taking costly mitigation action can seem irrational. It is commonly noted by opponents of mitigation action that New Zealand's small size (accounting for about 0.2% of total greenhouse gas emissions in 2006) means that any contribution that it makes to global mitigation efforts will

be miniscule. While Australia has larger absolute emissions, even it contributes only about 1.45% to the global total of emissions.[2] In comparison, China contributes over 19% of global emissions, and the United States 18.5%. The next largest emitters are Russia, with 5.2%, India at 4.9% and Japan with 3.6%. Australia ranks 17th and New Zealand 57th. Even reducing emissions in both Australia and New Zealand to zero, if taken in isolation would not have any discernable impact on the risks facing the planet. Indeed, combined emissions for the two countries in 2006 equalled less than one half of the increase in global emissions from 2005 to 2006.

But neither Australia nor New Zealand is joining global efforts to address climate change because of the size of its contribution to those efforts. They are joining those efforts because of the judgement that concerted action by the developed world to address this issue is required to induce the developing world to also make an appropriate contribution.

The logic runs like this. The only way to reduce the total concentration of greenhouse gases to prudent levels is for all countries to make a contribution. This is both a matter of maths – not even the biggest emitters, like China and the US, are large enough that their unilateral actions, especially in the short term, will have a significant effect on climate change – and a solution to the free-riding problem. 'All countries' includes the so-called BRIICs (Brazil, Russia, India, Indonesia and China). The only way the BRIICS will agree to this is if the developed world agrees to make major reductions in its level of emissions, first.

This subtle game of bringing the diverse nations of the world together into an agreement that overcomes the incentive to free-ride can be seen in the language of the existing international agreements and the process of negotiating new agreements. The United Nations Framework Convention on Climate Change (the UNFCCC) has as its ultimate

Figure 1: Agriculture dominates in New Zealand, energy in Australia

Source: UNFCCC

New Zealand   European Union   U S A   Australia
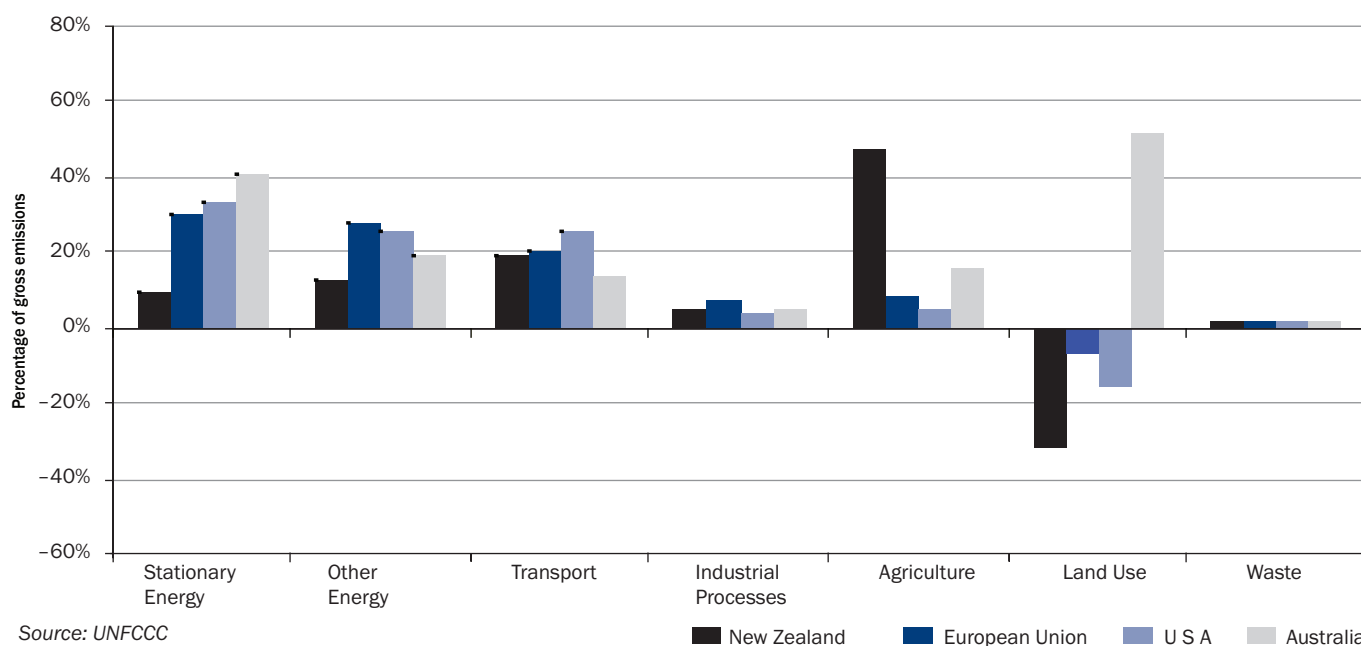
objective the stabilisation of greenhouse gas concentrations in the atmosphere at a (unspecified) level that would prevent dangerous man-made interference with the climate system. To meet this objective, countries agreed to be bound by the principle that they should act on 'the basis of equity and in accordance with their common but differentiated responsibilities and respective capabilities'. They have also explicitly agreed to the principle that developed countries should take the lead in combating climate change. The Bali Action Plan, agreed to at the United Nations climate talks in December 2007, repeats these principles. In deciding to launch action to reach a new international agreement, the parties agreed to consider requiring all developed countries to accept measurable, reportable and verifiable nationally appropriate mitigation commitments and actions. Developing-country parties would be required to undertake less stringent actions.[3]

The reasoning that mitigation policies of developed countries are directed at supporting international negotiations finds expression in the purposes clauses of the legislation establishing the Australian and New Zealand emissions trading schemes.[4]

Patterns of emissions

While there are similarities in the objectives Australia and New Zealand have set for their emissions trading schemes, they start from very different positions when it comes to the nature of emissions in each country.

Figure 1 compares the proportions of emissions coming from different sectors across New Zealand and Australia in 2007, with the European Union and the US included for comparison purposes. For New Zealand, agriculture is by far the largest source of emissions, while land use (principally forestry) offsets a large proportion of our gross emissions. In Australia, stationary energy – principally coal-fired electricity – is the major source, while land use has a variable effect on the total. In 2007, emissions from this sector were high and positive.

The story so far

In ratifying the UNFCCC, both Australia and New Zealand entered into commitments to implement measures to mitigate climate change by addressing man-made emissions within their borders. Despite a number of statements of intent to introduce policy measures, it was not until 2007 that the then New Zealand government introduced, and eventually passed (in September 2008), legislation for an ETS. The current government has introduced legislation that seeks to amend some of the core provisions of the ETS, especially in the early years of the scheme's operation. While a majority of Parliament supported this bill in its first parliamentary stages, to date there has not been a public commitment from a majority of MPs to pass the bill.

Australia has also taken a long time to implement any significant market-based mechanisms to address climate change. A package of 11 bills for the Carbon Pollution Reduction Scheme (CPRS) was passed by the House of Representatives on 4 June 2009. On 13 August the Senate voted against the bills. The government has indicated that it intends to reintroduce the bills before the end of 2009. At the time of writing, it is unclear whether, and in what form, Australia will introduce its scheme.

Emissions trading in Australasia

The idea behind emissions trading is that by setting limits on emissions or any other undesirable activity but allowing individuals to use market mechanisms, technologies and preferences to drive eventual outcomes, the problem being addressed will be corrected in a less costly manner than would be the case with government regulation. The core requirement of each scheme is the same. Each emitter (or deemed emitter in some cases, like miners of natural gas) is required to measure, record and report their emissions. For each tonne of greenhouse gas emissions, they must hold one 'emissions unit'. These units are costly and can be acquired from the government, either at auction or for free as part of a transitional assistance programme; purchased from the market; or earned by undertaking activities that remove gases from the atmosphere.

Table 1 outlines and compares the main provisions of the schemes proposed in Australia and New Zealand. Significant differences are italicised. For New Zealand, two columns are presented: the first sets out the emissions trading legislation as enacted in late 2008, while the second shows the major changes proposed in the Climate Change Response (Moderated Emissions Trading) Amendment Bill.

> In ratifying the UNFCCC, both Australia and New Zealand entered into commitments to implement measures to mitigate climate change by addressing man-made emissions within their borders.

The special role of the Kyoto Protocol

Both Australia and New Zealand have proposed to integrate their schemes, at least to some extent, with the Kyoto Protocol. The Protocol does not require parties to exclusively meet their targets by constraining the level of emissions within their borders. A developed country can meet its target by a combination of:
- reducing net domestic emissions (gross emissions less removals though forestry);[5]
- using an unused part of another country's target (emissions trading);

Table 1: Summary of the Australian and New Zealand schemes

Feature	New Zealand – current act	New Zealand – proposed changes	Australia
Core provisions			
Gases	All greenhouse gases	No change	All greenhouse gases
Sectors (and date of entry)	Stationary energy (2010), transport (2011), industrial processes (2010), waste (2013), *agriculture (2013)*, forestry (2008)	Entry of the stationary energy and industrial processes sectors deferred six months. Entry of transport brought forward six months. Entry of agriculture deferred to 2015	Stationary energy, transport, industrial processes, waste, *fugitive emissions, reforestation* (all 2011). *Consideration of introducing agriculture will take place beginning 2013, with entry not until 2015 at the earliest.*
Estimated coverage	~100% of emissions	No change	~75% of emissions
Number of firms with compliance obligations	200 in energy, transport and industrial processes. Up to 10,000 forestry participants, although participation for those owning forests planted after 1989 is voluntary. If agriculture applies at the farm level, there could be up to 15,000 entities covered.	No change	1,000 entities
Point of obligation	*Mostly upstream. Agriculture could be either upstream (at the processor level) or downstream (farm level).*	No change except in agriculture, where the presumption that point of obligation will be at the processor level is made stronger.	*Mixed upstream and downstream point of obligation*
Openness to international carbon markets	Open to (most) Kyoto units	No change.	Open to (most) Kyoto Units, *eventually*
Price path	*International prices*	*Fixed price, then international prices.*	*Fixed price, then capped price, then international prices*
Transitional assistance			
Assisted sectors	Pre-1990 forest, industrial processes, fishing and agriculture. For industrial processes, there is a trade-exposure test.	Transport and energy sectors to be given a price reduction.	Industrial processes and *stationary energy.* For industrial processes, there is a trade-exposure test.
Type of assistance	Free allocation of units	Transport, industry and energy sectors provided with a 'progressive obligation'. Requirement in the first three years is to surrender one unit for every two tonnes of emissions.	Free allocation of units
Quantum of assistance	Varies from sector to sector, but in all cases total level of assistance to a sector *is fixed, based on historical emissions.*	Move to Australian system.	*Open-ended, depending on future level of emissions.*
Timing of assistance	Generally, phased-out linearly from 2019 (first year of reduced allocation) to 0% in 2030.	Move to Australian system.	Open-ended, but with a 'productivity factor' applying to reduce level of allocation per unit of output.

- financing additional emissions reduction in another developed country (joint implementation); or
- financing emissions reductions in a developing country (the Clean Development Mechanism).

The system of national accounting is based on the issuance and surrender of emissions allowance, collectively called 'Kyoto units'. These units can be transferred between countries via a global registry operated by the United Nations: the International Transactions Log. With some restrictions, some of which apply only during the transitional period, both countries are allowing Kyoto units to be used to meet domestic obligations. One very important implication of this is that over time it is expected that the price of emissions units on both Australia and New Zealand will converge to the price of Kyoto units.

Linking emissions trading schemes

Both the Australian and New Zealand emissions trading schemes contain provisions allowing parties to surrender emissions units issued under another country's scheme for domestic compliance. In the jargon of emissions trading, this is known as 'linking'. In both cases, linking requires the foreign scheme to be approved by the government. The European emissions trading scheme also includes provisions to allow

linking to other schemes, although no moves have been made to do so as yet. Both the Senate and House of Representatives versions of bills to enact an emissions trading scheme in the US contain provisions to enable linking. If two schemes are linked, decisions made about the price and quantity of units issued in one scheme will have material implications for the government operating the other scheme.

How to harmonise

Harmonising regulations normally means that governments work together to design, implement or operate a policy rather than acting alone, although one country copying the provisions of another country's regulations would fit the definition of 'harmonisation'. The implication is that not only are harmonised schemes the same, but they are different from what would have been constructed through unilateral actions.

There is a wide range of ways in which countries can work together to achieve better policy outcomes than if they act alone. Institutional options for facilitating trans-Tasman regulatory cooperation or harmonisation fall into three broad categories:

- mutual, legally-binding commitments enshrined in a bilateral treaty signed by both parties;
- mutual, non-legally-binding commitments;
- unilateral coordination.

Treaties are legally binding, and once in force are difficult to withdraw from or amend. They therefore provide the highest level of certainty that the parties will meet their commitments, and of the likely outcomes of doing so. Due to this fact, treaty negotiation processes can be lengthy and contentious, as the parties strive to specify their commitments with care.

Political cooperation agreements often take the form of a statement of intention or a memorandum of understanding, and set out the parties' agreement to undertake mutual action. Political agreements are not legally binding like treaties, but do carry a lot of political force because they are essentially promises by one government to another. Not being legally binding, they do not provide the level of certainty that treaties provide, but are often less contentious and quicker to negotiate.

Agreeing to take independent but mutually-coordinated action domestically is similar to a political cooperation agreement but does not involve a formal agreement to do so. As such, it relies entirely on the political will of both governments to undertake the agreed actions. Commitments to take mutually-coordinated domestic actions therefore provide the lowest level of certainty that the parties will meet their commitments, but as they reserve for each party maximum flexibility, they are therefore relatively easy commitments to make.

The form of institutional and operational support required to help the parties achieve and maintain their specified commitments depends on the nature of the commitments each party makes to the other. There is a wide range of possible support structures, such as:[6]

- co-management/joint regulation, which may include a joint regulatory body;
- consultation, e.g. regular meetings of ministers and/or officials from both governments;
- reviews of existing laws and regulatory arrangements.

Food regulation in New Zealand and Australia provides an example of joint regulation. The two countries have signed a legally-binding treaty[7] under which both commit to a joint regulatory approach concerning the development of food standards. In order to support these commitments, the Australia and New Zealand Food Regulation Ministerial Council was established. The New Zealand government, the Australian Commonwealth government and each of the Australian state governments have a representative on the council. The council's function is essentially one of governance, with its key functions including policy development and general oversight of the food standards regime. Underneath

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the council sits Food Standards Australia New Zealand (FSANZ), which is an independent statutory agency charged with undertaking the technical work involved in developing food standards. The agency itself has staff in New Zealand and Australia, and is managed by a Board with a mixture of New Zealand and Australian appointments. Once FSANZ develops food standards, the Council agrees to the standards, after which both governments are obliged to ensure the standard is implemented in their countries. Consultation and reviews at both the political and operational level are also built into the process for jointly developing food standards.

An example of 'lower-key' cooperation is the coordination by the two countries with respect to business law. In 2000, and again in 2006, the governments of New Zealand and Australia signed a memorandum of understanding in which both governments agreed to coordinate to harmonise a wide range of laws affecting business. No new bodies have been established to support these efforts, but there are regular meetings between New Zealand and Australian ministers and officials in the relevant fields. One key mechanism for determining whether and what harmonisation should occur is review of existing laws and regulatory processes. Although not binding, this political agreement has resulted in a range

of business law harmonisation (for example, competition and consumer protection laws), and the work programme for continued harmonisation is extensive.

What instrument is required to specify the parties' harmonisation commitments, and the institutional and operational support required to achieve and maintain the agreed levels of harmonisation, depends on the nature and complexity of the harmonisation commitments. The more mutual and detailed the commitments, the more likely a formal instrument to record the parties' commitments will be needed and the greater the need for robust institutional and operational support to achieve and maintain them.

A commitment to develop a single emissions trading scheme, or to link and enable trading of each others' domestic units, would almost certainly require a formal instrument specifying both parties' respective commitments to make the necessary changes to domestic regulatory settings to achieve the level of harmonisation required. In the case of a single scheme, a treaty would almost certainly be required. A 'linking agreement' may take the form of a treaty, although could possibly also be a non-binding political cooperation agreement.

A single scheme would invariably require one or more joint regulatory bodies, involving actors at both the political and operational levels. Linking may not require a formal joint body to be established, but some form of joint institutional cooperation seems inevitable due to the possibility of unilateral action by one party adversely affecting the other. For example, if the schemes were linked with a price cap at a certain price, or without a price cap, then one country's decision to change the capped price or impose a price cap could have significant implications for the other. You would therefore expect to see some constraints on the parties' decision making, at the very least a requirement to consult the other party before making such decisions.

A lower level of commitment, such as independent but mutual adoption of certain design elements, may not require a formal instrument to specify the parties' commitments or much institutional and operational support. Nonetheless,

even with an informal agreement to carry out mutual action, at least some level of ongoing consultation is likely.

In summary, any option involving mutual commitments to harmonise the two schemes requires consideration of what instrument is required to specify the two governments' commitments to each other, and what, if any, institutional and operational support is required to help the parties achieve and maintain their commitments.

Table 2 summarises the relationship between the degrees of harmonisation, the nature of commitments involved at each main level of harmonisation and the institutional support required.

Why harmonise?

The economic case

Neither government has been particularly forthcoming on why harmonisation of emissions trading schemes is being considered, speaking in vague terms about the potential benefits for firms on both sides of the Tasman, including the reduction of transaction costs. The Australia and New Zealand School of Government, in its publication *Arrangements for Facilitating Trans-Tasman Government Institutional Co-operation*, argues that there should be clarity about the objectives being pursued when considering institutional cooperation. It suggests that common objectives that need to be considered include (emphasis added):

- lower business and other compliance costs and technical barriers *to trade*;
- increased policy and regulatory effectiveness *across borders*;
- increased cost effectiveness, policy implementation and enhanced capacity within government;
- increased influence over international policy directions, norms, rules and standards.

It is difficult to see how these objectives are relevant to emissions trading.

While there are some quirks in the international 'rules' regarding emissions sources,[8] emissions trading per se is not a traditional barrier to trade. Emissions trading generally applies neutrally between domestically-consumed and exported goods.

There are three reasons why harmonisation of emissions trading schemes might, at a conceptual level, be desirable. These are: to reduce compliance costs for trans-Tasman firms; to remove any competitive disadvantage by providing a level playing field; and to avoid so called 'leakage', which occurs when an environmental regulation causes the location of production to shift to a jurisdiction without the regulation.

Compliance costs

Reducing compliance costs is one of the often-quoted reasons for many trans-Tasman and other regulatory harmonisation proposals. The argument is that by having one set of compliance rules, rather than two, firms can comply with regulations at lower overall costs. Because both Australia and New Zealand are proposing to place the point of obligation

Table 2: Institutional arrangements

Option	Nature of commitments	Institutional support
Level 3: Full harmonisation (one scheme)	Reciprocal (treaty)	Joint regulatory body (political and operational)
Level 2: Mutual trade of domestic units (linking)	Reciprocal (treaty or political cooperation agreement)	Joint regulation Regular discussions and consultation
Level 1: Voluntary adoption of key design features	Unilateral (possible political cooperation agreement)	Ongoing consultation likely

of their emissions trading schemes high up the production chain, there will be few firms that actually have compliance obligations in either country. Outside forestry and agriculture, the New Zealand Government has estimated that about 200 firms will have compliance obligations. For Australia, the estimate is about 1,000. But I estimate that there will be only about 10 firms with compliance obligations in *both* countries. All of these are large multinational companies with extensive resources and expertise available to them. They are the sorts of firms that tend to be good at compliance.

So, having one set of compliance rules will be of limited benefit. What about the costs? There is no guarantee that any harmonised rules will be simpler than those currently proposed. Neither Australia nor New Zealand have particularly good reputations when it comes to producing low-cost regulatory regimes. And at the risk of sounding parochial – and bearing in mind the role I played in designing the New Zealand emissions trading scheme – I do think that the proposed New Zealand scheme looks simpler to comply with than the Australian system.

I see a real risk that, from the point of view of New Zealand firms without trans-Tasman compliance obligations, harmonisation would lead to greater costs than the counterfactual of a scheme designed and operated domestically. And as I note elsewhere, the process of harmonisation can erect barriers to the swift amendment of rules if improvements are required. I would also be

concerned that harmonisation would mean that the benefits of trans-Tasman regulatory competition would be lost.

Levelling the playing field

The second traditional reason advanced for harmonisation is to remove any competitive disadvantages faced by firms in one country selling into another. A common example is additional health standards applying to imported goods that do not apply to domestically-produced goods. Generally, implementing this sort of policy involves the destination country agreeing to apply the same regulatory provisions or taxes to both domestically-produced and imported goods and services.

In the case of emissions trading, the argument is that if country A puts a price on carbon, but country B does not, firms in country A will be at a disadvantage in both exporting their products to country B and in terms of goods imported into country A from country B. By far the largest impact of emissions trading on firms' costs will be the price of emissions; compliance costs, especially for the sorts of large firms with compliance obligations, are likely to be a small proportion of the price of units, especially once initial set-up and learning costs have been met. So what is needed in the trans-Tasman context for there to be a level playing field is that scheme coverage be the same and that covered firms face the same price of emissions.

Figure 2: Agriculture is much more important in New Zealand

Source: UNFCCC

New Zealand —— Australia ——
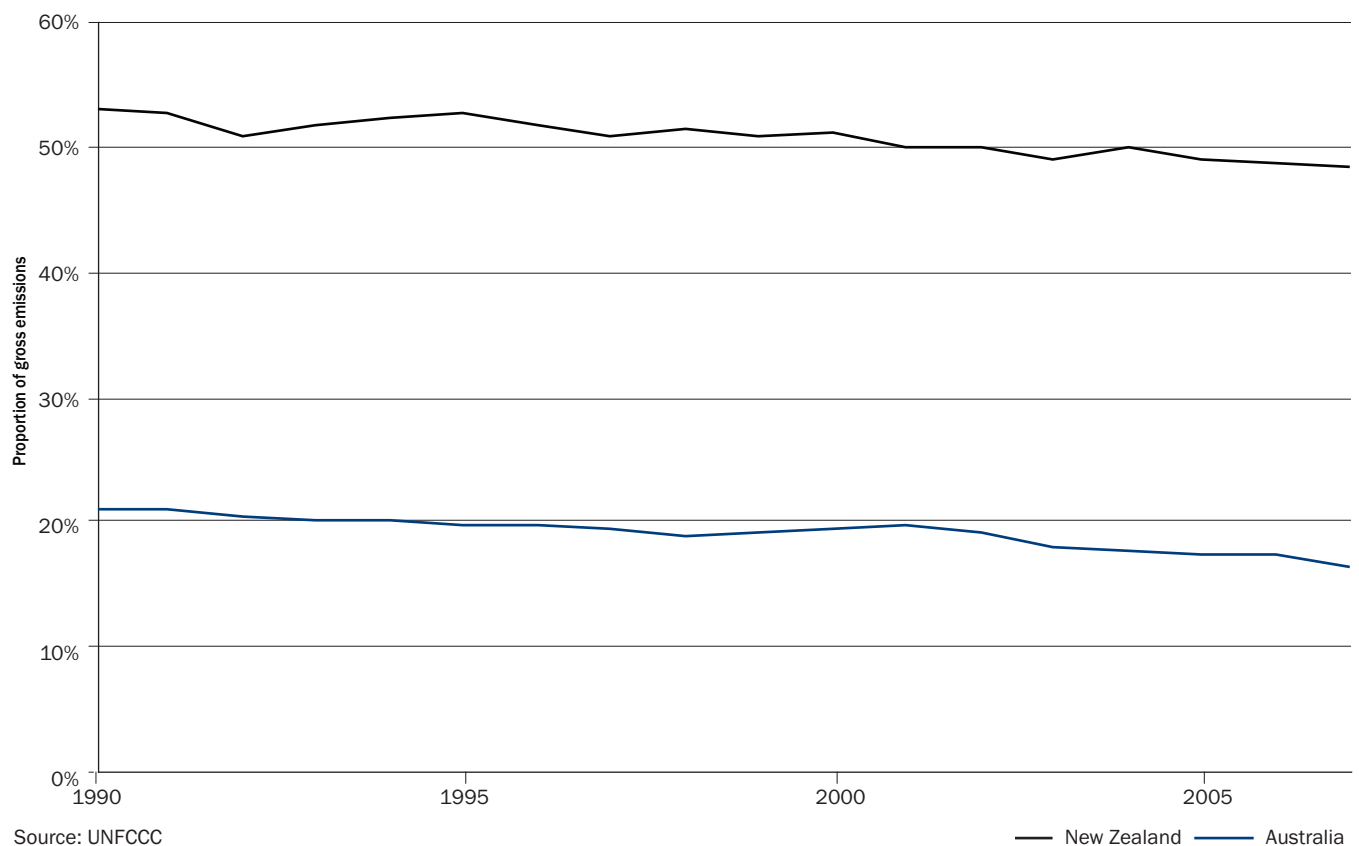
The way the Australian and New Zealand schemes are set up, it will be the 'world price' of emissions units that will drive the price of units in both schemes, although both Australia and New Zealand are proposing to fix (and in the case of Australia, then cap) the prices of units in the initial transitional stages of their scheme.

Coverage is an area where domestic policy choices will have a greater impact on firms. Unilaterally, Australia and New Zealand have both decided to cover transport (liquid fossil fuels), stationary energy and industrial processes. So firms in these sectors – and firms with inputs from these sectors – will be on a similar footing, given the expectation of a common price of emissions in both countries. Agriculture will be the one sector where, under current proposals, there will be an enduring difference in treatment if Australia does not decide to apply its emissions trading scheme to this sector.

With the Parliaments divided along political party lines about scheme design, introducing the possibility of harmonisation is only likely to complicate the domestic political situations. This political difficulty is likely to be greater in New Zealand, ...

In answering a question in Parliament on whether New Zealand was considering excluding agriculture from its emissions trading scheme, the Minister for Climate Change Issues, Nick Smith, recently said:

> Countries are free to implement their own domestic policies to reduce emissions, and most countries for which agriculture contributes a small proportion of their emissions have not included it. That means other sectors of the economy must carry the cost. The problem for New Zealand is that agriculture contributes such a large portion of our emissions that excluding it from our domestic policy puts a higher burden on the rest of the economy.[9]

This problem is illustrated in Figure 2, which shows the proportion of agricultural emissions in each country's total since 1990.

Thus, despite any competitiveness concerns, it seems highly likely, not to mention being highly desirable on environmental and equity grounds, that agriculture will have to be included in the New Zealand emissions trading scheme. This is a good example of where international considerations, while important, are not the only factor in scheme design.

Harmonisation of trans-Tasman emissions trading schemes will have no impact on the competition that Australasian firms face from the rest of the world. It is possible that in time all countries will agree to take action to mitigate emissions, meaning that there is either a price or regulatory constraints on emissions in all countries. But that day is some way in the future. In sum, the case for harmonisation to create a true level playing field looks weak, given the different industrial structures of our two countries and the existence of the rest of the world.

Leakage

The idea that the uneven application of emissions trading schemes between countries can cause shifts in the location of production features prominently in the literature of scheme design. It is a variant of the level playing field argument, but looks at the effects of uneven scheme application on the location of investment. The idea runs like this: if country A puts a price on carbon, but country B does not, firms in country A will have an incentive to shift production to country B. If this happens, country A will have lost employment and GDP and firms will incur relocation costs, but there will be no impact on climate change, since global emissions will stay the same and, as noted above, the location of emissions does not affect their impact on climate change. Even if firms do not relocate plant, because to do so would involve scrapping otherwise economic assets, the argument is that firms will not seek to increase investment in a country with stringent emissions regulations.

The empirical evidence to support the idea that leakage is a real problem is weak.[10] Indeed, it is often pointed out that the European Union, despite having stringent general environment regulations, is the location of significant industrial production, suggesting that firm location is driven by other considerations.

It is hard to see that leakage, if it is a problem, is one that can be addressed by trans-Tasman harmonisation. Even if Australia and New Zealand agreed to have identical and stringent emissions trading schemes, thus removing it from firm decisions about location across the Tasman, the rest of the world is still available as a investment location. It is hard to see why a New Zealand firm that was able to relocate production to Australia couldn't equally relocate to a developing country: mobile capital is, after all, mobile.

The institutional case

I think the economic case for harmonisation is weak, although I acknowledge that that conclusion is based on a number of judgements. But even if a strong economic case for harmonisation could be made, there are significant constraints that make successful harmonisation unlikely in the short term.

In addition to advocating for clarity of objectives when considering trans-Tasman regulatory cooperation, the Australia and New Zealand School of Government also suggests that key judgements need to be made about

the following policy objectives when considering the appropriateness of trans-Tasman cooperation: certainty, influence, flexibility and feasibility. The relative weight and compatibility of these objectives differs in different contexts. In the context of harmonising emissions trading schemes in New Zealand and Australia, the central difficulty is that not all the objectives are compatible or reconcilable.

For instance, a high degree of certainty about each party's commitments and the processes for achieving them will be needed if the two schemes are fully harmonised or linked. As noted above, a treaty or political cooperation agreement would almost certainly be required to specify the commitments and support required to achieve these levels of harmonisation. At the same time, emissions trading schemes are new regulatory instruments in both countries. Because neither scheme is yet fully operational, their likely impacts are not known for certain, although they are expected to have broad-based impacts across the economy. Accordingly, both governments will want to retain significant influence over decision making to ensure flexibility to respond and to adapt the schemes to meet local conditions. But giving both governments influence and maximising flexibility is not consistent with the high degree of certainty that is required to fully harmonise or link the two schemes. It necessarily introduces uncertainty because of the ability of either government to change the rules of the game at a later date.

This ultimately casts a shadow over the feasibility of fully harmonising or linking the two schemes. If it is not possible to provide the degree of certainty required to achieve harmonisation while meeting both governments' needs for influence and flexibility, then embarking on the process of negotiating and signing a treaty or political cooperation agreement may be a futile exercise from the outset. Negotiations could easily become bogged down as the parties seek to reconcile inconsistent and incompatible objectives.

On the other hand, a lower level of coordination – such as independent but mutual alignment of scheme design – may provide the parties with maximum influence and flexibility, but would lack any real certainty about the outcomes going forward. If the goal of harmonisation is to align the schemes to deliver purported economic benefits, then an arrangement whereby scheme design could diverge at any time due to the two governments' ability to make unilateral changes seems to defeat the purpose of the exercise.

The question of feasibility is also important in the context of the political situations in both countries. With the Parliaments divided along political party lines about scheme design, introducing the possibility of harmonisation is only likely to complicate the domestic political situations. This political difficulty is likely to be greater in New Zealand, since New Zealand is more likely to change its scheme design to accommodate the CPRS design than the reverse. Any amendment will involve cost to someone – whether falling on the taxpayer/consumer or polluters – and will therefore provide an opening for opposition to the change. This may

be in the form of opposition from a political party, from affected interest groups, or general public opposition to the prospect of Australian influence over regulatory design in New Zealand.[11] It has already been noted how hard it has been to introduce any form of greenhouse gas regulation in New Zealand. The prospect of harmonisation is only likely to add to the issues that generate opposition, and make the implementation effective regulation harder.

An analysis of the key policy objectives involved when considering harmonisation – certainty, influence, flexibility and feasibility – suggests that even if an economic case for harmonisation could be made, the incompatibility of these objectives in the emissions trading context means that efforts to specify and achieve harmonisation are unlikely to be successful. Furthermore, the issues that any harmonisation efforts may give rise to are only likely to further complicate the already volatile political situations in both countries, which could ultimately threaten each government's chances of introducing effective domestic regulation.

Conclusion

It might seem self-evident that Australia and New Zealand should jointly design and operate their emissions trading schemes, but the analysis presented in this article suggests otherwise. And that is the point: there should be careful analysis of the issue, not a jump to an automatic conclusion.

At the macro level, New Zealand and Australia have independently designed very similar schemes, based on similar policy objectives. The proposed changes recently announced by the New Zealand government move the two schemes even closer together. Both countries are proposing to take costly action to reduce emissions as part of wider global efforts to limit the effects of climate change. Both know that their efforts in isolation will have minimal effect, but they also know that joining with other developed countries to take early action is required to build the truly global cooperation needed.

But the industrial structures of the two countries are quite different, leading to very different emissions profiles. This means that the detailed focus of the two emissions trading schemes need to be different. In New Zealand, the focus needs to be on agriculture, forestry and transport, as these are the three largest sources of emissions. In Australia, stationary energy dominates.

Emissions trading is a relatively new policy instrument. While there are examples of small-scale tradable property rights schemes operating on both sides of the Tasman (commercial fisheries in New Zealand, abalone in Tasmania), neither country has any experience in designing or operating a national-scale scheme with the wide coverage proposed. There is, therefore, a case for policy advisers and decision makers learning from each other as we proceed. There is also increasing international experience on which to draw: the EU has operated a large-scale emissions trading scheme since 2005; the United States has used such a scheme to good effect in combating issues like acid rain. But it is a long step from learning from experience to harmonisation.

Given the complexity of harmonisation and the costs – in terms of both policy resources and future flexibility and sovereignty – I am not convinced that the case for harmonisation has been made, especially in the short term. I believe that while actively learning from each other's experience, New Zealand and Australia should focus their attention on the unilateral implementation of their respective emissions trading schemes and the international climate change negotiations. In time there may be advantages in drawing the schemes closer together, but not now.

In the context of wider trans-Tasman policy development, I think that there are valuable lessons to be taken from considering the costs and benefits of harmonisation of emissions trading. Just because each country has decided to implement the same policy tool does not ipso facto mean that a single, harmonised scheme is required. Policy makers should continue to subject such proposals to detailed scrutiny to ensure that the rhetoric of cooperation does not automatically mask the reality of the good case for separate policy design.

1   This paper is based on a presentation that I gave, together with Alastair Cameron of Buddle Findlay, on 31 July 2009 at a seminar entitled *Emissions Trading – Harmonisation with Australia: Issues and Options*. The seminar was organised by the Institute of Policy Studies and the New Zealand Climate Change Research Institute I would like to thank Alistair for permission to use some of his material in this article. Comments by participants at the seminar and by Jonathan Boston are also gratefully acknowledged. I, of course, remain responsible for all the views in this paper.
2   Data download from the World Resource Institute's climate analysis indicators tool: http://cait.wri.org/.
3   Bali Action Plan, FCCC/CP/2007/6/Add.1.
4   See section 3 of the New Zealand Climate Change Response Act 2002 and clause 3 of the Australian Carbon Pollution Reduction Scheme Bill.
5   Everything to do with Kyoto is complicated and has an acronym. Technically, removals are from 'Land Use, Land Use Change and Forestry', or LULUCF.

6   For an outline of the different kinds of institutional and operational support already used by the governments of New Zealand and Australia see Department of Finance and Administration and Ministry of Economic Development (2007), pp.11-17.
7   'Agreement between the governments of Australia and New Zealand concerning a joint food standards system', at http://www.mfat.govt.nz/Foreign-Relations/Australia/1-CER/0-Reference/0-joint-food-standards.php.
8   For example, under Kyoto rules, all emissions from deforestation are deemed to take place in the country where the trees grew and at the time the trees fell; emissions from fossil fuels are deemed to take place in the country where the fuels are consumed not mined, while emissions from industrial processes are deemed to take place where the goods are produced, not consumed; and emissions from international transport and travel are excluded.
9   Hansard, first session, 2008-09, week 21, vol. 656, p.5753.
10 The Stern Review noted that 'The empirical evidence on trade and location decisions, however, suggests that only a small number of the worst affected sectors have internationally mobile plant and processes' (p.253).
11 In spite of the many examples of trans-Tasman regulatory coordination, there are many examples of New Zealanders' vehement opposition to Australian influence over their domestic decision making. The recent controversy about the mandatory fortification of bread with folic acid is a recent reminder, where public opposition to a joint New Zealand/Australia standard requiring mandatory fortification lead to the New Zealand government abandoning the standard in spite of its agreement with Australia to introduce joint food standards. Similar public opposition to joint New Zealand/Australia regulation derailed the proposal for a joint medicines and therapeutics regime. A key component of the opposition was the belief that New Zealand was ceding its sovereignty over decision making to the Australians.

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Philippe Boncour and Bruce Burson

Climate Change and Migration
in the South Pacific Region:
Policy Perspectives

Introduction

The aim of this article[1] is to outline some of the key issues and themes discussed at the Institute of Policy Studies symposium in July 2009 on 'Climate Change and Migration in the South Pacific Region: policy perspectives'. The linkages between climate change, environmental degradation and migration are manifold and not always clearly perceived.

Moreover, many of the issues they raise are potentially controversial. The focus of the conference was on the possibility of climate change-related migration in the South Pacific, one of the regions of the world predicted to be most affected by the impacts of climate change. The conference used regional examples of situations where adverse environmental

events and processes have already resulted in migration and displacement as a lens through which to consider the wider human mobility and humanitarian issues raised by climate change globally. The conference also considered policies at the national level (e.g., is it possible to achieve a holistic government approach on these matters?) and international level (e.g., why is the humanitarian impact of climate change and more specifically environmentally-induced migration not included in the current United Nations Framework Convention on Climate Change (UNFCCC)?)

To begin with, we wish to clarify our usage of terms in this article. 'Migration' typically describes 'a process of population movement, either across an international border or within a state, encompassing any kind of movement of people, whatever its length, composition and causes, such as (but not limited to) migration of refugees, displaced persons, uprooted people, and economic migrants' (IOM, 2004, p.41;

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see also Kilot, 2004, p.76). Often migration is divided into categories of 'forced' and 'voluntary', but in the context of environmentally-induced migration the line between these groupings becomes blurred. Instead, one may try to imagine a continuum from clear cases of forced migration to clear cases of voluntary migration, with a large 'grey zone' in between (IOM, 2009, p.5). Exceptional cases are those of movement for survival due to imminent or acute environmental disaster, for which the term displacement may be most appropriate (IOM, 2004, p.19).[2] More generally, these and other phenomena related to the movement of people are subsumed under the larger concept of human mobility.

... climate change-related migration raises difficult policy issues related to immigration, development, the environment and humanitarian assistance.

Importantly, no internationally accepted term exists to date for persons moving for environmental reasons. In an effort to capture the complexity and breadth of the phenomenon, the International Organization for Migration (IOM) has advanced the following working definition of environmental migrants:

> Environmental migrants are persons or groups of persons who, predominantly for reasons of sudden or progressive changes in the environment that adversely affect their lives or living conditions, are obliged to leave their homes or choose to do so, either temporarily or permanently, and who move either within their country or abroad. (IOM, 2007; 2008, p.399)

For the purposes of this article, the term climate change-related migration (as a sub-category under the umbrella of environmentally-induced migration) will be employed to describe this new, relatively uncharted territory of migration. The term recognises that climate change *sensu strictu* is unlikely to generate population movements, but rather does so via associated events and processes which affect the relationship between societies and their environment.

The context

To outline the context in which the conference was set, we wish to address three questions around which the different sessions of the conference were organised, namely:

• What are the challenges in integrating migration in the climate change debate?
• Why now?
• Why the South Pacific region?

What are the challenges in integrating migration in the climate change debate?

Until comparatively recently the impact of climate change on migration has remained largely beneath the domestic and international policy radar. This is despite the Intergovernmental Panel on Climate Change (IPCC) noting in its First Assessment Report that 'the gravest effects of climate change may be those on human migration' (IPCC, 1990, p.103). A number of reasons for this can be identified.

First, the causes of climate change-related migration are complex. Environmental factors have long had an impact on global migration flows. Environmental events and processes, both fast- and slow-onset, including cyclones, floods, desertification, soil erosion and changing coast lines, can induce migration. Environmental factors, however, interact with numerous other conditions in places of origin and destination, including levels of development, human rights and conflict, politics and governance, and issues at the individual and household level, such as age and gender. Climate change adds another layer to an already complex nexus between migration and the environment. This makes it difficult to establish clear-cut causal linkages between climate change and migration or to isolate environmental factors as exclusive drivers of any particular migration phenomenon. Given the 'hard evidence'-focused context in which climate change policy generally exists, the lack of reliable data and of unambiguous causalities in this area may have driven a misperception that the possible human mobility and humanitarian consequences of climate change do not constitute a major policy problem. Linked to this is the fact that the consequences of climate change for migration, although predictable in many cases, may not manifest themselves immediately. This may have fostered an impression that, if at all, climate change-related migration is a policy problem of the distant future.

Second, migration, and climate change-related migration even more so, is a truly cross-cutting phenomenon (Morton et al., 2008, p.5). This complexity means that no one policy community can claim exclusive ownership and drive it up the policy agenda. Furthermore, climate change-related migration raises difficult policy issues related to immigration, development, the environment and humanitarian assistance. Successful policy intervention in this area therefore requires policy coordination and a whole-of-government approach that can be difficult to engineer.

Third, with increased economic migration[3] and a rise in the numbers of persons claiming refugee status in the 1990s, migration has increasingly been discussed in security terms (Story, 2005, p.4; Volger, 2002, p.188). In the context of a general 'securitisation trend', the movement of people across borders too has increasingly been seen as a 'security threat'. Similarly, climate change, via the potential of its consequences

to cause violent conflict, has also increasingly been framed in these terms (see, for example, Barnett and Adger, 2007; Brown et al., 2007; Matthew, 2008; Schubert et al., 2008). This may mean that the likelihood of migration being constructed as a positive policy solution in the climate change context may become subordinate to the 'high politics of security' (Brown et al., 2007, p.1154). In other words, migration is seen as part of the problem, not part of a solution. Yet it is beyond any doubt that migration has been an adaptation strategy in the face of environmental degradation and climate change adopted by individuals and sometimes whole communities for millennia (Brown, 2008, p.21).

Why now?
Scientific consensus is crystallising around a realisation that climate change, and more specifically anthropogenic climate change, is real and constitutes a near-term threat. Furthermore, there is a growing recognition that climate change and variability will exacerbate both the sudden and gradual environmental events and processes driving current patterns of migration and displacement. In 2009 the challenges before the international community have come firmly into the political and public consciousness, as the United Nations Climate Change Conference 2009 (COP15) in Copenhagen draws ever nearer. This meeting represents a critical milestone in the efforts to deal with the dangers posed by climate change at national, regional and international level.

However, neither the human mobility implications of climate change nor its broader humanitarian consequences are acknowledged by the UNFCCC or its Kyoto Protocol. This omission is of great concern to the humanitarian community as migration and displacement triggered by climate change cannot be systematically considered and properly addressed by the international community unless they are duly acknowledged within the UNFCCC process.

While the text of the UNFCCC speaks to the mitigation of and adaptation to climate change, the idea that migration represents a potential adaptation strategy has not prominently featured in the context of the UNFCCC. Where adaptation is linked to a particular context, these typically relate to ecological adaptation or planning for adaptation (see UNFCCC, 2007, articles 2, 4(1)(e), 4(1)(b)). There are also few instances in climate change literature which discuss migration as a potential adaptation strategy (see Adger et al., 2007, p.736).[4]

Overall, there is a need for an explicit recognition of the human mobility and humanitarian consequences of climate change in the successor agreement to the Kyoto Protocol. Leaving stark implications of climate change for human mobility, affecting millions of people all over the world, out of the document that will be shaping and guiding the international response to climate change for the years to come would be a major gap. A window of opportunity now

exists to place the issue of human mobility and humanitarian consequences of climate change at the heart of the international policy debate, and we hope that the peoples of the South Pacific can be part of shaping this discussion.

Why the South Pacific region?
The South Pacific is not alone in facing climate change. It will affect all countries in some way at some time. But given the low elevation of many South Pacific states, and their exposure to changing ocean weather patterns, it is likely that this region will feel the effects of climate change before many others. In 2008 alone the region experienced a number of natural disasters of a kind likely to be exacerbated by climate

> Some states which see their territory threatened by climate change and consequent sea-level rise are currently exploring the possibility of purchasing land in other states as a potential long-term solution for their populations.

change. For example, a devastating tropical cyclone (Gene) resulted in substantial damage to agriculture, infrastructure and utilities in Fiji, requiring the Fijian government to provide FJ$1.7 million worth of food rations.[5] Unusually high sea levels and swells have resulted in displacement of persons in Kiribati, Solomon Islands, the Marshall Islands and the Federated States of Micronesia (OCHA, 2008). Salt water intrusion into field and crops and contamination of freshwater aquifers has been reported in Solomon Islands (Webb, 2008, p.3). Low-lying atoll states such as Kiribati and Tuvalu are projected, at a certain threshold level of climate change, to face the risk of being completely overcome by the sea or otherwise rendered uninhabitable.

Some states which see their territory threatened by climate change and consequent sea-level rise are currently exploring the possibility of purchasing land in other states as a potential long-term solution for their populations. With regard to migration, some countries within the region are likely to produce some demand for migration to New Zealand. Indeed, we can already see examples within the region of communities migrating internally to avoid complete inundation by rising sea levels, such as the relocation of 2,600 islanders from the low-lying Carteret Islands to Bougainville, Papua New Guinea (Perry, 2006). These and other population movements in the Federated States of Micronesia and in Vanuatu all point towards a future where migration may become an unavoidable response to climate change for households, communities and even entire nations.

The South Pacific region, therefore, is in the vanguard of regions already having to grapple with the human mobility consequences of adverse events and processes which, if not already caused by climate change, are likely to be exacerbated by climate change in the coming years, as indicated by the IPCC in its Fourth Assessment Report in 2007. Importantly, this cannot be simply dismissed as 'bad luck' due to the 'accident' of one's geographical location. Given the significant anthropogenic nature of current climate change and the inequities in carbon emissions which are at the root of this change, there exists a moral obligation on the part of the international community to face up to these challenges. We believe, therefore, that the time has come to firmly put the issue of migration and displacement at the heart of the debate around the policy responses to climate change. As a region, the South Pacific provides a suitable lens through which to examine wider policy issues raised by migration in the context of climate change.

Some key policy challenges
Understanding the potential scale and patterns of climate change-related migration
The numbers of persons predicted to be at risk of being displaced due to climate change-related environmental events and processes represents something of a wild card in this area. Quite simply, there is no scientifically verified estimate of projected population flows. 'Guesstimates' range from 50 million to 1 billion. The most commonly cited figure is of

It is clear ... that the use of migration as an adaptation strategy is not open to everyone; it depends on resources, information and other social and personal factors.

around 200 million persons displaced by climate change by 2050 (Brown, 2008, p.11, citing Myers, 1993). To put this in perspective, this figure equates to what the IOM currently estimates to be the total number of migrants worldwide.[6] Some estimates have, like much of the climate change debate, a sensationalist element to them which can have negative effects on public and political opinion. This dearth of accurate statistical and substantive information on the possible migratory consequences of climate change impedes our ability to adequately prepare for and comprehensively respond to the humanitarian and protection needs of environmental migrants. The extent to which migration occurs in the coming decades will, in large measure, depend on which of the IPCC's emission scenarios (SRES) comes to pass. We need, as a first step, to obtain an accurate picture as to the potential scale and patterns of climate change-related migration.

It is likely that mass displacement will occur in many parts of the world as a result of sudden-onset events (e.g. storms, cyclones, flooding) made more intense or frequent (or both) as a result of climate change. However, an even greater number of people are likely to migrate because of slow-onset processes, at both early and more advanced stages of environmental degradation (e.g. sea-level rise, coastal erosion, desertification, declining soil fertility). At early stages of environmental degradation, individuals and households may engage in temporary or circular forms of migration, such as seasonal, rural-urban migration. Where environmental degradation is more severe and/or irreversible, resulting migration can require relocation of affected populations either internally or to a third country and may become permanent. Climate change-related migration may take place internally, regionally or internationally. Most empirical research, however, suggests that internal migration, mainly as rural-urban migration, or cross-border movement between neighbouring countries, are likely to be the predominant patterns (see generally Leighton, 2007, 1998).

Key issues in this context include:
- How many people will migrate and where?
- What migration patterns and volumes emerge in response to different environmental stressors?
- How can migration and environment datasets be enhanced and/or harmonised?
- How can household surveys be better utilised?

Understanding the complexity and multi-causality of climate change-related migration
As outlined above, migration decisions are influenced by social, economic and political factors, as well as individual characteristics such as age, gender, education, skills, risk-taking capacity, capacity to face new situations and the like. The extent to which environmental factors determine migration will depend on the underlying adaptive capacities of individuals, communities and countries. There exists a need to better understand how people cope with the 'shocks and stresses' of climate change and climate variability, and, in particular, the extent to which migration forms part of the adaptation strategy (Kniveton et al., 2008, p.37). In this regard, it is important to note that there is a lack of contemporary empirical studies as to how perceptions of climate change have influenced migration decisions made by individuals, households and communities (ibid., p.33). It is clear, however, that the use of migration as an adaptation strategy is not open to everyone; it depends on resources, information and other social and personal factors. Often it is precisely the most vulnerable and the most severely affected who are not in a position to migrate.

More specifically, there may be differentiated gender impacts that must be expressly factored into the policy-making process. In general terms, women are expected to

be particularly vulnerable to impacts of climate change as a result of existing gender inequalities which limit their access to information and decision-making power. This increased vulnerability is also a function of their frequently insecure property rights and access to resources, as well as of their reduced mobility due to caring for children and the elderly in situations of environmental stress (see generally IUCN, 2008, p.57; OHCHR, 2009; UNIFEM, 2008). Additionally, there are regionally specific gender implications (UNDP, 2008). In some Pacific communities (e.g. the Carterets in Papua New Guinea and some outer islands in Yap in the Federated States of Micronesia (cited by Cheryl Anderson in UNDP, 2008)), systems of land management and/or holding are matrilineal. Furthermore, women in the Pacific have traditionally engaged in collecting seafood within in-shore areas. As a result, coastal erosion may affect women differently than men who are traditionally engaged more in deep-sea fishing. In each case, loss of land would have a potentially significant impact on families and communities as a whole, and on gender relations within these communities. It is, however, important not to see Pacific women only as victims of climate change. Women have significant roles in traditional methods of disaster risk reduction, and may also possess valuable knowledge about changes to their physical environment (see generally Campbell, 2006).

The impact of climate change is also likely to be particularly acute for many indigenous communities. Also often having limited access to information and decision-making power, indigenous communities are particularly vulnerable due to their inhabiting of marginal land and reliance on ecosystems and ecosystem services that are susceptible to climate change. There may be disruption to systems of traditional knowledge. For example, in some parts of Solomon Islands livelihoods are already beginning to be affected by changes to wind patterns which are disrupting traditional sources of knowledge around crop planting (ICRC, 2008). Displacement away from traditional places of settlement may involve significant heritage and cultural loss, creating a profound sense of alienation and trauma.

Key issues in this context include:

- What are the causal links between migration, environmental events and processes and climate change and to what extent is the environment the primary driver?
- How do climatic and environmental drivers interact with social, political and economic motivations for migration?
- What are the gendered impacts of climate change and how do they affect migration?
- What may be the impact of climate change on indigenous persons and communities?

Managing climate change-related migration

In view of the variegated and complex challenges at hand, migration management responses to impacts of climate change and environmental degradation on migration and displacement must operate on several tracks. Firstly, given the environmental scenarios expected to arise with climate change in the future, the effectiveness of humanitarian response mechanisms to displacement and its negative impacts needs to be reinforced as much as possible. In addition to that, proactive approaches, in terms of preparedness and disaster risk reduction, must become a priority.

Secondly, while migration is still predominantly seen as a worst-case scenario, and there are indubitably cases where this holds true, migration should also be recognised as an adaption strategy. In fact, attempts to stem migration at all cost may increase rather than decrease people's vulnerability to environmental pressures. If it is accepted that migration is a coping strategy adopted by at least some persons or communities in the face of environmental degradation, it is in our view at least open to serious debate as to whether migration, in the context of climate change, should be characterised as solely a failure of adaptation. Whether this is so will depend largely on the point at which migration takes place in relation to the underlying environmental event or process, and what other non-migratory options (if any) are available. Regardless, there is room to increase the adaptive capacities of individuals, households and communities. Appropriate policies are needed to facilitate migration as an

> ... attempts to stem migration at all cost may increase rather than decrease people's vulnerability to environmental pressures.

adaptation in and of itself, while simultaneously trying to limit instances of forced migration. The role of sustainable development is crucial in this equation. The developmental basis of communities and countries is decisive for any national or regional policies on adaptation to climate change (including the National Adaptation Programme of Action created within the UNFCCC process) and on migration. Migration itself can be mobilised as an adaptation or development strategy, for example where migrant remittances contribute to income diversification for households otherwise relying on diminishing ecosystem services.

More globally, other questions that arise in this context include whether potential risk linked to climate change becomes a factor in national-level migration policy making. If so, what weight should it be given? Can seasonal or other time-bound policies be implemented? Would this be effective considering the long timeframe needed to reverse climatic processes such as desertification and sea-level rise?

Key issues in this context include:

- What policies and initiatives currently exist to address

internal and international migration, from prevention and mitigation policies to return and reintegration?

- What lessons can be learned from existing government responses?
- How can we reduce vulnerability to disaster-induced displacement?
- How can migration be used as part of adaptation strategies?
- How can capacity be built to implement such policies?

Finding workable definitions and solutions under international law

As noted in the introduction, people migrating for environmental reasons do not fall squarely within any one category of 'forced' or 'voluntary' migration, and as such, they also do not fit neatly into the categories provided by the existing international legal framework. Terms such as 'environmental refugee' (El-Hinnawi, 1985, p.4) or 'climate change refugee' have gained much popular currency, but do not have any legal basis in international refugee law.[7] Moreover, there is consensus among concerned agencies, including the Office of the United Nations High Commissioner for Refugees (UNHCR), that their use is to be avoided as these terms are misleading and could potentially undermine the international legal regime for the protection of convention refugees (IOM, 2009, pp.4-5; UNHCR, 2008, p.7).[8] It is largely for this reason that the IOM proposes the working definition of 'environmental migrants'.

Definitions matter as they determine entitlement to rights and establish the threshold for accessing any protection regime (Dun and Gemenne, 2008, p.11). Should protection be limited to situations of forced migration or displacement? But given the complexity of the task of deciding, hard and fast, what constitutes 'forced migration' in the context of climate change, is this realistic and practicable, or will it inevitably leave many without rights and protection?

The situation of those migrating or displaced due to environmental factors raises significant and complex issues of international law. Particular challenges arise in the context of shrinking or disappearing states – a phenomenon predicted under some scenarios to manifest in the South Pacific. The following are but a few examples of the existing international legal concepts and instruments and some associated problems which may provide guidance to policy makers:

Human rights. There is little doubt that climate change events and processes will have an impact on human rights in different ways (see generally OHCHR, 2009 and International Council on Human Rights Policy, 2008). Respect for human rights must be an integral part of any policy response to the migration and displacement consequences of climate change, no matter how the motivations for movement are defined. The work of treaty-monitoring bodies has meant that the content of the civil and political, and economic, social and cultural rights recognised under binding multilateral treaties is better understood and an expanding set of standards has been developed to guide rights-sensitive policy making. The potential for existing international human rights,

humanitarian and/or refugee law to offer protection to the rights of those migrating or displaced due to climate change needs to be fully explored.

Statelessness. The international law regime on statelessness[9] is designed to deal with issues of deprivation of nationality following state succession or conflict of nationality law. It has not been designed to deal with questions arising where no successor state exists and the predecessor state has disappeared, as may occur in relation to some small island states. In the context of climate change, does the law require that all or just the habitable parts of the territory disappear?[10] If these states are declared to continue to exist in some legal sense, their populations will not be de jure stateless, to which the international regime largely responds. Their lack of an effective nationality means they may well be considered de facto stateless persons, for whom the protection regime is weaker.

Self-determination. Complete loss of territory will have a significant impact on the rights of the affected peoples to self-determination,[11] which has internal and external aspects (Joseph et al., 2004, p.146; Nowak, 1993, p.22). The internal aspects relate to freedom to pursue economic, social and cultural development, and include participation in political processes. The external aspects relate to freedom from foreign domination and the right of peoples to freely determine their political status and place in the international community. While some aspects of internal self-determination can be accommodated through the democratic process of the host country and its existing obligations under international human rights law,[12] how will these rights survive in full with the complete loss of territory without sovereignty being established over other territory? Similarly, how can displaced peoples exercise their right to freely dispose of their natural resources, including maritime resources?[13] Finally, cultural identity is intimately bound up with particular territory, the loss of which is likely to pose a challenge for the protection of cultural development.

Internal displacement. The Guiding Principles on Internal Displacement, although technically a non-binding, soft-law document, have been influential in shaping how states respond to the predicament of the internally displaced.[14] Importantly, the Guiding Principles have been one source of inspiration behind the Draft African Union Kampala Convention on Internally Displaced Persons, which shows how soft-law instruments can, in time, solidify into hard-law instruments.[15] 'Hard-law' policy instruments may be not be attractive to states, particularly when the potential scale of the obligations assumed is unknown. A 'soft-law track', following 'framework' and 'protocol' approach, may the most workable route to ensure the rights and protection of those migrating or displaced due to environmental factors.

Key issues in this context include:

- What rights do environmental migrants have? How can those migrating or displaced for environmental reasons be best protected?
- What are the definitions and concepts needed and do

they already exist under international law?

• What are the strengths and limitations of existing definitions under international law; how can they be improved?

• Does calling those displaced in this context 'refugees' weaken its currency or does a failure to do so weaken the case for their legitimate claims for protection?

• What is the role of hard-law versus soft-law instruments in this debate?

Conclusion

Having reviewed some of the critical issues, how best, then, to ensure effective and equitable responsibility-sharing in respect of climate change-related migration? One of the most significant obstacles that had to be overcome to secure the UNFCCC was the negotiations involved in reconciling divergent state interests (see Bodansky, 1993, pp.475-7). It seems clear from this experience that trying to create a global binding agreement may not be the best, or at the very least the most feasible, course. It must also be open to debate whether a regional approach is the best one in terms of reaching some international agreement on climate change-related migration. What, we ask, does 'region' mean in this context, and how might different actors within a region share responsibility for the issue? More fundamentally, given the truly global nature of climate change and the historical provenance of current greenhouse gas (GHG) emissions, is it appropriate or fair to take a regional approach? At the same time, it may be possible to draw upon existing regionally-situated arrangements of inter-communal and inter-island cooperation in the wake of natural disasters (see Campbell, 2006, p.23).

A fundamental issue to consider is whether it is desirable to frame this issue in such zero-sum terms. Would a hybrid model involving global, regional and, importantly, bilateral features perhaps be better suited? While the most effective burden-sharing arrangements are likely to occur at the regional level, the fact that all states will, to some extent, be affected by climate change means that, ideally, the agreement should also contain an element of global management. Also, the South Pacific states are not individually or collectively responsible for the current build-up of dangerous atmospheric GHG levels.

To conclude: it is, in our view, vitally important that in seeking to find policy solutions to an issue of global importance the bilateral dimension is not overlooked. It is individual states which, in the exercise of their own sovereign rights and taking into account historical, cultural and other ties, will have to decide the contours of their policy response to climate change-related migration. Bilateral state cooperation is an important feature of contemporary global migration management and must be enhanced in this particular context. Nevertheless, to be truly effective and equitable, such bilateral arrangements must be informed and guided by relevant regional and global arrangements and processes. In particular, they must be guided by the UNFCCC and a successor agreement to the Kyoto Protocol, in which we hope to see the human mobility implications and humanitarian consequences of climate change expressly acknowledged, and which together will guide the overarching political approach and mechanisms for practical implementation of relevant programmes to assist the affected populations.

We believe that by disaggregating the issues of 'who goes where and when?' and 'who pays?' while aligning them in an interconnected and mutually-reinforcing series of global, regional and bilateral responses under the umbrella of the UNFCCC, it is possible to envisage responsibility-sharing arrangements with variable but broadly balanced commitments and responsibilities.

2 Displacement is defined as a forced removal of a person from his/her home or country, often due to armed conflict or natural disasters.

3 Economic migrants are defined as persons leaving their habitual place of residence to settle outside his/her country of origin in order to improve his/her quality of life (IOM, 2004, p.21).

4 In many other instances it is not acknowledged or explored in any detail. For example, discussing small island developing states, a recent report by the UNFCCC secretariat notes that the habitability and thus sovereignty of some states are threatened due to reduction in island size or complete inundation. However, this stark vulnerability is not separated out from other vulnerabilities of a lesser order of magnitude (UNFCCC, 2007, p.25). See also UNFCCC, 2007, p.42 noting that migration might result, but the profound policy issues raised are simply not dealt with.

5 $1.7 million for tropical cyclone Gene rehabilitation (Relief Web: Fiji, 12 February 2008, http://www.reliefweb.int/rw/dbc.nsf/doc104?OpenForm&rc=5&cc=fji).

6 See http://www.iom.it/jahia/Jahia/about-migration/facts-and-figures/global-estimates-and-trends.

7 Note, however, that there may be exceptional cases in which environmental factors combine with discriminatory modes of governance and constitute persecution. See here Burson (2008).

8 Furthermore, regional instruments such as the 1969 AU/OAU Convention Governing the Specific Aspects of Refugee Problems in Africa and the 1984 Cartagena Declaration on Refugees have expanded refugee definitions covering 'events seriously disturbing public order'. While they were not intended to cover displacement as a result of natural disasters per se (see, e.g., Epsiell at al., 1990, p.96; Cuellar et al., 1991, p.493; Muzenda, 1995, p.51), they may provide some impetus for further progressive regional interpretation of the refugee definition.

9 The primary international instruments are the 1930 Hague Convention, the 1954 Convention relating to the Status of Stateless Persons and the 1961 Convention on the Reduction of Statelessness. The principles underlying these instruments are supported by provisions in other treaties, such as the 1957 Convention on the Nationality of Married Women, the 1979 Convention on the Elimination of All Forms of Discrimination Against Women and the 1989 Convention on the Rights of the Child. See also the 1997 European Convention on Nationality.

10 The best-known formulation of the basic criteria for 'statehood' includes criteria such as the existence of a defined territory and a permanent population. See Crawford, 1979, p.36; Grant, 1999, p.5.

11 Article 1(1) of the ICCPR and ICESCR: 'all peoples have the right to freely determine their political status and freely pursue their economic, social and cultural development'.

12 In particular, the ICCPR and ICESCR.

13 See article 1(2) of ICCPR and ICESCR. As Paskal (2007, p.5) asks, 'Does this require Tuvalu, for example, to tether a boat to its former island and keep a few people there to continue to claim these rights?'

14 E/CN.4/1998/53/Add.2: 'persons or groups of persons who have been forced or obliged to flee or to leave their homes or places of habitual residence, in particular as a result of or in order to avoid the effects of armed conflict, situations of generalized violence, violations of human rights or natural or human-made disasters, and who have not crossed an internationally recognized State border'. This definition could foreseeably cover all those forcibly displaced within their country due to the effects of climate change.

15 Similarly, the Cartagena Declaration was the product of a colloquium attended by experts and representatives from 10 Central American governments and, although strictly non-binding, it has been influential in setting policy in the region.

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Alana Cornforth

Behaviour Change: Insights for Environmental Policy Making from Social Psychology and Behavioural Economics

This paper surveys research on behaviour change and identifies ways that social psychology and behavioural economics can assist with environmental policy making. By understanding why and how people make decisions – and how decisions are affected by framing, habits, cognitive biases, and risk perception and interpretation – we can design policies that are more effective, less costly and more acceptable to the public.

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Neoclassical economic theory

Environmental policy making based solely on neoclassical economic theory is insufficient, and sometimes totally misguided, for achieving the desired public response. Neoclassical economic theory describes how people *should* choose in certain situations, but it also claims to describe how people *do* choose (Thaler, 1979). Neoclassical economic theory is built on the assumptions that people 'maximise utility' (satisfaction), have rational economic preferences among identifiable outcomes, and act independently on the basis of complete and relevant information.

However, in certain situations people often act in ways that are inconsistent with neoclassical theory (Kahneman and Tversky, 1984; Thaler, 1979). Thaler (1979) found that, in these situations, neoclassical economic theory makes 'systemic errors in predicting behaviour' (p.39). Dawnay and Shah (2005) identify problems with neoclassical economic theory as a tool for motivating effective behaviour change, specifically because it:

- doesn't explain where preferences come from, and assumes preferences are fixed;
- finds altruism difficult to explain;
- disregards self-expectations and commitments;
- assumes loss aversion does not exist; and
- assumes people always act rationally and logically and have the ability to make the complex calculations required to make the best choices from many alternatives.

Insights from social psychology and behavioural economics

Behavioural economics is an emerging branch of economics that integrates findings from social and cognitive psychology to better understand and predict people's economic choices.

Loss aversion, the endowment effect and the status quo bias mean that people can be resistant to change

Research shows that people dislike losing something more than they like gaining it, and will often take large risks to avoid losses while avoiding small risks to make gains (Kahneman and Tversky, 1984; Thaler, 1992; Dawnay and Shah, 2005). This is called loss aversion. People also place extra value on things they consider theirs, and are systemically unwilling to give their things up. This is known as the endowment effect (Thaler, 1992; Bender, Kandel and Goldstone, 2004; Sunstein and Thaler, 2008; Dawnay and Shah, 2005).

Loss aversion and the endowment effect mean that people demand much more to give something up than they would be prepared to pay to acquire it. This is contrary to neoclassical economic theory, which states that people should be willing to pay the same amount to acquire something as they will accept in compensation to be deprived of it (Thaler, 1992). Cost-benefit analysis to value environmental goods typically involves using willingness-to-pay surveys ('how much would you be prepared to *pay* to prevent X happening or to gain X?') or willingness-to-accept surveys ('how much would you be prepared to *accept* as compensation for X?'). Neoclassical economics assumes that there is no difference between the two survey types. However, in practice people's willingness-to-accept price has been shown to be up to 20 times their willingness-to-pay price (Dawnay and Shah, 2005).

… when an option is presented as the status quo it becomes significantly more popular; and the more options people are given, the stronger the bias for the status quo

Loss aversion and the endowment effect help to produce inertia, meaning that people are generally resistant to changes to the status quo (Thaler, 1992). Thaler describes this as the status quo bias: a preference for the current state that biases people against change unless there are persuasive incentives to change. Samuelson and Zeckhauser's 1988 experiments showed that people have a strong inclination to retain the status quo. They found that when an option is presented as the status quo it becomes significantly more popular; and the more options people are given, the stronger the bias for the status quo (Thaler, 1992).

Because of the status quo bias, default options attract large market share (Sunstein and Thaler, 2008). Default options are pre-set choices – such as the chosen electricity provider

when you move into a new house. People can opt to change providers, but it requires making an effort to switch. Research has shown that people generally stay with the default option (Pichert and Katsikopoulos, 2007). People's bias for defaults is reinforced by a common assumption that the default setter has implicitly endorsed the default (Sunstein and Thaler, 2008).

Implications for environmental policy

• Policy makers should be aware of the discrepancies between willingness-to-pay and willingness-to-accept surveys. Dawnay and Shah (2005) warn that, in some situations, the type of survey used may determine the outcome of an analysis.

• The status quo bias suggests that policy makers may face resistance if they frame a choice as a departure from the status quo.

• The endowment effect could suggest that people will be more open to environmental protection if they consider the environmental goods as 'theirs'.

• There is considerable opportunity to nudge people into environmentally desirable behaviour through 'green' defaults (for example, carbon neutral electricity providers). However, this raises the question of which default should be set, and who determines it.

Framing and ordering affect the choices people make

People are very susceptible to how questions and problems are framed. Depending on how it is framed, the same information can lead to different outcomes. Framing information means presenting it in a way that will resonate in a certain way with a particular group of people. Framing leads to predictably different choices (Kahneman and Tversky, 1986; Milch et al., 2009). Because people are loss averse, whether information is framed in terms of losses or gains leads to systemically different decisions (Kahneman and Tversky, 1992). For example, telling people that conserving electricity will *save* them $X per year is significantly less effective than telling them that not conserving electricity will *lose* them $X per year (Sunstein and Thaler, 2008).

The order in which people consider benefits and costs has been shown to affect their choices (Milch et al., 2009; Swim et al., 2009). Hardisty, Johnson and Weber in 2006 conducted an experiment where an optional 2% fee was added to airline tickets, alternatively described as a 'carbon tax' and a 'carbon offset' to fund carbon reduction technologies (Gertner, 2009). Passengers were asked to identify with a political group (Republican or Democrat, as it was an American experiment), and to write down their thoughts in order as they decided whether to pay. They found that 65% of those identifying as Republicans were willing to pay for a carbon offset, but only 27% were prepared to pay for a carbon tax (Swim et al., 2009). Democrats were largely willing to pay for both. When Republicans considered a carbon tax they

had very negative early thoughts about the costs of the tax (resulting from a strong aversion to the tax frame), leading to strongly negative conclusions. When considering the carbon offset, both Republicans' and Democrats' early thoughts were more positive as they considered the benefits of funding clean technology before the costs of funding the offset, leading to positive overall conclusions and willingness to pay. People's initial willingness to pay the 2% fee was determined by their receptiveness to the 'tax' and 'offset' frames (not the tax mechanism itself), which in turn affected whether they considered benefits or costs first (Gertner, 2009).

Implications for environmental policy
- Framing policies as avoiding losses is more effective than framing in terms of gaining benefits.
- The *order* in which people consider benefits and costs can influence their decisions. Prompting people to consider benefits before costs can make them more accepting of policy proposals.

Social norms are powerful influences on behaviour

Social norms are behavioural expectations and signals within groups and societies that directly and significantly encourage and guide behaviour (Schultz et al., 2007). The main influence on people's behaviour is the behaviour of other people, particularly people they like (long-lasting influence) and people in authority (shorter-term effects) (Sunstein and Thaler, 2008; Finkelstein, 2009; Dawnay and Shah, 2005). People learn their behaviour from watching others, and look to others for guidance on how to act (a phenomenon called social proof), deriving norms about what is appropriate and accepted behaviour (Swim et al., 2009; Finkelstein, 2009). Social norms are particularly influential in ambiguous or stressful situations, or when others are experts (Sunstein and Thaler, 2008; Dawnay and Shah, 2005).

Sunstein and Thaler (2008) describe the extent to which people conform to social norms. They describe an experiment where taxpayers were sent four kinds of information. One group was told that their tax money funded public goods, such as environmental protection; another group was threatened with information about the legal risks of not paying their taxes; a third group was given increased information on filling out their tax return form; and the final group was told that 90% of people had already fulfilled their tax return obligations. The only intervention that had any effect on people's behaviour was the final one, which told people that there was a high compliance rate. Direct appeals to altruism, increased information and threats did not have a noticeable effect on behaviour.

Research shows that people often assume that undesirable behaviours are more common than they really are (Shultz et al., 2007). Social norms marketing campaigns (campaigns that use normative messages to try to change 'socially significant' behaviour, such as alcohol consumption or recycling, for example) are increasingly being used as an alternative to more traditional approaches to behaviour change (such as information campaigns, appeals to altruism or appeals to people's fears). These campaigns attempt to reduce undesired behaviour by letting people know that the behaviour is not as prevalent as they think (perceptions of what is commonly done in a given situation are known as *descriptive norms*) However, this can have an undesired, 'boomerang' effect by increasing the behaviour in people who previously avoided it. Schultz et al. found that it was possible to avoid the boomerang effect by introducing another type of norm to social norms marketing campaigns: a norm describing perceptions of what is commonly approved of or disapproved of within the society or group (an *injunctive norm*). They found that when household power bills displayed the average amount of electricity that other households in the same community were using (descriptive normative information), people tended to decrease or increase their electricity use to fit the norm. The undesired boomerang effect (low-energy users increasing their energy use to fit the norm) was prevented by giving people positive feedback (injunctive normative information). High-energy users received frowning-face emoticons ☹ on their power bills, while low-energy users received smiley-face emoticons ☺ (Schultz et al., 2007; Swim et al., 2009; Sunstein and Thaler, 2008). The combination of descriptive and injunctive normative messages meant that heavy users made even bigger cuts, and the light users remained frugal (Schultz et al., 2007).

> People learn their behaviour from watching others, and look to others for guidance on how to act (a phenomenon called social proof), deriving norms about what is appropriate and accepted behaviour ...

Implications for environmental policy
- Public policy should marginalise undesired behaviour and refer to undesired behaviour as an individual action that can be controlled, not something that everyone is already doing (Finkelstein, 2009).
- Public policy should promote desired behaviour as the norm.

Group cooperation can lead to better public outcomes

Numerous group and individual decisions pave the way for widespread support for policies (Gertner, 2009). To promote cooperation in making these decisions, it is crucial to understand the dynamics of group and individual decision making (Gertner, 2009; Krantz et al., 2008). Research shows that, while both are important, the order in which they occur is significant (Gertner, 2009; Milch et al., 2009).

People inherently enjoy being part of groups and display strong biases to in-group members (Dawnay and Shah, 2005; Gertner, 2009). The more that people identify with a group, the more willing they are to make decisions that benefit the group as a whole (Van Vugt, 2009). Van Vugt's (2001) water conservation experiments found, for example, that households with strong senses of community identity did not need a financial incentive to conserve water during a water shortage.

Group decision making has both advantages and disadvantages over individual decision making. Milch et al. (2009) found that groups tend to be more accurate in certain judgement tasks (such as estimating numbers and risk assessment) than individuals. However, group members often do not share information with the rest of the group, and groups are sometimes more susceptible than individuals to decision-making biases.

> ... promoting environmentally responsible behaviour is generally unhelpful, as it leads to feelings of helplessness by 'concentrating on sacrifice rather than quality-of-life-enhancing solutions'.

Experiments simulating shared-resource (commons) dilemmas have shown that cooperation deteriorates when people experience (or believe that they are experiencing) inequality or inequity (Swim et al., 2009). Trust and fairness are crucial for overcoming commons dilemmas. Krantz et al. (2008) describe how environmental decisions often appear to be commons dilemmas, where 'non-cooperation is the dominant strategy', even though it makes everyone worse off in the long run. Activating cooperation within groups helps to overcome this problem. Krantz et al. suggest:
- encouraging individuals to conform to group norms;
- enabling individuals to share group successes; and
- ensuring individuals carry out group-role obligations.

Experiments at Columbia University's Center for Research on Environmental Decisions (CRED) have shown that introducing arbitrary group symbols – such as a blue star – and telling people that they belong to the 'blue star team' can increase group participation from 35 to 50%; while simply seating people at a table together can increase participation rates to 75% (Krantz et al., 2008).

CRED researchers have also found that the order in which people consider decisions (group versus individual) has a significant effect on cooperation. When people make decisions as members of groups before making them as individuals, their conversations involve more inclusive words like 'us' and 'we' than when they make them in the opposite

order. Groups also tend to be more patient than individuals when considering delayed benefits (Gertner, 2009; Milch et al., 2009).

Implications for environmental policy
- Building people's sense of community belonging and identity could lead to greater cooperation.
- Structuring the public decision-making process to involve groups early in the process could lead to a better balance between social outcomes and individual outcomes.

Altruism and people's sense of fairness affect behaviour

Dawnay and Shah (2005) identify situations where people do not expect or even want payment, and find that financial rewards in fact occasionally act as a disincentive to desirable behaviour: for example, volunteer work where payment could detract from the warm fuzzy feeling of doing a good deed. Ariely and Heyman (2004) found that in non-monetary exchange relationships, altruism leads to a performance level that is 'high, constant, and insensitive to payment level' (p.788). Financial penalties are usually expected to act as a disincentive to undesired behaviour, but have been found to sometimes have the unintended effect of legitimising, and thus increasing, such behaviour (Gneezy and Rustichini, 2000; Ariely and Heyman, 2004). People feel guilty when they go against social norms and 'do the wrong thing', but fines have been shown to sometimes offset guilt by making people feel as though they have been punished and have atoned for their behaviour (Dawnay and Shah, 2005). To address problems with public goods allocation, neoclassical economic policies often redistribute tax revenue from polluting activities to the people most adversely affected. However, Dawnay and Shah found that this approach often makes people feel as if they are being bribed to accept the polluting activity, which undermines their motivation to 'do the right thing'. They found that it is more effective to directly address people's concerns.

People's willingness to pay for public goods is affected by how fairly they think costs and benefits are distributed. The more fairly people perceive the process and the outcome to be, the more they will contribute. Bender et al. (2004) found that when people were given money to allocate between their own use and a public good, most contributed about 50% to a public good. However, Fehr and Gächter (2002) found that without altruistic punishment, cooperation breaks down. Altruistic punishment is when people punish those who do not cooperate, even though punishment is expensive and there is no material gain for the punisher. Fehr, Fischbacher and Gächter (2002) found that, if treated fairly, people often both cooperate voluntarily and apply altruistic punishment. This is called strong reciprocity. They found that strong reciprocity can lead to 'almost universal cooperation in circumstances in which purely self-interested behavior would cause a

complete breakdown of cooperation' (Fehr, Fischbacher and Gächter, 2002, p.1). Fehr and Fischbacher's 2004 research found that altruism can evolve so that cooperation becomes the default behaviour in large groups – so long as people not only altruistically punish those who do not cooperate, but also punish people who fail to apply altruistic punishment (Fehr, Fischbacher and Gächter, 2002; Fehr and Fischbacher, 2004; Buchanan, 2005).

Care needs to be taken when appealing directly to people's altruism. Kaplan (2000) found that the usual altruism-centred approach to promoting environmentally responsible behaviour is generally unhelpful, as it leads to feelings of helplessness by 'concentrating on sacrifice rather than quality-of-life-enhancing solutions' (p.1). Likewise, attempting to motivate people with fear can be unhelpful, as it can lead people to minimise or ignore problems (Stern, 2005). When people feel they don't have control over a situation, they are much less likely to cooperate or to see much point in changing their behaviour (Zax, 2009; Dawnay and Shah, 2005).

Implications for environmental policy
- To prevent people feeling helpless, policy makers should take a participatory approach to forming policy or choosing policy instruments, and also avoid overloading people with excess information and choice (Dawnay and Shah, 2005).
- Policies should build on the control people do have over their environment, and empower people to help manage their local resources.
- Policy makers should be cautious with financial incentives and penalties, as they can have unintended consequences.

Habits are significant obstacles to behaviour change
Bender et al. (2004) describe how following others' behaviour, and our own habits, creates shortcuts, allowing us to 'economise on mental effort'. Whenever we make a decision we have three options: follow others, repeat an action we've previously taken, or choose anew. Because it is much easier for us to take a shortcut – and follow others or our own previous behaviour – we generally do take shortcuts rather than choose anew. Easy decisions with known, hassle-free outcomes produce rewarding feelings, which in turn reinforce those decisions in a feedback loop, creating habits. Habits can be difficult to change if they are frequently repeated and if there are strong associated rewards, particularly immediately following the action (Dawnay and Shah, 2005).

Dawnay and Shah found that the first step to breaking undesirable habits is simply being made aware of them. Once we are conscious of a habit, we can assess the benefits and costs of other behaviours. We may then choose to adopt a new behaviour, which, in time, becomes a new habit. Visual cues can be helpful in changing habits, as they can remind us of desirable behaviour.

Implications for environmental policy
- Where public policy is trying to change behaviour, particularly something that is clearly a habit, then social psychology and behavioural economics become significantly more important than simple neoclassical economic incentives.
- Policy makers should be aware of the existence and strength of pre-existing habits that may hinder people in changing their behaviour.
- Environmental policy should make people aware of their unconscious habits and of preferred alternative behaviours, and should provide a variety of incentives to adopt environmentally conscious habits, as well as providing people with prompt feedback to spur and reinforce desired behaviour change, such as visual cues (for example, colourful recycling bins with bottle-shaped holes).

> When our actual behaviour diverges from our expectation of how we usually behave (or from our perception of how others expect us to behave) we often feel uncomfortable.

Divergence of self-expectations and behaviour can lead to cognitive dissonance
When our actual behaviour diverges from our expectation of how we usually behave (or from our perception of how others expect us to behave) we often feel uncomfortable. This is known as cognitive dissonance, and either our self-expectations or our behaviour must change to resolve it (Dawnay and Shah, 2005; Stoll-Kleemann, O'Riordan and Jaeger, 2001). Stoll-Kleemann, O'Riordan and Jaeger (2001) showed that people find the consequences of climate change alarming. However, they also found that people find the idea of changing their energy-intensive lifestyles more daunting. These competing tensions create cognitive dissonance, and people form 'socio-psychological denial mechanisms', meaning they overestimate costs and underestimate benefits of shifting to less energy-intensive behaviour while blaming other people's and government's inaction.

If we have publicly expressed our attitudes or beliefs, we are more likely to change our behaviour so that it remains consistent with them (Dawnay and Shah, 2005). Therefore, commitments and promises are important for ensuring people stick to behaviour. When people make a small commitment (for example, signing a petition), they are more likely to agree to make a much larger commitment a few days later (for example, donating money). People are also more likely to stick to a commitment if it is public, if they verbally agree or write down their intentions, or if they make the commitment as a member of a group (Finkelstein, 2009).

Implications for environmental policy
- Knowledge of the effect of commitments and promises would help policy makers design better policy options. Understanding key public perceptions would help avoid undesirable policy responses, such as those arising from cognitive dissonance.
- Policies should encourage people to make small commitments, make commitments public and build on small commitments.

Asymmetric discounting biases people towards the present

As part of cost-benefit analysis, economists typically discount future costs and benefits relative to present costs and benefits. The discount rate is the rate at which future outcomes are devalued. Determining the correct discount rate to make cost-benefit choices between different environmental policy proposals is one of the biggest uncertainties in environmental economics, particularly the economics of climate change. However, to predict how people will respond to different

immediate, tangible costs and sacrifice immediate, tangible benefits. Their future, uncertain and abstract benefits are discounted. Hardisty and Weber's (2009) research found that people's strong negative reactions to immediate costs and sacrifices mean that it is unlikely that people will make decisions leading to long-term sustainable behaviour.

Weber et al. (2008) greatly reduced intertemporal discounting in people's choices by manipulating the order in which the participants in their research considered the benefits of immediate or delayed consumption. When prompted to argue for delayed consumption first, participants showed 'drastically reduced' intertemporal discounting. Hardisty and Weber (2009) found that social norms typically determine the order that people consider different options.

Implication for environmental policy
- Controlling the order in which individuals and groups consider the benefits of immediate or delayed consumption can reduce intertemporal discounting.

> When assessing risk emotionally, people tend to underestimate the danger of events they have never experienced and events that appear physically and temporally distant, and to overestimate the likelihood of low-probability events if they have personally experienced them.

People use both analytical and emotional decision-making processes to process risk; risk experienced via personal experience is more motivating than risk experienced via description

People use two systems to process and assess risk: analytical (or reflective) and emotional (or associative, affective) (Gertner, 2009; Sunstein and Thaler, 2008; Swim et al., 2009). When we experience risk through our analytical system we consciously consider costs and benefits. Analytical risk processing is a rigorous and therefore slower process that must be explicitly taught (Swim et al., 2009). When we experience risk through our emotional system, it is a non-formal, automatic, individual process – we experience risk as an instinctive feeling, an urgent gut reaction (Weber, 2006). The two systems reinforce each other, but in situations where their outputs differ, the emotional system generally dominates. In the case of climate change there seems to be a conflict between the two systems: the emotional system is not sending warning signals, even though analytical assessment tells us that it is a huge problem (Swim et al., 2009).

People's fear of risk often does not correspond to objective risk assessment. The same information can lead to different choices depending on how a risk is assessed (Weber, 2006). Experiments in analytical risk assessment have shown a bias for immediate benefits and a tendency to undervalue future outcomes (Gertner, 2009). When assessing risk emotionally, people tend to underestimate the danger of events they have never experienced and events that appear physically and temporally distant, and to overestimate the likelihood of low-probability events if they have personally experienced them (Gertner, 2009; Weber, 2006). People generally overestimate the likelihood of easily imagined risks, and underestimate the risk of things that happen relatively frequently (Sunstein

environmental policy proposals, we need to understand people's perceptions of intertemporal trade-offs (for example, between the economy and the environment). This requires understanding the *actual* discount rates that are *implicit* in people's intertemporal decisions (Hardisty and Weber, 2009).

Research shows that people often implicitly discount 'irrationally'; that is, in ways contrary to the predictions of neoclassical economic theory (Weber et al., 2008; Dawnay and Shah, 2005; Hardisty and Weber, 2009; Thaler, 1992). People underestimate future benefits and overestimate future costs, and they also over-value present benefits and under-value future benefit. People typically discount gains more than losses and discount small outcomes more than large outcomes. Weber et al.'s (2008) experiments showed that people demand more in compensation for delaying consumption than they are prepared to give up in order to accelerate consumption.

This asymmetrical intertemporal discounting of costs and benefits poses problems in dealing with environmental issues like climate change. Actions to mitigate climate change incur

and Thaler, 2008; Dawnay and Shah, 2005). People also discount the risk of things they enjoy doing, as well as the risk of things that they are familiar with (i.e. where they have daily exposure to a risk) (Bender et al., 2004; Swim et al., 2009). The American Psychological Association warns that 'greater familiarity with climate change and its risks, unless accompanied by alarmingly large negative consequences, may actually lead to smaller rather than larger perceptions of its riskiness' (Swim et al., 2009, p.46).

Risk experienced via description is risk that is learned from experts, usually in the form of statistical information. Risk experienced by recalling personal (bad) experience is more effective at prompting action than risk experienced via description, as it usually produces a strong visceral response (Gertner, 2009; Weber, 2006). Because climate change is characterised by uncertainty, and its effects are not yet being widely experienced (or at least noticed), people have to rely on descriptions of the risks – scientific models and expert judgement, or media interpretations of these – which do not favour immediate action. By the time we experience strong emotional responses to climate change that are based on personal experience, it may be too late to avoid particularly adverse outcomes (Swim et al., 2009; Weber, 2009; Zax, 2009). Lejarraga (2009) found that people are willing to trade off complicated, detailed information experienced by description for less accurate but simpler personally experienced information.

Research also shows that many people do not trust risk messages that come from scientists or government officials. This lack of trust helps create reactance: a negative reaction towards policy or advice that appears to threaten individual freedom. The American Psychological Association emphasises that changing behaviour requires trust, especially when people believe that the change involves a cost (Swim et al., 2009).

Implication for environmental policy
- Weber argues that we need to find ways to evoke visceral reactions in people, by emphasising the local and short-term effects of climate change rather than trying to muster empathy for things that could happen to someone else, somewhere else (Weber, 2006; Zax, 2009).

People have a finite pool of worry and are susceptible to the single-action bias

Weber (2006) found that people have a finite pool of worry. This means that we often struggle to maintain our fear of one problem when a new problem comes along. She also identifies the single-action bias occurring when one action (such as buying a hybrid car, or voting for a green candidate) effectively assuages the fear (climate change) that prompted the action, meaning that we don't take further actions and are back where we started (Gertner, 2009; Weber, 2006).

Implication for environmental policy
- Policy makers need to be aware of these biases so that they do not abandon policy efforts aimed at one risk (climate change) in favour of another (financial recession), and to ensure that they apply a range of policy instruments that target problems most effectively.

Increased information does not necessarily lead to behaviour change

Abrahamse et al. (2005) found that increased information leads to higher levels of knowledge, but not necessarily to behaviour change. McKenzie-Mohr and Smith found that campaigns relying only on providing information often have 'little or no effect' on behaviour, and insist that most complex behaviour needs a multifaceted approach, which will also need to change over time (McKenzie-Mohr and Smith, 1999, p.7).

Changing human behaviour is an important part of addressing the problem of climate change

Stern (2005) found that single-strategy approaches to behaviour change have largely been ineffective. This is because behaviour change depends on many factors, and targeting only one type of behaviour is likely to make a difference to only a small percentage of people.

Implications for environmental policy
- When distributing information, policy makers should look at the quality and framing of the information, not the quantity.
- Policies should address actual and perceived barriers to behaviour change.
- Policies should use multifaceted, contextualised approaches to behaviour change rather than single-strategy approaches.

Conclusion

Kaplan (2001) found that effective environmental policies 'must be based on a coherent conception of human nature that speaks to the relationship between how people approach new information, how information relates to motivation, and how information and motivation relate to behavior change' (p.1). Social psychology and behavioural economics offer effective, and potentially inexpensive, approaches to addressing these questions. Anthropogenic climate change is caused by human behaviour. Changing human behaviour is an important part of addressing the problem of climate change – whether it is changing individuals' consumption habits, or enhancing decision-making processes to favour social outcomes over individual outcomes. If policy makers apply an understanding of social norms, cognitive biases, competing motivations, group dynamics, and other insights from social psychology and behavioural economics, they have the potential to significantly motivate environmentally beneficial changes in individual and group behaviour.

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David Bromell

Diversity and Democracy

A challenge for public policy in New Zealand, as elsewhere, is how to keep a diverse society democratic and, conversely, how to make democratic practice more inclusive in an increasingly diverse society.

The discussion that follows makes two assumptions. Firstly, New Zealand's population exhibits an increasing diversity of ethnicity, culture, religion, family form, values and so on (Boston, Callister and Wolf, 2006).[1] Statistics New Zealand recorded more than 200 ethnic categories in the 2006 Census; one in ten usually resident New Zealanders identifies with two or more ethnic groups; and young New Zealanders, particularly, increasingly exhibit dual, multiple, hybrid (e.g. New Zealand-Chinese – or Chinese-New Zealander) and mobile ethnic identities.[2] Monoculturalism is, therefore, not an option for New Zealand. We (whoever the 'we' are) cannot turn the clock back to a golden age in which we were all much the same, or thought we were. Neither is it an option to 'send migrants back to where they came from'.[3] Twenty-three per cent of people usually resident in New Zealand in 2006 – nearly one in four New Zealanders – were born overseas. In the Auckland region, 37% were born overseas (Statistics New Zealand, 2009b, p.14).

Secondly, as Winston Churchill put it, 'Democracy is the worst form of government except all the others that have been tried.' Democratic institutions are imperfect and fragile and frustrating, and democratic processes are never ideal, but the democratic experiment has run long enough, and in enough countries of the world, to convince me that democracy is our best hope of living together in freedom, justice and peace.

On the basis of these two assumptions, I will highlight, and illustrate, three points of tension in the theory and practice of democracy in an inescapably diverse society:
- individual rights that all share equally versus special group rights;
- liberty versus fraternity; and
- democracy as a 'market' versus democracy as a 'forum'.

I will then propose that these tensions be managed pragmatically in public life as enduring, even natural, tensions, rather than attempting to resolve them by recourse to ideologies that make differences a ground for division and blur a clear and consistent focus on our common humanity.

Individual rights that all share equally versus special group rights

The first point of tension is whether government should limit its role to securing and protecting individual rights that all share equally, or whether government should recognise social groups, and assign 'special rights' (see Hart, 1955, especially pp.185-8) to those groups or adopt 'special measures' (or what is variously called 'affirmative action', 'positive discrimination' or 'preferential treatment') (Callister, 2007) to

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Are public institutions to be and remain blind to differences of race, ancestry, skin colour, ethnicity, culture, religion and so on?

tackle disadvantage that correlates in some way with ethno-cultural group membership.

Is it 'one rule of law for all'? Are public institutions to be and remain blind to differences of race, ancestry, skin colour, ethnicity, culture, religion and so on? Are the only rights that count universal rights that all share equally by virtue of our common humanity? Or are there rights and privileges that attach to some and not others: for example, to Māori by virtue of claims to indigeneity, or claims based on the Treaty of Waitangi? If so, ought special group rights to be permanent or time-limited and limited specifically to reducing social and economic inequalities? And do special group rights extend to special representation rights: for example, reserved seats on local authorities or in Parliament?

If we do opt for group-specific rights, what are the trade-offs between group recognition and rights and the democratic principle of equality? Is there to be a hierarchy of ethnic groups in New Zealand: first, Māori as tangata whenua; then the descendants of Anglo-Celtic British settlers; and then the johnnies-come-lately, all later arrivals? In other words, are some New Zealanders, at least in some respects, more equal than others?

Liberty versus fraternity

The second point of tension is similar and related and concerns tensions implicit in the French republican motto: 'Liberté, Egalité, Fraternité'.[4] Is democratic government about securing and protecting individual liberty, or is it about fraternity – defining, safeguarding and promoting the collective interests and well-being of citizens and communities ('the common good')? This tension lies at the heart of debates between liberal (and particularly libertarian) and communitarian political philosophies and various attempts to bridge these.[5]

Are the interests of all best served when each of us freely pursues our own visions of the good life, provided we don't significantly limit or harm others' exercise of their freedom? Is it better for all of us if government butts out of our lives? Should we be free to work out for ourselves, in diverse ways, matters of ethnic, cultural and religious identity and practice, without either interference or support from the state? Are our personal and social group identities matters that properly belong in the private realm, in family and kinship groups, and in clubs, societies and other voluntary associations?

Or does government have a legitimate role in defining, safeguarding and promoting the collective interests of citizens and communities, including identifying desired community outcomes and social, cultural, economic and environmental values and priorities for both current and future generations?

If the state should limit individual liberty in various ways for the sake of the common good, what, in turn, ought to be the limits to state paternalism? And how might we ensure that 'the common good' is not defined and captured by a tyranny of the majority, or by noisy, politically active minorities, in ways that suppress or mask dissent and difference, let alone citizen indifference to local authority Long Term Council Community Plans and to voting in local body elections?[6]

Further, how will we calculate the trade-offs between public recognition of special group rights (particularly 'indigenous rights') and competing claims for equal access to 'the commons', as we've seen, for example, in debates about race-based and needs-based policies and programmes in New Zealand (State Services Commission, 2005; Callister, 2007), and about the Foreshore and Seabed Act 2004 (van Meijl, 2006)?

Democracy as a 'market' versus democracy as a 'forum'

The third point of tension is between the practice of democracy on the model of a 'market' (aggregative democracy), and the practice of democracy on the model of a 'forum' (deliberative democracy).[7]

Is politics essentially a numbers game played out among diverse interests, in which people who wish to exercise political power trade off various interests against each other and compete to aggregate votes, to 'do the numbers', in order to gain and retain office? Or is democracy more like a forum, in which we participate as citizens in our own self-government through discussion, debate, deliberation and persuasion, shaping and changing one another's minds through a formative politics until some workable consensus is reached?

If we think democracy is better served by minimal government and maximum protection of individual liberty, we'll likely prefer the 'market' model of democracy. If, on the other hand, we opt for the 'forum' model, then we need institutions and public spaces where citizens of all sorts can rub shoulders, encounter the reality of each other's lives, and talk and deliberate together (Sandel, 1996). This has implications for the design of libraries, parks, recreation centres, shopping malls, transport systems, broadband infrastructure and urban design generally, and for how central and local government plan and conduct public consultation and citizen engagement.

Both/and, or either/or?

Of course, I have my own ideas and opinions on each of these three points of tension. (Some make me tenser than others!) My initial academic training, however, was as an historian and history amply illustrates that these are perennial tensions in the theory and practice of democracy. They are not mutually exclusive either/ors that can, or should, be resolved once and for all. More often than not, we have to learn to live with a both/and, and settle for solutions that are liveable for now, without expecting they will hold for all time.

I will proceed to illustrate this in relation to each of the three points of tension I have identified.

Individual rights and group recognition and rights

The idea of liberal democracy emerged following the European wars of religion in the sixteenth and seventeenth centuries. What eventually resolved this conflict wasn't granting special group rights to particular religious groups, but separating church and state and entrenching each individual's freedom of religion. Within the private sphere, people were to be free to associate voluntarily with their co-religionists, whoever they might be, without either interference or support from the state. The one condition was that when individuals exercise their personal liberty within the private sphere, they should respect others' rights. Tolerance and non-coercion thus became political virtues.

Thomas Hobbes and those who followed him (Spinoza, Locke, Montesquieu, Hume and de Tocqueville) initiated the project of modern political philosophy and of liberal democracy on this basis. As Mark Lilla (2007, p.92) summarises it, the project imagined a new kind of political order:

> It was to be an order where power would be limited, divided, and widely shared; where those in power at one moment would relinquish it peacefully at another, without fear of retribution; where public law would govern relations among citizens and institutions; where many different religions would be allowed to flourish, free from state interference; where individuals would have inalienable rights against government and their fellows.

This is the hard-won tradition of liberal democracy, a precious cultural legacy that European settlers brought to these islands. And in fact these European developments were reflected in New Zealand during the nineteenth century as rival Anglican, Methodist, Catholic and Presbyterian missions jostled for position and place (and the 'saving' of Māori souls) in the new colony. At the signing of the Treaty of Waitangi in 1840, Bishop Pompallier expressed concern that establishing a British colony might lead to interference in religion. He asked for an assurance that 'free toleration' would be allowed in 'matters of faith', and that a public guarantee be given to the Māori to this effect (Orange, 1992, p.53). A carefully written statement was prepared by CMS missionary Henry Williams and read to the assembly. William Colenso's version of this statement, as cited by Claudia Orange (ibid.), reads: 'The Governor says the several faiths of England, of the Wesleyans, of Rome, and also the Maori custom, shall be alike protected by him.'[8]

Public recognition of religion was debated again during the first session of the House of Representatives, on Friday 26 May 1854, immediately following the election of a Speaker. James Macandrew moved: 'That it is fit and proper that the first act of the House of Representatives shall be a public acknowledgement of the Divine Being, and a public supplication for His favour on its future labours' (New Zealand Parliamentary Debates, 26 May 1854, pp.4-6). Other members expressed concern that the House 'be not converted into a conventicle' and that no offence be caused to 'Jews and Unitarians'. Samuel Revans 'thought the motion would lead the House away in a retrograde direction from the free spirit of the Constitution, which appeared to have been framed so as that the colonists of New Zealand at any rate should be exempt from the causes of heartburning on religious questions which, being interwoven in the old institutions at Home, could not be so readily got rid of.'

Frederick Weld's amendment, 'That this House, whilst fully recognizing the importance of religious observances, will not commit itself to any act which may tend to subvert that perfect religious equality that is recognized by our Constitution, and therefore cannot consistently open this House with public prayer', was lost by 20 to 10, however, and the original motion put and carried.

A subsequent motion was then put and carried, 'That, in proceeding to carry out the resolution of the House to open its proceedings with prayer, the House distinctly asserts the privilege of a perfect political equality in all religious denominations, and that, whoever may be called upon to perform this duty for the House, it is not thereby intended to confer or admit any pre-eminence to that Church or religious body to which he may belong.' The Reverend F.J. Lloyd (Church of England), being in attendance, was then introduced and read prayers ('Sound: Parliament's Opening Prayer').

Thirty-three years later, the question was whether public education in New Zealand should be secular. Until 1877, education was the responsibility of each province, which subsidised schools run by the Anglican, Methodist, Catholic and Presbyterian churches. With the abolition of the provinces in 1876, central government took over running schools. In large part because of rivalry between the churches, the minister of Justice, Charles Bowen, introduced a bill into the House that was passed as the 1877 Education Act. The act withdrew all subsidies from church schools and made schooling free, secular and compulsory for all children aged between seven and thirteen.

It is curious that a society that was rightly cautious about extending public recognition and rights to one form of cultural identity (namely, religion) has, since the mid-1970s, been less critically reflective about extending public recognition and rights to another form of cultural identity (namely, ethnicity).

... recognition should be largely symbolic rather than tied to resources and permanent special group rights.

At the first reading, on 24 July 1877, Charles Bowen advocated for secular education as 'the only way to be absolutely fair'. This sentiment was mirrored by William Gisborne in the second reading debate on 31 August:

> I wish to say that I am strongly in favour of secular education by the State. I believe that it is the only education which the State can possibly impart to its subjects, not because I undervalue religious education, but because practical experience has shown that if a State enforces religious education in its school system it will immediately create religious animosity and dissension, and it will do more harm than good (New Zealand Parliamentary Debates, 24 July 1877, p.179).

C.A. de Lautour also spoke in favour of secular education:

> There is no man yet bold enough to stand up in this House and disavow any sympathy with religion; there is no man who would say that children are not to be trained up in religion; but we do hold that religion can be taught by the Church – can be taught at the hearth, and it is not necessary that it should be introduced into the daily school (ibid., p.197).

This was the classic liberal stance. Matters of religious belief are for individuals to determine freely for themselves; they are matters for home and hearth, and for churches and other voluntary associations, not for the state and for state institutions.[9]

It is curious that a society that was rightly cautious about extending public recognition and rights to one form of cultural identity (namely, religion) has, since the mid-1970s, been less critically reflective about extending public recognition and rights to another form of cultural identity (namely, ethnicity).

In fact, neither in New Zealand nor elsewhere has Hobbes's 'Great Separation' of church and state ever been consistently achieved. New Zealand has no official religion or established church, but state and ceremonial occasions are commonly held in Anglican cathedrals or officiated over by Anglican clergy, and since the 1975 Private Schools Conditional Integration Act the state has substantially funded Catholic and other 'special character' integrated schools, which makes it next to impossible to quibble at state funding for Muslim, Jewish, Buddhist and other religious schools and otherwise maintain a consistent separation between church and state.

But more than a failure of consistency, this indicates what Francis Fukuyama (2006, p.6) has described as 'a hole in the political theory underlying modern liberal democracy'. The 'hole' concerns whether, how and to what extent liberal societies should recognise groups as well as individuals.

This is a genuine problem. The human self is torn between freedom and belonging, independence and community. We value autonomy, self-determination, freedom. But the social groups we inhabit aren't more or less optional extras that we freely choose to have, or not to have. Our relationships, attachments and identities shape and re-shape the self. We don't just *have* relationships, attachments and belongings; we *are* our relationships, attachments and belongings (Taylor, 1989). As Cervantes put it, 'Tell me what company you keep and I'll tell you what you are.'

So yes, the self is free, but it remains deeply embedded in a society, in a culture, in certain social groups, and in certain attachments and identities. And of course we bring these belongings and identities to our political participation, because even if we choose not to, others almost certainly will. So there is, and should be, some place in public life for recognition of social groups and their importance in our lives (Taylor, 1994). Nevertheless, I will argue that this recognition should be largely symbolic rather than tied to resources and permanent special group rights. For if dealing with the question of group recognition and rights in relation to religion has proved difficult, the challenge is amplified in relation to ethnic identity. Usually, though not always, people affiliate with just one religion at a time. But people commonly can and do affiliate with two or more ethnic identities, forge hybrid identities and change their identities over time and in different contexts and for different purposes.

New Zealand has a long history of inter-ethnic partnering and parenting (Callister, Didham and Potter, 2005) and a high rate of intermarriage (Didham, 2004). In a study of Māori intermarriage, Callister (2004) found that around one half of partnered Māori had a partner recording other than Māori ethnicity. One in ten usually resident New Zealanders identified with two or more ethnic groups in the 2006 Census.[10] Two-thirds of babies registered as Māori, one half of babies registered as Pacific peoples and just under a third of babies registered as European or Asian are also registered as belonging to some other ethnic group or groups (Statistics New Zealand, 2009a).

This makes it impossible to divide New Zealand's population up into stable and mutually exclusive 'ethnic groups', in order to assign different types of recognition, special group rights or special measures. This is just one reason why I have argued elsewhere (2008, pp.35-46, 291-5; 2009, pp.243-5) that claims to indigeneity and indigenous rights in the New Zealand context make little sense now and are likely to make even less sense in future. It is becoming increasingly difficult to define clear boundaries around who is 'indigenous' and who is not without resorting to arguments that fall back onto discredited race theories about 'one drop of blood' being enough.

There remains an important place, however, for *symbolic* recognition – and this makes possible a both/and balancing of the tension between individual rights that all share equally and social group recognition. For example, there is now a reasonably secure public consensus that, whatever we think about claims to indigeneity, Māori are and ought to be recognised publicly as the 'first settlers' of New Zealand and that Māori consequently have a status as tangata whenua (people of the land), at least in the sense of being 'first among equals'. This works itself out in widespread acknowledgement of the Treaty of Waitangi as a founding document of the nation,[11] in recognition of Māori as an official language and its increasing use in public broadcasting, in the singing of the national anthem in both Māori and English and in the use of elements of Māori ceremonial at public occasions and as part of 'brand New Zealand'. Over time, there may be scope to extend this symbolic biculturalism by, for example, changing the name of the country (to Aotearoa?) and adopting a new or dual national flag. As Jacob Levy (2000, p.230) has commented: 'Liberalism is right to give rights and resources moral priority over recognition and symbols; but that should not prevent liberals from seeing the tremendous importance symbolic disputes can have to their participants.'

In line with the recommendations in Paul Callister's (2007) discussion (cf. Bromell, 2008, p285, n13), 'special measures' may also have a place in public policy but ought to be used only when the following conditions apply:

- there is a clear and defensible rationale for them, which has broad political and public support;
- the target can be clearly defined;
- membership of the target group is a strong predictor of disadvantage, and targeting is accordingly not significantly compromised by intra-group diversity and under- or over-representation;
- there is strong evidence that the proposed measure or measures will efficiently and effectively reduce the disadvantage;
- a goal and/or timeframe is identified and agreed, beyond which the special measure or measures will expire; and
- the effectiveness of the measure or measures once implemented is monitored and evaluated.

In achieving a balance within a liberal democracy between protecting individual rights and publicly recognising social groups, there does, however, have to be a bottom line. Liberal democracy is not value neutral. It requires an active commitment to the equal worth and dignity of each human person and equal opportunity to lead lives we ourselves have reason to value. The fact is, not all cultural groups do uphold liberal values about the equal worth, dignity and liberty of people as individuals. Both liberalism and democracy are seriously compromised by the kind of cultural relativism that tolerates anything and everything and criticises nothing.

Liberty and fraternity

So what about balancing individual liberty and the collective interests and well-being of citizens and communities? In fact, we do it all the time. In September 2009, Samoa made the change from driving on the right to driving on the left. The road code is a restriction on individual liberty but we accept it as a way of minimising the risk of harm that would ensue if everyone drove wherever and however they wished.

Or, to go back in time, consider the debate that raged in New Zealand between the 1870s and 1919 about the sale and consumption of alcohol. The prohibition movement very nearly carried the day (see Daniels, 1966). In a referendum held in April 1919, the initial vote favoured prohibition by 246,104 to 232,208. But a few days later, the votes of the New Zealand Expeditionary Force and other personnel still overseas following World War One were counted. The soldiers' votes were overwhelmingly in favour of continuance, by 31,981 to 7,723, which swung the balance. Continuance was narrowly carried with 51% of the votes. In terms of balancing individual liberty and social well-being, we continue to live with this debate, however, in terms of drink-driving and the sale and supply of alcohol to young people.

The 2003 Smoke-free Environments Amendment Act, restrictions on the display and sale of tobacco products and the excise tax imposed on tobacco are another example of government seeking to balance the freedom of individuals to smoke tobacco if that's what they want to do with minimising the harm caused to others by passive smoking in public places and the cost to our public health system of disease caused by smoking. Social marketing that targets smoking in cars and private homes, to reduce the harm caused to children by passive smoking, pushes the public-private distinction even further. And for many, the Crimes (Substituted Section 59) Amendment Act 2007 No 18 overstepped the bounds, and resulted in the August 2009 citizens-initiated referendum on the question 'Should a smack as part of good parental correction be a criminal offence in New Zealand?'

My point is that public regulation commonly involves arbitrating a practicable balance between securing and protecting individual liberty, and defining, safeguarding and promoting the collective interests and well-being of citizens and communities. And if this balancing act is to be and remain democratic, then my third point of tension comes to the fore: balancing a 'market' model of democracy with a 'forum' model of democracy.

Public regulation commonly involves arbitrating a practicable balance between securing and protecting individual liberty, and defining, safeguarding and promoting the collective interests and well-being of citizens and communities.

Democracy as a 'market' and democracy as a 'forum'

In the market model, politicians pay attention to well-defined interests: for example, to senior citizens, to church leaders, to iwi, to environmentalists, to the business sector, and so on. The job of government is to provide for these diverse interests by arriving at deals and compromises. The process parcels up diverse interests into more or less coherent packages so politicians can deliver on the promises they have made to their supporters, which is what makes the process democratic. If politicians fail to respond to the interests and priorities of those who voted them in, that is a failure in the political marketplace and they are likely to be voted out at the next election.

The 'forum' model, on the other hand, doesn't assume that interests are fixed and known in advance. Rather, it assumes that interests can and should be shaped and reshaped by processes of public debate and consensus-building which allow collective interests and identities (the common good) to emerge and to prevail.

In principle, I am drawn to the model of democracy as a forum in which minds are changed, my own included, and we end up, more often than not, with a position that none of us anticipated at the outset. But I also recognise how easily deliberative democracy can be taken over by minority (and quite unrepresentative) voices simply because, for whatever reason, they have the motivation and make the time. And deliberative democracy does take time, a great deal of time.[12] It can also drag decision making down to the lowest common denominator and entrench the status quo in ways that inhibit the exercise of political leadership in moments of crisis and opportunity.

In fact, no government exclusively follows either the 'market' or the 'forum' model of democracy. Even if, for practical reasons, government works more like a market than a forum much of the time, consultation does occur more often than not, some of the most important work of Parliament is thrashed out in cross-party select committees, the Official Information Act helps to keep the process more or less transparent, and the media plays a more or less adequate role in informing, stimulating and reflecting public debate.

Ideas, not ideology

There are, I have suggested, three perennial, even natural, tensions in the theory and practice of democracy in diverse societies. Each of these needs to be managed in public life, without prematurely resolving them by an either/or choice between polarised, ideological positions.

As Bhikhu Parekh (2008) has argued, our particular identities and our universal human identity are dialectically related. He urges us to appreciate the plurality and interaction of our social identities; to acknowledge difference and dissent and aim at no more than a broad and fluid consensus; to avoid oppositional politics and accept that our allegedly opposed identities are interdependent and products of a common system of social relations; and to develop a critical politics of identity, rather than naturalise or accept uncritically an historically inherited view of a collective identity (a politics of culture).

To carry such a project forward in the New Zealand context will be difficult, but not as difficult as in some other national contexts and certainly not impossible, given our small population, our 'two degrees of separation' and something of a national preference for pragmatic 'muddling through'. Above all, it requires the kind of policy making and statecraft that are wise and not just clever, that both acknowledge the manifold ways in which we are different from one another and keep a clear and consistent focus, not on all that could divide us, but on all we have in common.

1   I focus in what follows on ethno-cultural (including religious) diversity, because since the end of the Cold War this has become the most common source of political violence in the world (Kymlicka, 1995, p.1).

2   For a summary of New Zealand's demography based on data from the 2006 Census of Population and Dwellings, see Bromell (2008), pp.27-35. See further Callister, Didham and Potter (2005); Carter et al. (2009); Howard and Didham (nd); Kukutai (2008); Kukutai and Callister (2009) and Statistics New Zealand (2007a).

3   See, for example, Ralston (2008) on comments by New Zealand First deputy leader Peter Brown in April 2008. John Campbell's TV3 interview with Peter Brown on 2 April 2008 can be accessed at http://www.3news.co.nz/NZ-First-MP-grilled-over-anti-Asian-immigration-stance/tabid/817/articleID/51227/cat/221/Default.aspx.

4   On managing the tensions between liberty, equality and fraternity in public policy, see Moroney (1981).

5   The tension between liberalism and communitarianism further corresponds to a choice between deontological and teleological ethics (the 'right' and the 'good'). See, for example, Sandel (1982), Gamwell (1984) and Kymlicka (1989).

6   Restructuring of local government in 1989 and the introduction of postal voting was initially accompanied by an increase in voter turnout at local authority elections, peaking at 61% in 1992. Since then voter turnout has declined steadily, however, with the exception of the 1998 elections. It dropped below 50% in 2004 for the first time since 1989. Turnout in the 2007 elections was 44%. By comparison, voter turnout at the 2008 general election was 80%. Source: Department of Internal Affairs (2008), and Party Results and Turnout by Electorate.

7   I owe the metaphors of democracy as a 'market' or 'forum' to Politt (2003), pp.84-5.

8   Hugh Carleton's version, in his Life of Henry Williams (as cited by Palmer, 2008, p.392, n113), reads: 'The Governor wishes you to understand that all the Maories [sic] who shall join the Church of England, who shall join the Wesleyans, who shall join the Pikopo or Church of Rome, and those who retain their Maori practices, shall have the protection of the British Government.'

9   The Catholics, however, were not happy. Bishop Patrick Moran of Dunedin wrote, in an editorial in the New Zealand Tablet on 31 August 1883 which was reproduced as a standing editorial until 25 June 1897 under the heading 'Progress and Justice in the Nineteenth Century': 'The Catholics of New Zealand provide, at their own sole expense, an excellent education for their own children. Yet such is the sense of justice and policy in the New Zealand Legislature that it compels these Catholics, after having manfully provided for their own children, to contribute largely towards the free and godless education of other people's children!!! This is tyranny, oppression, and plunder' (New Zealand Tablet, 31 August 1883, p.15).

10 i.e., at level one of the ethnic classifications used by Statistics New Zealand. See further Statistics New Zealand, 2005, 2007b.

11 I include acknowledgement of the Treaty of Waitangi as 'symbolic biculturalism' because, as Andrew Sharp (2002, p.11) has observed, references to it as the 'founding document' of the constitution are more a matter of rhetoric than of legal reality.

12 In advocating for participatory democracy, Iris Marion Young (in Fung, 2004, pp.47-8) acknowledges the time and energy this demands of citizens but proposes that this be compensated for by a shorter working day and the creation of democratic forums in workplaces, with paid childcare to enable parents to attend meetings.

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Robert A. Buckle[1]

Asia-Pacific Growth
Before and After the Global Financial Crisis

Introduction

The modern era of globalisation has been associated with significant economic transformation around the world, but also an increasing frequency of financial crises. According to Eichengreen and Bordo (2002) there were 39 national or international financial crises between 1945 and 1973. Their frequency increased to 139 between 1973 and 1997, culminating in the Asian financial crisis. These crises occurred predominantly, but not exclusively, in emerging economies.

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The recent global financial crisis is unusual in a number of important respects. It occurred after a period in which emerging-market-originated financial crises and risk levels seem to have declined substantially (Taylor, 2009, pp.38-9). Also, this crisis occurred after a period of sustained high growth and lower income volatility and sustained low inflation (the 'great moderation'), at least for many developed economies. Moreover, the crisis was triggered not in an emerging economy but in the world's largest and most advanced economy, the United States.

The origins of the global nature of this crisis were not simply US policies. Global economic and financial relationships that evolved over the preceding decades were an important pre-condition. What is more, the origins have an important Asia-Pacific dimension. The crisis arose from a potent constellation of events which included the growth strategies of emerging economies in the Asia-Pacific region. These strategies led to global financial imbalances. These imbalances, when combined with the monetary, fiscal and regulatory policies in the United States, exposed the risks of disintermediation, corporate governance practices and financial innovations, and contributed to a housing bubble. Given the magnitude of the US economy and the seriousness of the financial shock in the US, the crisis reverberated back across the region, and globally, with potentially important implications for the future Asia-Pacific growth process.

Export-biased growth and convergence in Asia-Pacific

There are several parts to the process that precipitated the recent global financial crisis of 2008 and 2009. One important part was the process of rapid economic growth centred on the Asian region, and in particular the importance of export-biased growth for China and other emerging economies in the region.

Deng Xiaoping's reforms in China since 1978 and the liberalisation of India's economy after the crisis of 1971 heralded a remarkable period of growth in the Asia-Pacific

region and what could be described as the 'Third Industrial Revolution'. Together with the more recent emergence of other Asia-Pacific economies, such as Vietnam and Peru, and at earlier stages in the region of Korea, Singapore and Chile, for example, these economies have transformed global production chains and global financial linkages and have generated a wealth gain to the world. This wealth gain has been manifest in reductions in the real price of consumption goods. It has also triggered significant terms of trade gains for economies, such as Australia, New Zealand and Canada, supplying raw materials to these rapidly emerging economies. For the Asia-Pacific region as a whole, this remarkable transformation resulted in the world's centre of gravity of economic activity gradually shifting towards the region and income convergence in the region (see Buckle and Cruickshank, 2008).

The process of rapid economic growth in the more successful emerging economies was also characterised by a dependence on export-biased growth. There are a number of reasons for this. On the one hand, financial market underdevelopment in emerging economies makes it more difficult for domestic savings generated by higher income growth to be recycled into the local economy. Furthermore, uncertainty with respect to the provision of public goods or social security in public health systems and education systems can lead to precautionary saving and a higher rate of saving overall and hence a lack of domestic recycling of the income growth, particularly if financial markets are underdeveloped.

Export-biased growth became a feature of China's growth process from the early 1990s after it became apparent that domestic demand was not growing fast enough to absorb the rapid investment-led growth in the production of manufactured goods. While retaining investment-driven growth, there was a switch towards exports and substitution of domestic production for imports to absorb the rapid expansion in manufacturing capacity, particularly in the coastal and urban regions. China in fact became an integrator of global and regional production networks, being a net importer from Japan, Korea, the ASEAN countries, Australia and India and a massive net exporter to the US and the European Union (Wong, 2007).

The disruption to growth and economic development caused by the Asian financial crisis in 1997/98 also prompted a stronger emphasis on export-biased growth in the region. Following economic liberalisation, rapid economic growth in these Asian economies resulted in high growth in imports and increased dependence on foreign capital to finance their investment. For many Asian banks, borrowing was in foreign currency while lending was in their national currency. This meant they were exposed to the risk of sharp changes in

China's export development model was underpinned by pegging its currency to the United States dollar at an undervalued rate in order to generate trade surpluses and accumulate foreign reserves.

the exchange rate. When the crisis did occur, banks and corporations suffered severe financial losses. For example, the Indonesian rupiah lost 80% of its value almost overnight. Bank and corporate foreign currency exposures led to severe losses. Indonesia's GDP fell by 4% in the first year following the crisis, and it was some three years later before its GDP recovered to the pre-crisis level. South Korea recovered more quickly, as did Malaysia, but Thailand suffered a long period of stagnation after the crisis.

The public sectors in the crisis-affected economies incurred significant fiscal costs to bail out their bankrupt financial systems. Caprio and Klingebiel (2003) estimate that for Indonesia the fiscal cost of the Asian crisis was about 55% of its GDP. For Thailand the estimate was over 30%, for South Korea about 30% and for Malaysia about 17%.

Although one of the consequences of the Asian crisis was that financial systems improved, it also meant that many governments in the region became reluctant to allow their economies to run up current account deficits. There has been a fear of exchange rate floating and a preference to maintain an undervalued exchange rate to support a strong current account position. The Chinese government certainly observed what happened to its neighbours in 1997/98 and concluded that it would not allow anything similar to happen in China.

The Asian financial crisis set the scene for the emphasis in subsequent years on export-biased growth in China and other emerging economies in the region. China's export development model was underpinned by pegging its currency to the United States dollar at an undervalued rate in order to generate trade surpluses and accumulate foreign reserves. In order to give effect to this process, the monetary authority in China has had to sterilise the potential effects on the domestic money supply by issuing government bonds and by increasing the reserve requirements of its financial institutions.

Another lesson of the Asian financial crisis was to ensure robust financial institutions and systems. While this has helped the emerging Asian economies to weather the current crisis, ironically the development of production and financial linkages that have aided growth and convergence in the upswing years, and the dependence on export demand, have also played a significant part in exposing these economies to the contagion effects of the current crisis. What was an advantage in the period leading up to the recent crisis has been exposed as a weakness in this crisis.

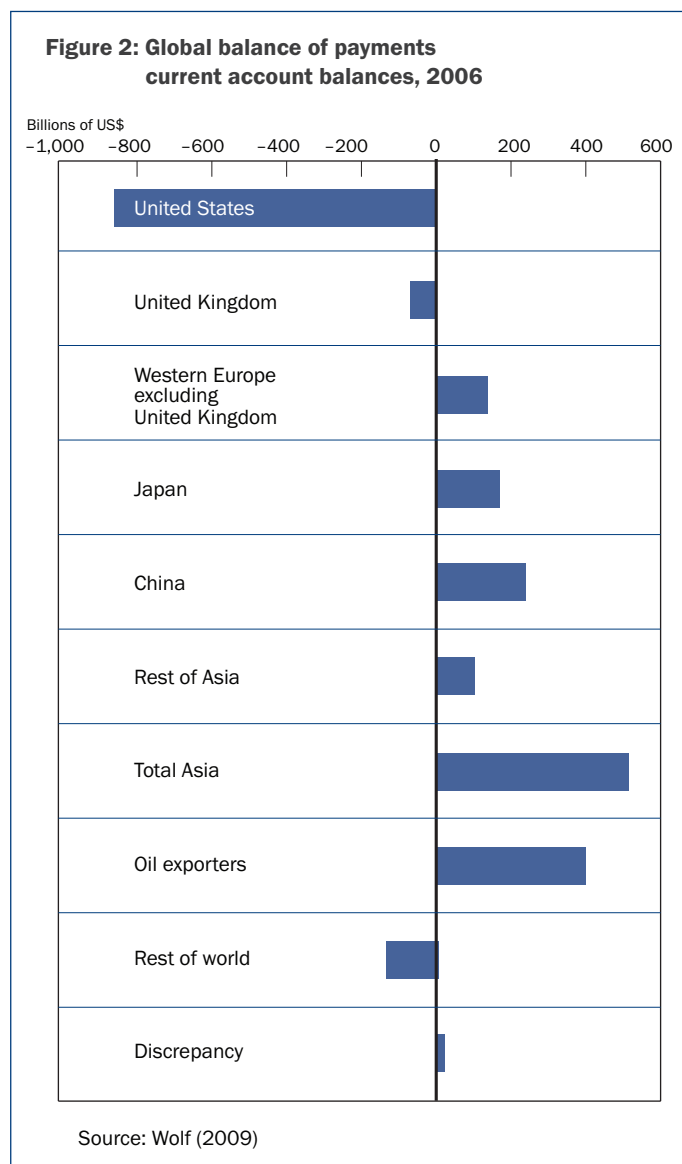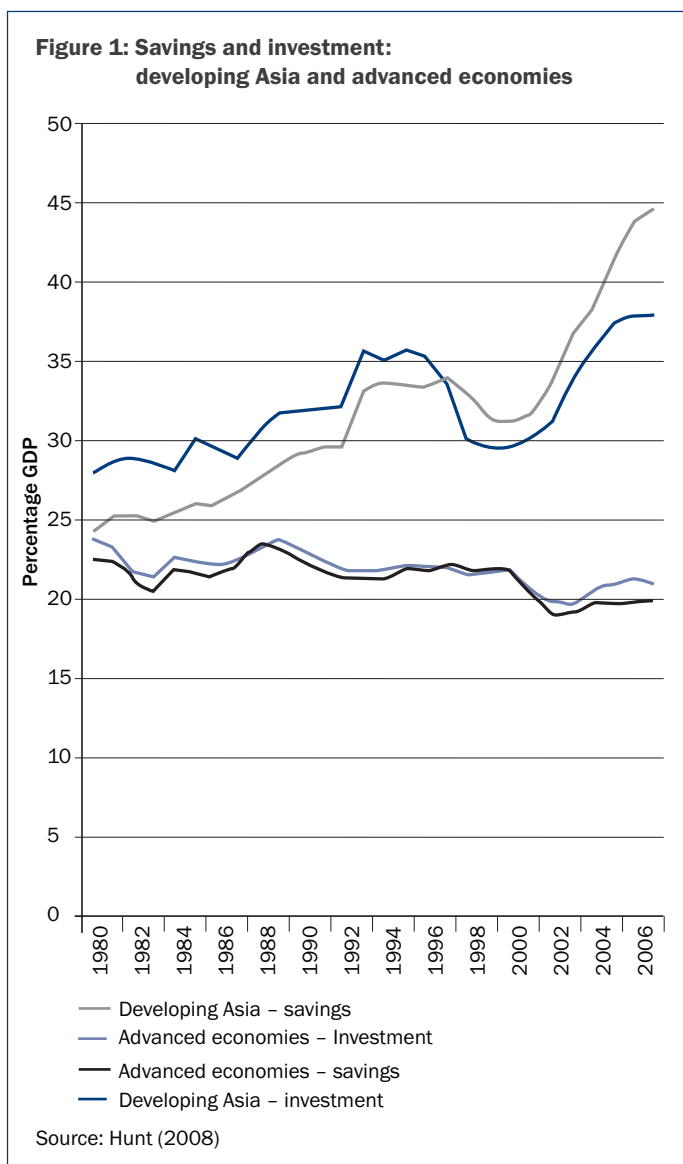### Global imbalances (or 'Bretton Woods II')

The emphasis on export-biased growth, growing current account surpluses and increasing foreign reserves in the

Asian region, particularly in China, was an important ingredient in the emergence of global imbalances, a savings glut and excess liquidity during the lead-up to the current financial crisis. High domestic saving and large current account surpluses had been particularly evident in China. While Chinese households tended to save at a very high rate, a rise in Chinese corporate savings, including saving by state-owned enterprises, has been at the core of the rapid rise in China's savings (see Wolf, 2009). The government itself has also been a large saver. For similar reasons, the surge in oil prices and oil revenues for oil exporting countries added to the glut of savings in these economies.

The consequential current account surpluses of China, other Asian economies and oil exporting economies were recycled to enable persistent current account deficit economies such as the United States, Spain, the United Kingdom, and the smaller developed Asia-Pacific countries of Australia, Canada and New Zealand to consume and invest far more than their domestic income would otherwise enable. As Hunt (2008) has pointed out, prior to the current crisis there had been a rapid growth in savings in emerging Asia compared to

the recovery of investment in this region. In contrast, there had been a secular decline in the investment rates and an even larger fall in savings rates in advanced economies (see Figure 1), a process made possible by the recycling of savings in the former group to finance the dissaving of the latter group.

The IMF (2005) attributes the decline in advanced economy saving rates to increased access to credit facilitated by various financial market innovations, a decline in public saving in some advanced economies such as the United States, and an increase in elderly dependency rates in economies such as Japan. The IMF considers that declining investment rates, particularly in Europe and Japan, are due to demographic trends and reduced investment requirements for industrial economies as a whole. But the key point is that despite stronger investment growth in the emerging economies, saving rates increased even further and despite a secular decline in investment rates in advanced economies, saving rates there declined even further. These differences were manifest in balance of payments current account balances (see Figure 2). The distribution of these balances

Figure 1: Savings and investment: developing Asia and advanced economies

Source: Hunt (2008)

Figure 2: Global balance of payments current account balances, 2006

Source: Wolf (2009)

is reflective of the important financial relationships that emerged, particularly between the world's largest (and highest income) economy, the United States, and many emerging economies, and notably China.

The co-dependence between the respective saving rates, current account balances and corresponding financial capital flows has been termed by Dooley, Folkerts-Landau and Garber (2004a, 2004b) 'Bretton Woods II', in acknowledgement of the similarity to the type of financial arrangements that evolved under Bretton Woods institutions during the postwar years. Under Bretton Woods the reserve currency was also the US dollar. In that era, savings in Japan and Europe supported the US dollar and funded the US current account deficit that was being used to finance US consumption and investment growth, and eventually the war in Vietnam. The system ended in 1971 when US-dollar convertibility into gold was suspended, the US dollar was floated and other countries broke from pegging their currencies to it.[2]

Current account imbalances and the corresponding flows of financial capital can be an important means by which resources in net saving economies are lent to countries that are dissaving. Provided relative prices are able to adjust appropriately, this process can lead to a more efficient global allocation of savings and investment. Sometimes the unwinding of these 'imbalances' is painless, especially when the investment consequent on these transfers generates revenue to warrant the earlier borrowing or dissaving. At other times they can be a painful process, particularly when speculative attacks result in exchange rate adjustments that significantly increase the cost of debt to the borrower countries, as occurred during the Tequila crisis of the mid-1990s and the Asian financial crisis of 1997/98.

The global financial imbalances of the new millennium were, however, rather different from past experiences. The direction, at least in net terms, of the capital flows was predominantly from emerging markets to developed economies. Moreover, these flows were dominated by the relationship between China and the US, where China in effect became the banker for the United States. In other words, in Bretton Woods II, the US was the principal destination for this glut of savings in the emerging economies, and the level of savings in China in particular was the largest source of savings. According to Wolf (2008), the US was absorbing about 70% of the surplus savings in the rest of the world.

Governments in emerging economies were directly responsible for much of the recycling in the form of capital outflows from those economies. This has occurred either because domestic residents were not able to hold foreign assets, as in China, or because most of the export revenue

Prior to the outbreak of the current crisis, property price booms had been spreading across several economies. In 2006 nominal house price inflation exceeded 10% in eight out of 18 OECD economies.

accrued to governments, as in many of the oil exporting economies. Hence there emerged large sovereign wealth funds.

The implication for exchange rates was significant. One of the reasons for such large current account surpluses for emerging economies was the management of exchange rates in order to maintain export competitiveness. The surpluses were used to purchase United States assets, thereby assisting to maintain demand for and the value of the US dollar, preventing it falling against their own currencies. This process has been described as 'vendor financing', in recognition of the fact that countries with large volumes of exports to sell have been financing their biggest market.

A key feature of this process was that, in contrast to borrowing by emerging economies, because it is the issuer of an international reserve currency the US has been able to incur debt denominated in its own currency. This significantly changes the distribution of risk compared to when emerging economies were borrowers leading up to the Asian and Tequila crises, for example. The distribution of risk is relevant when we consider the potential implications for emerging Asia-Pacific economic relationships and growth in the post-crisis period.

All else being equal, an excess of investment over savings, as has occurred in the US and other advanced economies, should lead to an increase in long-term interest rates in those economies. However, the Bretton Woods II process of intermediation had the effect of providing easy credit and depressing United States and global long-term interest rates (see Figure 3).

The process of global imbalances and global intermediation had another important effect. By recycling savings to purchase US financial assets and supporting the US dollar, the resulting elevated real exchange rate for US tradable goods and services disadvantaged producers in that sector, causing it to shrink (as manifest in the current account deficit). The reason this didn't result in a much earlier recession in the US is that, in contrast to the household sector in China, the household sector in the US was dissaving and maintaining high rates of demand for non-traded goods, particularly high rates of residential investment. An expansionary US fiscal policy was another important factor sustaining US non-tradable demand.

United States policy: triggering and prolonging the crisis
Politicising the housing market

Prior to the outbreak of the current crisis, property price booms had been spreading across several economies. In 2006 nominal house price inflation exceeded 10% in eight out of 18 OECD economies. This boom was particularly evident in, but not restricted to, Anglosphere countries (the US, UK,

Figure 3: Global long-term interest rates
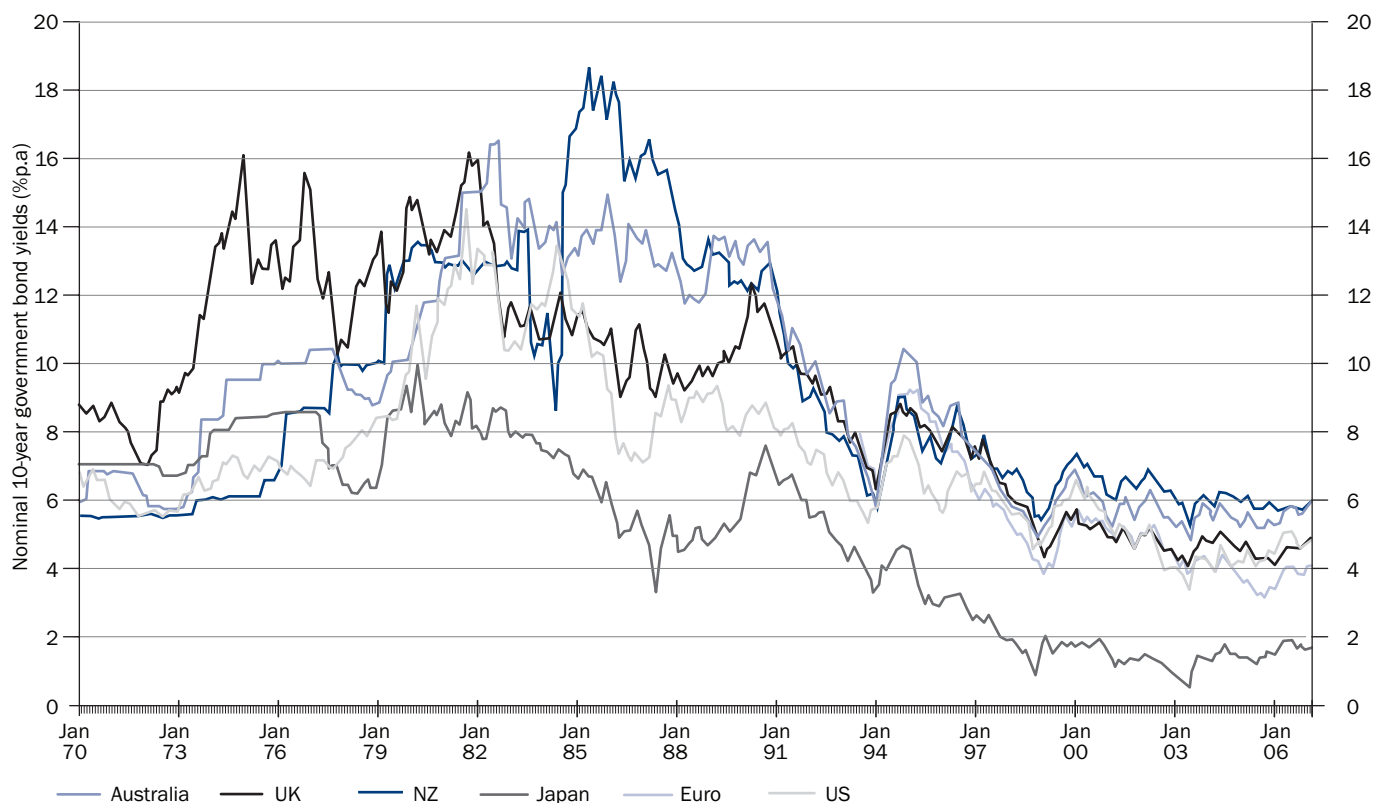
New Zealand, Ireland, Canada, Australia), described by Ferguson (2008) as the first property-owning democracies. For the United States, the basis of this property-owning democracy was developed particularly during the latter part of the Great Depression. The New Deal introduced many of the institutional features of current US housing policy which have underpinned the US housing market. Indeed, Ferguson suggests that the most successful and enduring component of the New Deal was how it transformed the US housing market.

During the Depression, US mortgages were typically short-term, and were not amortised. The establishment of the Federal Housing Administration provided federally-backed insurance for mortgage lenders, and encouraged large, long-term, fully amortised low-interest loans (Ferguson, 2008). The foundation for a national secondary market was established with the introduction of the Federal National Mortgage Association ('Fannie Mae'), authorised to issue bonds and use the proceeds to buy mortgages from local Savings and Loans associations (S&L). S&Ls became the foundation for growing property ownership in the post-Depression years.[3]

From the 1930s onwards the US government was effectively underwriting the mortgage market (Ferguson, 2008). Before the 1930s about 40% of American homeowners were owner-occupiers. Today that figure is close to 70% (as it is in other parts of the Anglosphere).

This structure came under threat in the late 1970s and 1980s when, in the wake of Paul Volcker's higher interest rate anti-inflation strategy, less regulated financial institutions were able to compete more effectively for deposits. To restore the position of Savings and Loans associations, the

Carter and Reagan administrations provided tax breaks and deregulation (see Ferguson, 2008, p.254). The crisis resulting from the mismatching of assets and liabilities, and fraudulent practices, was a clear lesson in the consequences of well-intentioned but poorly designed regulation. It did not have the global implications of the current crisis, but it provided the opportunity for investment banks and the less regulated financial sector to establish a stronger presence in the mortgage market and to develop financial instruments such as mortgage-backed securities.[4] Moreover, the majority of mortgages still qualified for an implicit guarantee from the government-sponsored enterprises (GSEs) 'Fannie Mae', 'Freddie Mac', and 'Ginnie Mae'.[5]

Politicisation of the housing market continued under the Bush administration, as highlighted by President Bush in December 2003 when he remarked: 'it is in our national interest that more people own their home' (cited in Ferguson, 2008, p.267). The combination of declining real interest rates, political support and financial innovations appeared to have markedly boosted home ownership. In the ten years from 1995 to 2005, home ownership increased from 64% to around 70%. Ferguson (2008) suggests that half of that can be attributed to the sub-prime lending boom.

The sub-prime crisis
The history of financial crises suggests that financial deregulation tends to be followed by financial innovations. These innovations can lead inadvertently to higher risk which raises the probability of financial failure. In recent years, many countries have abolished regulations limiting the range of activities in which their banks can engage. One

explanation for these regulatory reforms is that this enables greater diversification of assets and liabilities needed to withstand shocks (Adalet, 2007). In the US, the Glass-Steagall Act (1933) restricting commercial bank involvement in investment banking was abolished in 1999. This removed restrictions on mixing commercial and investment banking, and it allowed commercial banks, and insurance companies like AIG, to encroach on the traditional investment banking services.

Eichengreen (2008) observes that while this was basically sensible policy, based on a model that had proved viable in Germany and other parts of Europe, in the US financial environment it had serious unintended consequences. Investment banks were forced to develop new lines of business to sustain their profitability. It created an environment that prompted the originate-and-distribute model of securitisation, the extensive use of leverage and the growth of the sub-prime mortgage market.[6]

The sub-prime model relied on low interest rates, rising real estate prices and mortgagees maintaining their ability to service the mortgages. Taylor (2009) suggests there is a dynamic interaction that tends to accentuate risk-taking. When house-price inflation is high there is a tendency for housing foreclosure and delinquency rates on adjustable-rate sub-prime mortgages to fall. This probably reflects the benefits of holding onto a house and working longer hours to meet the mortgage payments when house prices are rising rapidly. The declining rates of foreclosure and delinquency that occurred in the US during the early part of the millennium may have confused many, including rating agencies, as to the true extent of risk. This problem would have been accentuated by the complex securitisation techniques that evolved during this period and led to what Taylor has described as the 'Queen of Spades problem' – where people don't know which securities had the bad mortgages in them.

Repackaged as collateralised debt obligations (CDOs) and with the assistance of favourable credit ratings, these sub-prime securities were transformed from risky loans into highly-rated investment-grade securities. The risk was spread across the globe to institutions seeking what were thought to be secure returns for pension funds, insurance funds, etc. However, the process accentuated the information asymmetry risks. Ferguson nicely captures the information risks:

Those who knew best the flakiness of sub-prime loans – the people who dealt directly with the borrowers and knew their economic circumstances – bore the least risk. They could make a 100% loan-to-value 'NINJA' loan (to someone with no income, no job, or assets) and sell it on the same day to one of the big banks in the CDO business. In no time at all the risk was floating up a fjord (Ferguson, 2008, p.269)

> The sub-prime model relied on low interest rates, rising real estate prices and mortgagees maintaining their ability to service the mortgages.

'Light touch' regulation in the US (and in the UK and parts of Europe), fragmented regulatory systems and failures of supervision are therefore considered by some to have played an important part in enabling the development of markets for CDOs and the global spread of these securities (see the discussion in Henderson, 2009). This process of globalising the risk exposed not just the US financial system but many parts of the global financial system to greater risk of contagion. When the Federal Reserve did start to raise interest rates from late 2004 through to 2006, huge numbers of sub-prime mortgage holders were not able to service the renewed higher mortgage interest rates, causing foreclosures which burst the real estate bubble. From 2006, US house prices started to fall for the first time since the early 1990s, and housing starts dropped like a stone. By 2007 the collapse of the US sub-prime mortgage market was reverberating across the United States and global financial markets.

US monetary policy: too late and off target?

The role of the US Federal Reserve and monetary policy is still hotly debated. During the early part of the new millennium, the Federal Reserve decisions were primarily concerned with the sharp slump in GDP growth, following the collapse of the dot.com bubble, a fear of the deflation that had plagued Japan in the 1990s and the impact of 9/11. To boost demand, the Federal Reserve quickly lowered the federal funds rate from around 6.5% to below 2% in late 2001. The rate was then gradually reduced to 1% and held there until early 2004.

Taylor (2009) is of the view that the Federal Reserve allowed this loose monetary policy to go on for too long. His argument is based on a comparison of Federal Reserve funds rate decisions from 2002 to 2006 with federal funds rate decisions that would have been made had the Federal Reserve followed the same decision-making rule used during the period of 'great moderation'. He argues that Federal Reserve interest rates in the period 2001–2004 represented an unusually large discretionary deviation from the usual decision rule. They fell well below what historical experience suggested the policy response should have been, and accentuated the US housing boom. This sharp easing in monetary policy contributed to the subsequent upswing in the business cycle and inflation, and therefore the eventual decision to lift interest rates sharply again from 2005 to 2006, decisions that were more in line with early monetary policy. While the period of low interest rates helped fuel the sub-prime mortgage market, the sudden reversal of interest rates contributed to the collapse of that market.

If this argument is correct, then the break in interest rate policy may not have been restricted to the United States Federal

Reserve alone. Ahrend, Cournède and Price (2008) argue that deviations from the 'Taylor rule' by central banks in several other countries contributed significantly to the housing booms in those countries. They demonstrate that countries with the largest interest rate deviations below what previous policy rules would have predicted experienced the biggest housing investment booms.

On the other hand, some consider it not credible to blame all the US excesses of recent years on US monetary policy (see, for example, Ferguson, 2008, p.267). Dunaway (2009) considers that because the yield curve in the US was relatively flat in the early part of the decade in response to the global 'savings glut', Federal Reserve increases in short-term rates may not have fully passed through into long-term rates.

It is difficult to identify the relevant weights we should attach to central bank interest rate decisions and the glut of savings from emerging economies in contributing to the global decline in real interest rates and the housing boom. What is clear is that this was a global phenomenon. The global connections could be explained by national monetary policies reacting to potential exchange rate appreciations that could have been prompted either by the glut of savings in emerging economies lowering global long-term real interest rates, or in response to the US Federal Reserve decisions to lower interest rates. Under either argument, central banks around the OECD economies would be observed to be simultaneously lowering short-term interest rates. These two arguments seem to be observationally equivalent.

Did US policy prolong the crisis?

Many have suggested the crisis can be dated from June 2007, when two hedge funds owned by Bear Stearns were revealed by Merrill Lynch to be insolvent. Bear Stearns bailed out one fund but let the other collapse. Rating agencies subsequently began downgrading residential mortgage-based CDOs and by the end of 2007, American Home Mortgage had filed for bankruptcy, mortgage investment funds were being suspended, Northern Rock was nationalised by the government in the UK, numerous hedge funds were wound up, and asset write-downs by banks eliminated hundreds of billions of US dollars from their balance sheets. What is more, the government-sponsored Fannie Mae (which under encouragement of government policy had significantly increased its share of US mortgages) was placed in serious risk of collapse.

US policy makers have also been criticised for prolonging the crisis. The US Treasury and Federal Reserve initially interpreted the crisis as if it was a liquidity problem. The Term Auction Facility (TAF) and the 2008 Economic

> The financial crisis spread quickly from the US to Europe, reflecting the direct vulnerability of Europe's financial sector to the US-originated credit exposures, as well as the adverse relaxation of credit standards within Europe itself.

Stimulus Package, and even the initial cuts in the Federal funds rate in the early part of the millennium (which contributed to a lower exchange rate and higher oil prices in US dollars) were focused on improving liquidity. However, Taylor and Williams (2009) argue that the principal underlying problem was one of 'counterparty risk'.[7]

The decline in house prices, reduced job security for homeowners and higher risk of bankruptcy are likely to have increased the risk of deterioration in bank balance sheets, causing greater concern about counterparty risk. Banks were criticised for not lending to traders or being reluctant to lend to each other. This has commonly been interpreted as a liquidity problem, whereas in fact the underlying problem may have been that banks were more concerned with counterparty risk.

The Taylor and Williams critique, and criticism by others such as Anna Schwartz (2008), implies that there was in the US, and possibly elsewhere, an initial diagnosis error by policy institutions, and implies that policy errors by policy makers not only sparked the crisis but may also have prolonged it. In any event, perceived risk levels seem to have declined following the implementation of the Troubled Assets Relief Programme and the introduction of guarantees by the Federal Deposit Insurance Corporation, Federal Reserve support for the Commercial Bills Market and similar actions in other countries.

Prognosis and implications for Asia-Pacific growth

The IMF has described the current global situation as the outcome of 'the largest financial shock since the Great Depression' (IMF, 2009a). The collapse of the US housing and sub-prime lending markets, and the spread of toxicated assets across the financial centres of Europe, had such a powerful domino effect that what started as a financial shock turned into a global production slump. In October 2009 the IMF forecast an annual decline in global GDP in 2009 of 1.1% (IMF, 2009b). This compares to growth of 3% in 2008 and 5.2% in 2007, and represents a negative turnaround of over 6% growth in two years! (see Figure 4). If this proves correct, it will be the first annual fall in world GDP in the postwar era.

These forecasts reflect a feature of this global recession that Bollard and Ng (2009) consider distinguishes it from previous global recessions of the postwar era. The financial crisis spread quickly from the US to Europe, reflecting the direct vulnerability of Europe's financial sector to the US-originated credit exposures, as well as the adverse relaxation of credit standards within Europe itself. The eventual spread to emerging economies, including China and many other parts of the Asia-Pacific region, has been primarily through trade and commodity price channels. The financial shock

had an adverse impact on confidence and wealth in advanced economies, causing a slump in consumer and investment demand, thereby transmitting the shock to the traded-goods sectors and to commodity prices via the traditional channels. The IMF expects the volume of world trade to fall by 11.9% in 2009 and commodity prices to fall by 30.6% for oil and 20.3% for non-oil commodities.

This unusual characteristic is reflected in the IMF forecasts, which are for advanced economy GDP to fall by 3.4% this year, a growth reversal of 6.1% in two years. Emerging and developing economy GDP growth is expected to grow by only 1.7%, a growth reversal as severe as for developed economies. China and India are expected to be more resilient and grow by 8.5% and 5.4% respectively in 2009, but this is still below growth in the previous two years.

How will this crisis and the ensuing global recession influence the Asia-Pacific growth process in the future? The global financial crisis has exposed the weaknesses of the pre-crisis model of export-biased growth dependent on US and EU domestic demand growth. What had been an advantage for emerging economies under Bretton Woods II prior to the crisis has proved to be a weakness during the crisis.

While the lessons of the Asian financial crisis were absorbed and have been applied to improve the resilience of financial markets in the Asian region, the effects of the current crisis are particularly apparent in the collapse of exports in the region. The inevitable slump in China's exports has been accompanied by a decline in China's import growth and hence its demand for output from other Asian economies. Cyclically sensitive high-tech manufacturing exports were hit particularly hard and Asian manufacturing exports were more severely affected than during the dot.com crash and the late 1990s Asian financial crisis (IMF, 2009a). This was particularly the case in Thailand, Singapore, Korea, Taiwan, Malaysia and Japan (Figure 5). Asia's tightly integrated supply chain, a feature that promoted high growth during the preceding decade, propagated the effect of the US and European slump across the region.

Furthermore, the risks to emerging economies of the Bretton Woods II model of 'vendor financing' have also been exposed. Foreign central banks, like China's, and sovereign wealth funds that have invested in US Treasury and other

Figure 4: Global economic growth and IMF forecasts
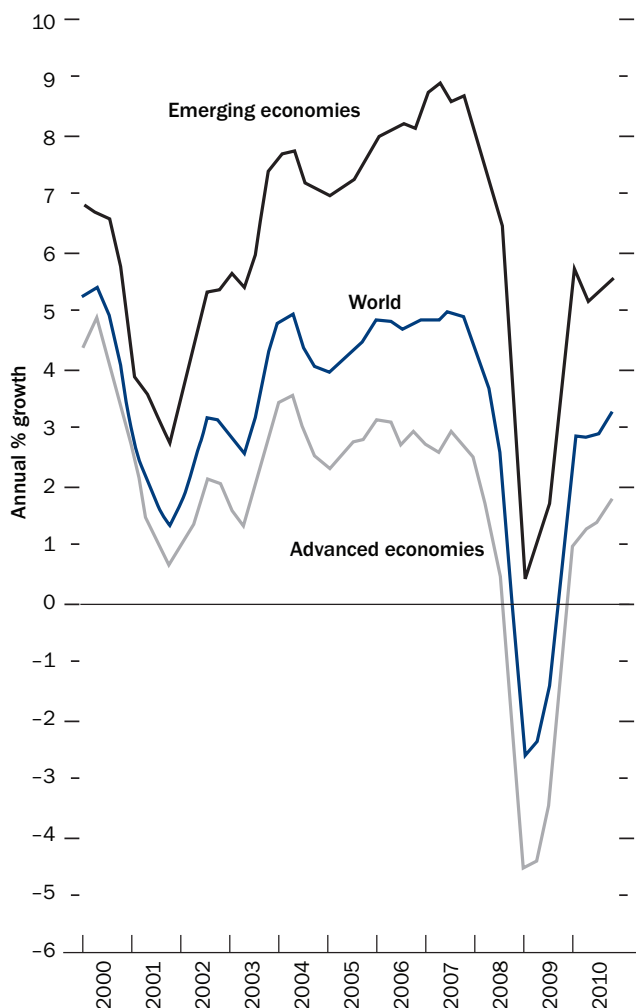
Source: International Monetary Fund (2009), http://www.imf.org/external/pubs/ft/weo/2009/02/c1/fig1_pdf)

Figure 5: Asian high-tech manufacturing exports
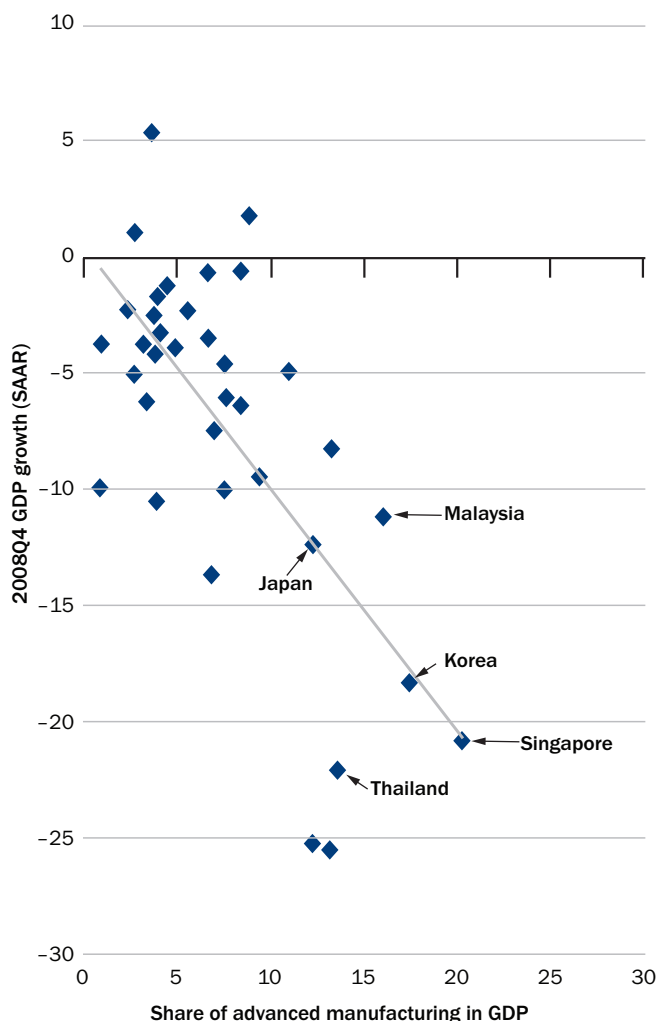
Source: International Monetary Fund (2009a)

agency securities and which have financed the large US current account deficits of recent years, have suffered immense capital losses. Moreover, because these investments are typically denominated in US dollars, the reserve currency, they are highly exposed to exchange rate risk. Foreign central banks and sovereign wealth funds holding US dollar-denominated assets remain vulnerable to a fall in the value of the US dollar should the Bretton Woods II model not be sustainable.[8]

An alternative future growth scenario is one in which saving rates in developed economies increase or growth continues to stagnate, and there is a shift away from the heavy reliance on export-biased growth by China and emerging economies and a greater reliance on domestic demand to sustain production.

Declines in house prices and financial wealth have affected consumption spending in the US as households attempt to rebuild wealth. US household saving is rising and is expected to continue to rise above its current level (Dunaway, 2009). Furthermore, the effectiveness of the Federal government fiscal expansion plans has been hindered by concerns at the prospect of an emerging fiscal crisis in the US and by attempts by many state governments to restore their fiscal balances. The US Federal fiscal deficit is expected to be 5.5% of GDP by 2019, and national debt accumulate to the levels immediately after World War Two when the US was paying off war debts (Auerbach and Gale, 2009). At some point US government saving will also have to rise. Europe and Japan also seem unlikely to provide an alternative source of demand recovery. There seems little scope for fiscal and consumption-based growth in Japan, which seems likely to remain dependent on export demand, particularly from China.

Attention therefore inevitably turns to Asia, and in particular whether China will be able to rely more on domestic demand as the engine of growth. Many commentators have noted the sectoral and geographical imbalances and the income inequality and rural discontent that China's growth process has to date created. The Chinese leadership had been aware of the need for change even before the global financial crisis. At the fifth Party Plenum in October 2005 the 11th Five-Year Plan was adopted, calling for a redirection of China's growth strategy, one that is more broad-based and more balanced and sustainable (Wong, 2007). The global situation since the financial crisis has provided further impetus for change in China. China has started to move more strongly in this direction by instructing state-owned enterprises to invest reserves in domestic infrastructure and to maintain employment and boost domestic spending. It is also converting its huge stock of foreign reserves into claims on resources around the world. But China still faces a difficult transition, that will require financial reforms (to improve the intermediation of savings) and the removal of price

> **There seems little scope for fiscal and consumption-based growth in Japan,** which seems likely to remain dependent on export demand, particularly from China.

distortions (including the low cost of capital and undervalued exchange rate) that have underpinned the investment and export-biased growth process of the previous stage of its development.

It seems unlikely therefore that the Asia-Pacific growth model based on export-biased growth from emerging economies and vendor financing of imports by developed economies (the US in particular) will be sustained in the post-crisis era. If advanced economies start to save more as households start to restore housing equity and governments start to tackle the fiscal deficits that have rapidly emerged from the crisis, external deficits in developed economies will start to decline in the post-crisis era. Higher saving rates by advanced economies will impact on the export and foreign investment environment for emerging economies.

If saving rates do rise in advanced economies, sustained growth convergence that has characterised the Asia-Pacific region during the past two decades will require lower saving rates in emerging economies and a greater dependence on domestic demand to restore their relatively high growth rates. But a new model based on stronger domestic demand growth in emerging economies will require sectoral rebalancing, and structural and real exchange rate changes that enable these economies to attract a greater share of domestic and advanced economy savings. The transition to this new model will take time and may result in slower Asia-Pacific and global growth in the immediate future, but it may also provide a more robust basis for sustained growth and reduced risk of financial crises.

Conclusion

The recent financial crisis resulted from the conjuncture of events that included growth strategies and exchange rate policies in emerging economies, investment decisions of central banks in these emerging economies, including oil exporting economies, the financial innovations that were spurred by US regulatory changes, and corporate governance practices. Previous postwar financial crises in the US, such as the Savings and Loans crisis, did not have the same global impact that the recent crisis had. The conjuncture of US and European financial practices and emerging economy growth strategies propelled the collapse of the US sub-prime mortgage market into the worst global financial shock and recession of the postwar era.

The crisis exposed the risks of global imbalances (or Bretton Woods II) of the last two decades, and the vulnerability this process presents for emerging economies striving to 'catch up'. The risks of the model of export-biased growth were exposed. If the Asia-Pacific region is to restore its position as the engine of global growth, if emerging economies are to retain the impressive rates of growth and convergence of

the last two decades, a new growth model will be needed, one more dependent on domestic demand growth and recycling of saving towards, rather than away from, those economies.

The implications for developed economies on the periphery, such as New Zealand and Australia, will be important. The success of the growth transition in China, and other emerging economies in the region such as Vietnam, will have an even more important impact on commodity prices and on the opportunities to exploit these growing markets, particularly if the US economy fails to recover to the growth rates of the pre-crisis era. Similarly, the diversification of Asian saving away from the US market could have a significant impact on exchange rates in these countries, particularly if China continues to manage its exchange rate. The global financial crisis may not necessarily be epoch-defining, but it seems certain to provoke a significant change in Asia-Pacific growth dynamics.

2   There have been other periods when global savings flowed from one region to another. An example is the pre-World War One gold standard period, when the industrial economies of Britain, France and Germany financed the development of resource-intensive regions such as Australia, Canada, New Zealand and some of the southern-cone economies of South America.

3   The New Deal also introduced federal deposit insurance, while mortgage interest payments had been tax deductible since the inception of the federal income tax in 1913.

4   In 1980 only 10% of the US home mortgage market had been securitised, but by 2007 this proportion had risen to 57% (Ferguson, 2008, p.260).

5   In 1968 the operations of Fannie Mae were split in two: the Government National Mortgage Association (Ginnie Mae), catering to poor borrowers, and a re-chartered Fannie Mae established as a privately-owned government-sponsored enterprise (GSE). Two years later, to provide some competition in the secondary market, the Federal Home Loan Mortgage Corporation (Freddie Mac) was established. The effect was to again broaden the secondary market for mortgages and, in principle, provide lower mortgage rates.

6   Henderson (2009) provides an excellent description of the 'originate-and-distribute' model of housing finance and the information asymmetries that emerge by breaking the process into five critical links: the originator, the packager, the rating agency, the repackager and the credit insurer.

7   Counterparty risk is a situation in which banks become reluctant to lend to each other because of the perception that the risk of default on loans has increased and the market price of taking on such risk has risen. This situation requires a focus on the quality and transparency of bank balance sheets.

8   Concerns about the sustainability of the Bretton Woods II model and emerging economy vulnerabilities prompted calls to boost resources for international financial institutions. The G20 leaders, for example, agreed at a meeting in London in March this year to strengthen financial supervision and regulation and make an additional US$850 billion in resources through international financial institutions such as the IMF (including a boost to SDR allocation), World Bank and other multilateral development banks, and to speed up reform of these institutions to ensure national representation is more in line with the changing global economic balance.

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Mike Reid

The Problem with Defining Core Services

One of the fundamental challenges faced by those who design governance systems involves determining at which level of government public decisions should be made, and whether the decisions are overwhelmingly political, managerial, technical, or should be left for citizens to make themselves. When designing democratic systems one of the critical considerations is ensuring that decision-making power is well distributed to avoid risks to citizens' liberty. These questions are currently on the minds of people involved with local government.

Since its election in 2008 the current government has initiated a number of policy debates that directly broach the question of who should be making decisions about the nature and role of local government. While the question of Auckland governance (see Reid, 2009) has been in the headlines, the debate has recently been extended by the addition of two further issues: who should determine what councils do and how should this occur? It is an issue which burst into life with the release of a Cabinet paper entitled 'Improving Local Government Transparency, Accountability and Fiscal Management' (TAFM) (Cabinet Office, 2009). In that Cabinet paper, which signalled a review of the Local Government

Act 2002, the minister of local government, Rodney Hide, stated that councils should focus on core services, which in his view meant:

> while there is no definition of core services for local government, I would expect there to be general acceptance that it includes transport services (roading, footpaths and public transport); water services (water supply, sewage treatment, stormwater and flood protection) and public health and safety services (refuse collection and regulation of nuisances). (Cabinet Office, 2009, p.4)

Not surprisingly, the paper generated a flurry of activity as almost every group, from librarians to museum providers, sought to get their particular services on the supposed list.[1] However, it was far from clear whether the paper reflected government policy or ministerial wishful thinking. Following public release of the TAFM paper the opposition sought to expose discrepancies between the minister's minimalist view and a range of statements and initiatives endorsed by the prime minister suggesting much broader roles.[2] Since then

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the issue has continued to attract attention, driven particularly by the minister of local government's regular speeches on the issue. The following extract is typical:

> Ratepayers and citizens need much more say in what's done with their money, because they have to pay the price for the often silly and outlandish expenditure decisions of councils. If money is spent poorly and a project flops, it's the poor old ratepayer who foots the bill.
>
> There are plenty of examples of inappropriate council spending ñ Hamilton City Council's investment in the local Novotel Hotel and the South Taranaki District Council buying the Hawera movie theatre. One of the Southland local authorities even took ownership of a local Lotto shop! That's an outrageous use of ratepayers' hard-earned money.
>
> We are going to shift the balance of power back to ratepayers and citizens so they have the control they deserve. (Hide, 2009a)

While the minister's proposals are expected to have their first reading in Parliament before the end of the year, the issues he raises deserve somewhat greater scrutiny than they have so far received. This article attempts to answer at least four critical questions raised by the debate: What is the core service debate all about? How relevant are the minister's examples of non-core services? Is there a problem? And what are the likely implications for councils and their communities should the minister's plans go ahead?

What are core services?

According to the minister of local government and his officials, local government should have a core set of services determined by Parliament and these services are those associated with physical infrastructure and the protection of health, rather than services concerned with enhancing well-being. Councils that wish to offer services beyond the core would be required to get their citizens' permission, probably through some form of binding referenda. It is an idea that is worthy of somewhat greater scrutiny than it has so far received.

The notion that services provided by local governments can be divided neatly into categories of core and non-core is something about which there is little if any supporting theory. Most accepted theories which address the role of government, whether local or national, tend to be less definitive, accepting that such decisions are best not set in concrete as appropriateness is likely to be affected by changing technology, politics and values. A prescriptive act leads to volumes of amendments as situations arise that weren't envisaged. History suggests a fairly dynamic understanding of what services we think our public sectors should undertake. For example, today we no longer expect councils to run abattoirs, even though a few years

ago it was considered routine. Today citizens' have higher expectations of their local and central governments than they did a century ago, particularly with the growth of the welfare state since the Second World War. So the idea that we should fix roles and functions in legislation is at least curious.

Economic theory treats governments as having four primary roles: allocative, distributive, regulatory and stabilisation (Bailey, 1999). Distribution, regulation and stabilisation are roles that national governments are best positioned to undertake, whereas allocative functions are best undertaken by local governments (ibid.). The economic case for local government hinges on the value of decentralising or devolving services to lower levels of government in order to meet the diverse preferences of consumers, yet services probably should not be considered in isolation from form and finance. Thinking about the interrelationship between functions, form and funding, Bailey suggests that:

- local government should provide the majority of public sector services because their benefits are localised;
- local government should only provide services where the risk of local market failure is high and of government failure is low;
- the jurisdictions of local governments should as far as practicable be coterminous with the areas benefiting from the provision of their services;
- councils should be as small as possible, while still achieving economies of scale;
- matching of financing and benefit may require regional government for the provision of some services;
- scope for exit should be facilitated by increasing the scope for inter-municipal competition for residents and decentralisation of services within council areas.

Thinking about functions in relation to form and funding suggests a contingency and dynamism that is not captured in the current debate on core services, which has not really got beyond the suggestion of a list determined by Parliament. Bailey's work suggests that ideas about core services will vary according to the size of councils, how they are funded and the form of the local government system. For example, any idea of core is likely to be affected by the existence or otherwise of strong regional government. What might be core in the new Auckland is unlikely to be core in Waimate.

Citizens themselves, however, do have a sense that some local services are more important than others and when asked what these council services might be the majority of citizens tend to highlight the most recognisable. A nationwide

In popular conception, core is probably regarded as essential: that is, whatever other things councils do, we must have roads, water and sewage systems and the rubbish needs to be collected.

telephone survey commissioned by Local Government New Zealand in 2006 asked respondents what the top priorities for councils should be. The answers were roads and road safety (38% of respondents); water and sanitation (32%); town planning and environmental management (22%) and rubbish collection and disposal (19%). Other services were regarded as enhancements. Interestingly, when asked to identify what services are undertaken by councils most respondents could identify only three: rubbish collection and disposal; road and road safety services; and water and sanitation services. Core seems to be those things we use regularly and know for certain are provided by the council. In popular conception, core is probably regarded as essential: that is, whatever other things councils do, we must have roads, water and sewage systems and the rubbish needs to be collected.

> So 'core' is a fluid concept, which is likely to be contingent on technology as well as on political and community preferences.

One of the problems with attempting to define councils' services as being either core or discretionary, with the core defined by Parliament, is whether or not all councils provide them. For example, one of the minister's core services, according to TAFM, is rubbish collection. It would be a very expensive exercise if councils were to be required to ensure that all properties had access to a public rubbish collection service, as this is a service few rural communities currently have access to; it is a similar story with potable water and sewage. How can something be a core service if some councils don't actually provide it for many of their citizens? One way around this difficulty would be to create three categories of services, for example:

- mandated core services: determined by Parliament and required of all councils;
- mandated discretionary services: a list of discretionary services determined by Parliament that councils can adopt if they wish; and
- fully discretionary services: any lawful service that the community gives the council permission to undertake through a poll or referendum or similar means.

Something like the above appears to be the most logical move should the government wish to be more prescriptive about the activities councils undertake. However, are there other ways of conceptualising the notion of core services? As a noun, 'core' refers to the centre of things. For example, the core of the earth is the centre of the earth. If we take this definition and apply it to services and organisations we are probably referring to those services which are in some way at the centre of our organisations: that is, what they exist to

do. What organisations exist for is to fulfil their purpose, so surely their purpose should be at the centre of their role. The Local Government Act 2002 describes the purpose of local government in relatively abstract terms, namely:

a) to enable democratic local decision making and action by, and on behalf of, communities;

b) to promote the social, economic, environmental and cultural well-being of communities in the present and for the future.

In other words, local government exists to provide a way for communities to make decisions about their current and future well-being, bearing in mind that the rest of the legislation then puts limits around the extent of that decision-making power. Other jurisdictions take a similar approach to defining the purpose of their local government systems, with statements such as promoting 'the good governance of the community' or 'promoting well-being' common. The purpose statement in the Local Government Act 1974 was less succinct but similarly emphasised collective decision making. So, at the highest level of abstraction, the core of local government involves the process of collective decision making.

When approaching the matter of what local government should do there are two fundamental questions: who should decide, and is there actually a problem? Under the current legislation there are two mechanisms which determine what councils do: one is the passage of binding legislation by Parliament and the other is a decision supported by a majority of councillors in a formal meeting. Interestingly, the number of responsibilities Parliament has placed on local governments is relatively modest, particularly when compared to other countries, with the majority being regulatory functions carried out on behalf of the Crown. These are described in the Appendix to this article. The minister's announcements so far could be interpreted as suggesting that core services are those defined by Parliament and anything else will be discretionary. However, the minister goes slightly further, suggesting that decisions about undertaking any of these discretionary services should not be made by elected councillors. They should instead be made by the community itself, through a referenda process.

The problem of definition

The reification of core services in legislation fails to recognise the degree to which the range of services provided by councils tends to be dynamic over time. Today, no self-respecting city of any size could go without a medium-sized indoor sports stadium, reflecting growing community wealth and changing expectations. In the past it was normal for councils to operate abattoirs, ports, airports and, until the early 1970s, the fire brigade. Increasingly, councils are putting activities like art galleries, museums and zoos into trusts and companies in order to establish them as arm's-length entities and attract

investment from other parties. So 'core' is a fluid concept, which is likely to be contingent on technology as well as on political and community preferences. It is not a concept that fits well with the idea of nationally-dictated lists of permissible local activities.

A century ago, councils operated gas works and electricity departments, and Wellington City, for example, employed the conductor of the local sinfonia orchestra. As societies change, so does the range of activities we expect our local civic organisations to provide. In the sixties and seventies, as urbanisation increased, councils became operators of car parking buildings, and many still are. However, as improved technologies and higher demands have encouraged the private sector to become more active, other councils have moved out of this activity and left it to the market. In fact, the history of local government is one in which councils have shown a capacity to adapt to meet the needs of changing societies. Their proximity to communities means councils are better placed than Parliament to respond.

The proposal to define core services takes us back to the Local Government Act 1974, which had approximately 300ñ400 pages concerned with describing the activities councils were permitted to do. Yet despite this level of detailed guidance, councils frequently resorted to legal advice to ensure their intended decisions were within the law. Risk aversion was rife. The problem concerns our ability to define clearly the nature of a service. For example, while it may seem straightforward to put in legislation that running parks is a permitted activity, the definition of 'park' is likely to be contested ground. Will a sports field or a forest park be consistent with the definition of 'park' employed in the legislation? And will the right to provide parks extend to botanical gardens and scented gardens for the blind? How would the town belt of Wellington be defined? Is all of it a park, or only those areas specifically labelled as parks, like Hataitai and Newtown? Attempting to resolve these issues through legislation highlights the problems of blunt instruments.

Likewise, while the legislation might permit councils to operate museums and libraries, will it be legal to run a combined museum and library? Will the combined facility be defined as some new form of facility which does not appear on the list? While the definition of museum might be relatively clear in the popular mind, would Te Papa, with its interactive attractions, comply? If a museum includes live tuatara in its exhibitions, will it still be a museum, or will it have become a zoo and possibly outside the core? Do not laugh: this is what life was like under the Local Government Act 1974. The result was a range of quite perverse behaviours as councils sought to find ways around the limitations of statutory language in order to meet the needs and expectations of their citizens. Parliament simply lacks the information to make these kinds of judgements

and our society is, thankfully, not uniform enough to compartmentalise.

Defined lists make councils risk averse as their focus tends to shift from a concern with community well-being to the issue of whether decisions are legal or not. As well, measures which create recourse to lawyers in order to define the nature of each service increase the opportunity for gaming, as they allow external parties to utilise the core debate to drive the policy agenda, effectively undermining representative democracy. Given the contingent nature of most council services (even roads ñ it was only ten years ago that proposals were being discussed for taking them away councils), enabling locally-elected members in consultation with their citizens to determine the mix of services that best matches local preferences and willingness to pay is surely the most efficient choice.

New Zealand is a country of communities and they vary considerably. The local government framework currently gives councils substantial discretion which enables them to develop the appropriate mix of services to reflect the different communities they govern. For example, while the cost of roading dominates the budgets of most rural councils, in a few cases reaching 60ñ70% of their expenditure, in urban councils it is generally less than 20%. The challenging issues for most cities concern the soft infrastructures, like youth services, community safety and economic development. Is it reasonable to try and define a core set of services for a sector which is so diverse? Will we see a resurgence of local bills, as existed before the Local Government Act 2002, to validate local decisions taken to deal with local issues which were outside the core?

> ... the whole reform of Auckland is an indication that we need to adjust our governance arrangements to reflect local and regional diversity.

Will a list of parliamentary-defined core services enhance local democracy?

In practice, any list of services given the status of 'core' by Parliament is likely to enhance the status of those services in comparison to others, even if the others are more relevant to a particular community. Clearly that will be Parliament's intention, but is it desirable in the context of our goal of strengthening local democracy? One issue, which is noted above, is the risk that those councils not currently providing the defined services will come under community pressure to provide them, with corresponding pressure on funding for

smaller rural councils. In addition, a nationally-defined list will be seen as the default functions of local government and might be seen as representing a 'creeping centralism' which will, over time, result in greater homogeneity and standardisation and less diversity between councils. We are in a period in our history when the idea that Wellington knows best would attract almost universal scorn. Indeed, the whole reform of Auckland is an indication that we need to adjust our governance arrangements to reflect local and regional diversity. This suggests an appetite for greater diversity, not less.

Nationally-elected politicians are poorly placed to second guess the decisions of locally-elected politicians when determining, in consultation with citizens, the appropriate mix of local goods and services to match citizens' preferences and willingness to pay. These are seldom simple decisions

> Thought … needs to be given to developing a framework that allows for management of low-skill migration and, in these [domestic] jobs, a primarily female migration. This framework needs to keep multiple goals in mind.

as they involve trade-offs (the 'I want to do X but not if it means losing Y' debate) and are best made in a deliberative setting. There are also advantages in these decisions being made in multiple local settings rather than in one place, such as Parliament, as it diminishes the risk of policy capture by single-interest groups.

The New Zealand Parliament has the undisputed authority to make decisions about what councils do, if it chooses to exercise that authority. In the past, Parliaments have tended to approach this issue with some caution, as local government is part of a nation's constitutional framework and decisions that undermine local self-government effectively undermine its democratic framework. The critical aspect of a democracy is that governments are able to respond to the needs, expectations and demands of their citizens.

Even if Parliament approached the issue with due caution, there is still the question of whether or not a national body is in the best place and has access to the necessary information to determine the right mix of activities local authorities should undertake. Until 2002 local government legislation was generally based on the principle of ultra vires, which essentially limited councils to only those activities the legislation allowed. Not surprisingly, the legislation was often out of touch with the demands being made on councils, necessitating frequent trips to Parliament for amendments; for example:

- to allow the Wellington Regional Council to contribute to the costs of constructing the 'cake tin' in Wellington;

- the transfer of local facilities and tourism promotion from the three territorial authorities in Taranaki to the Taranaki Regional Council at the request of the territorials; and
- to enable the Hawke's Bay Regional Council to distribute port profits through a one-off payment of cash to local ratepayers.

In short, legislation is a blunt and inflexible instrument. Parliament is too far removed from the local coal face to know in advance what communities require and national politicians lack the appropriate incentives or flexibility to respond quickly to local needs.

The impact of defining core services on the role of councillors

New Zealand has a system of representative local democracy; that is, elections are held regularly in order to elect representatives to make decisions on behalf of their citizens, in a similar manner to the way in which central government works. Actions that interfere with the relationship between voters and elected members can be problematic, as they have the potential to reduce the elected members' decision-making sphere and undermine their accountability. The more the decision-making authority of elected members is constrained by higher-level governments, the less interest citizens are likely to take in local government. For example, a survey undertaken by the Local Government Chronicle in the United Kingdom identified the limited decision-making authority of councillors in that country as a major reason for poor voter turnout at local government elections. In the United Kingdom, constraints on councillor decision-making are caused by the highly centralised nature of their system and extensive use of nationally-determined performance targets.

Reducing the scope of councillor discretion is also likely to diminish the willingness of people to stand for elected office, as the opportunities to 'make a difference' will be considerably less than under a generally empowered regime. Certainly, early feedback Local Government New Zealand has received from some of its members suggests that many of them will reappraise their political futures if the role of an elected member is diminished further. The same applies to staff. Recent research undertaken by the Society of Local Government Managers suggested that officials would also find a more prescriptive and limiting approach to their council's role less satisfying from a job/career perspective. Key aspects of their work which they valued involved:
- a place where you can make a difference to peoples' lives;
service to the community;
- making the best of poorly-crafted government legislation;
- making a difference for the future; and
- working for the development of the city.

Requiring Parliament to define core services essentially removes the decision from local communities, who pay the

bill, and thus limits their ability to make trade-offs with regard to the use of their own resources. It may also require councils to undertake complex processes to go beyond the parliamentary list which are unlikely to be efficient. These decisions are best made locally; the question is, should they be made by local politicians elected by and accountable to local citizens, or by citizens themselves?

Measures to shift decision making from elected members to citizens themselves through referenda are likely to be quite problematic, as many of these so called non-core activities need only very minor resources to achieve their aims and are likely to cost less than the cost of a referendum. In addition, the evidence suggests that participation in referenda will be quite low, and likely to decrease over time if councils need to resort to them frequently. The result is that a small number of voters will be able to control council expenditure and activity. It is difficult to see this as somehow preferable to the current situation, where elected councillors make such decisions in open forum based on a consultative process. Presumably, those community facilities outside the core which are not supported by a referendum will need to be disposed of. Will important parts of our cultural heritage thus be up for sale because they are non-core?

Is there really a problem?
One of the astonishing aspects of this discussion is the lack of any proper evidence that New Zealand has a problem here. The core service debate appears to be driven by a perception that councils have extended their activities beyond what the majority of their citizens are prepared to pay for or what they have traditionally done. There is simply no evidence to back this view, particularly given the fact that New Zealand local government is one of the smallest local government sectors in the OECD and isn't growing significantly, as shown in Figure 1.

In the last five years, three separate inquiries have considered this question and each has come to the same conclusion: namely, that there is no evidence of any systemic increase in new activities undertaken by local authorities. The first study was undertaken by a joint officials group, the Local Government Funding Project. In its final report the officials state:

> no evidence to date has been produced to suggest that local government as a whole is undertaking a wider group of functions than it had prior to 2003. In cases where councils have taken on additional responsibilities these have proved to be quite small in scale and operational in nature. (Local Government Funding Project Team, 2006, p.18)

This view was reinforced a year later by both the report of the Inquiry into Local Government Rates and the Local Government Commission's review of the Local Government Act 2002. The report of the Rates Inquiry stated:
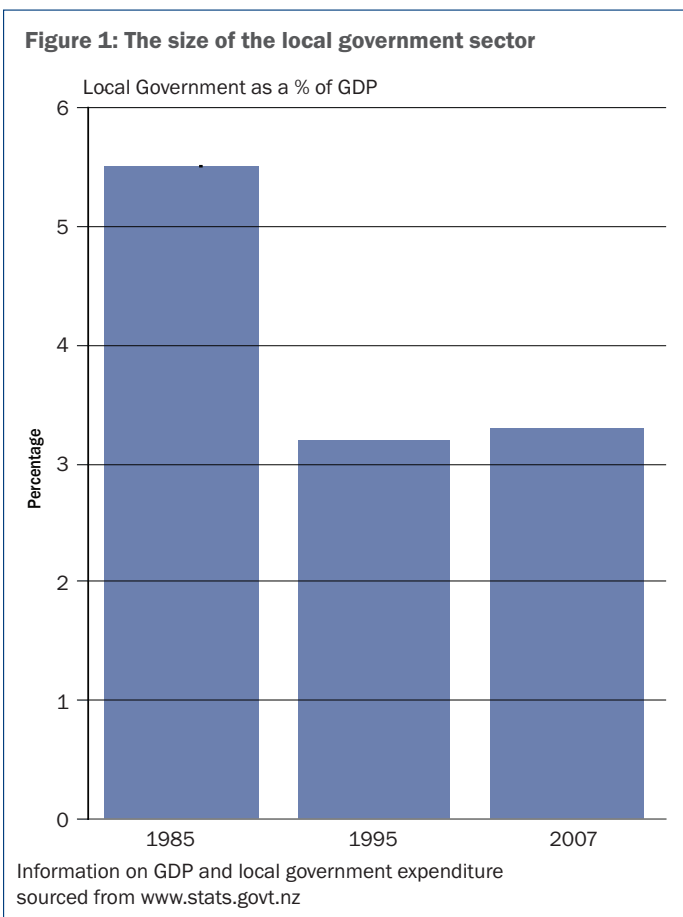
> The panel received many submissions suggesting the LGA 2002 has been a major driver of increased expenditures

in that it encouraged councils to move into activities outside their 'core business' by giving them a power of general competence. The Panel could find little evidence to support this. (Rates Inquiry, 2007, p.5)

To the degree that there has been change it is most pronounced in a few regional councils that have contributed primarily to regional economic development activities, such as investment in regional facilities. Rather than problems, these decisions should probably be seen as economically prudent, as the regions are better placed to spread the costs of these services over the full range of beneficiaries, one of the reasons for the reorganisation of Auckland. Yet despite systemic evidence to the contrary, the minister of local government continues to argue that local politicians are taking liberties and spending ratepayers' money on activities for which they have no credible licence, activities that are not core and for which they have not sought ratepayer or citizen permission.

So what do non-core activities actually look like? The minister has highlighted three examples, as noted earlier: the Hamilton City Council's investment in the local Novotel Hotel; the South Taranaki District Council purchase of the Hawera movie theatre, and one of the Southland local authorities' (Invercargill) ownership of a local Lotto shop. These examples deserve further consideration.

Hamilton City's investment in the Novotel Hotel represents a publicñprivate partnership between the city

Figure 1: The size of the local government sector

Local Government as a % of GDP

Information on GDP and local government expenditure sourced from www.stats.govt.nz

and Tainui, which was looking to invest some of its Treaty of Waitangi settlement resources in the local economy. While it is unusual for a council to invest directly in the operation of a hotel, it is not at all unusual for councils to offer incentives for business to locate in their districts, through, for example, a rates holiday. Hamilton City has every reason to expect the central government to support and encourage this investment as it fits very well with its national objectives to enhance Māori economic development and skills development. We should also add that the Novotel itself has made an important contribution to the economic performance of the city.

South Taranaki's decision to purchase the building that houses the town's only cinema and subsequently lease it back to the cinema operator must surely be seen in the context of a council acting to protect the town's heritage. Councils fund the preservation of our heritage in numerous ways, from giving grants, as Wellington City Council did to the Embassy Theatre Trust prior to the launch of The Lord of the Rings, to direct ownership of opera houses and town halls (and sometimes movies are shown in these buildings). Before making the decision to purchase the theatre, the council would have considered a full range of options for the building's preservation. It is difficult to think of the preservation of our past as somehow not being a traditional local government role.

The minister's criticism regarding the Lotto shop is puzzling as, seen from a different perspective, it is an example of a council being innovative and fixing a local problem ñ something the minister seems to want but is reluctant to allow councils to do. The background to the council and the Lotto shop story began with the closure of banks and their unwillingness to instal ATM machines in Bluff. Not only were local residents in need of cash, tourists who travelled to land's end often found themselves unable to stay and enjoy the local facilities for the same reason. After failing to convince the banks to provide an ATM, the council took the logical step of purchasing a Kiwibank franchise itself and placing it in the council's service centre. As it turned out, the Lotto shop was part of the franchise.

As a result of the council's initiative, locals and visitors now have access to funds and the service centre is generating an income to lower its cost to ratepayers. It is a solution in which everyone wins, except, apparently, the minister. What makes the minister's discomfort so surprising is that Lotto is actually a government-owned service. Hence, the council is helping the government by providing a base for one of its Lotto shops in a community that would otherwise not be able to access its money and spend it on what they want, including gaming and other local services. Why does the minister think this is a bad thing? Interestingly, the types of examples cited are not ones of councils making poor economic choices. In many instances the ratepayers benefit through lower rates. The criticism seems to be purely about a philosophy of not wanting things done if they are done by any arm of government. Economically, I would venture to suggest that few things of this nature undertaken by councils 'fail' as

councils tend to be very cautious in what they support.

The minister's rhetoric on the core service question has morphed somewhat since the beginning of his term. More recently it has begun to take an 'if you don't eat your greens you won't get any pudding' tone. Consider: 'I also believe, its crucial, especially so in these times, that councils ensure that core activities are properly identified and funded before spending occurs on more discretionary activities' (Hide, 2009b). Again, it is a position which begs the question: is there a problem and have we got data that suggest core services, or big essential stuff, is somehow being overlooked?

Interestingly, the best data are the various analyses undertaken of council long-term plans, undertaken by both the Rates Inquiry and more recently the Department of Internal Affairs, which looked at the new 2009ñ2019 plans. Both analyses show strong evidence of council expenditure dominated by capital investment in the three big infrastructures: roads, water and wastewater services. What this data tells us is that the Local Government Amendment Act (No.3) 1996, which introduced long-term financial planning in order to force councils to focus on their long-life infrastructures, worked, particularly after these plans became subject to audit following the Local Government Act 2002. In fact, New Zealand local governments are regarded as amongst the best asset managers in the local government world, with most Australian states having copied our approaches to asset management and long-term planning and our engineers selling their expertise internationally.[3]

There is, perhaps, one other evidence set we can look at to see whether or not councils have their focus on the minister's core services, and that is surveys of community satisfaction. What do citizens think about councils' performance on the development and maintenance of our big infrastructure activities? Councils undertake regular surveys to test citizen perception of the quality of their services; they are a useful window on how councils are perceived. In general, rankings tend to be highest for our basic infrastructure services. A sample of residents' satisfaction surveys taken in 2008 indicates relatively positive rankings for the major infrastructural services (see Table 1).

Table 1: Levels of satisfaction with infrastructure services[4]

	Wastewater	Potable water	Roads	Mayor/ councillors
Rotorua	78%	93%	80%	58%
Rodney	78.1%	76.1%	60.8%	58.4%
Waikato	42%	51%	58%	59%
Ashburton	81%	84%	78%	69%
Southland	94.1%	72%	75.9%	90.3%
Porirua	88%	94%	88%	N/A

While noting that in any jurisdiction there may be local issues, residents' views about the performance of their councils in relation to the delivery of the three large infrastructures does not suggest any systemic problem. Considering too their views of the performance of their elected members, which are all relatively positive, with the exception of Southland which is outstanding, the three infrastructures would seem to be the least of our problems.

When Parliament intervenes in the relationship between voters and their elected members, or second guesses the decisions made by local elected members after deliberating with their citizens, it risks weakening not only the framework of local democracy but also New Zealand's overall democratic framework. As Professor John Roberts wrote in 1968:

> The growing power of government, as evidenced by its ever increasing intervention in the economic and social affairs of the people, constitutes another reason for the existence of an efficient system of local government. While central and local government must share, as collaborative partners, the total task of governing the nation, an effective local government structure is an important counterweight to the growth of central government power. Local government is not solely a matter of the management of local services; it provides the democratic machinery for the expression of local opinion on all matters of public policy. (quoted in Boswell, 1981)

Councils provide a range of roles within our democratic system, including that of providing a valve for community discontent with national policies. If councils are to play their appropriate role in our democracy, citizens and their elected members need the authority to make decisions about their various localities. Parliament currently places obligations on local authorities with regard to some of the activities they undertake and the decision-making processes they operate. This is fair and reasonable. However, if democracy is to operate effectively, Parliament must be circumspect in how it exercises its authority and ensure that it focuses only on matters of national interest, supporting local democracy and allowing it to address those issues that are of local or regional nature.

Conclusion

As framed by the minister of local government, the issue of core services not only concerns the role of councils, it has a direct bearing on the capacity of councillors to make decisions. The minister has suggested that decisions to go beyond 'the core' might be left up to citizens themselves to decide, through a poll or referendum. The immediate concerns of the local government sector involve cost and complexity (imagine the cost of referenda in a city as big as the new Auckland) and the loss of flexibility to act as local issues and needs require.

However, referenda also provide additional opportunities for minority interests to influence or capture the allocation of public resources. International experience, for example in California, is replete with examples of wealthy single-interest groups exploiting referenda opportunities to promote their particular agendas. They also create the 'tyranny of the majority' problem. How likely is it that initiatives such as a marae development plan or a recreation project for disabled children would survive if dependent on community referenda? It is often only through strong and inclusive leadership by elected members that marginalised groups are acknowledged and treated equitably. These are judgements best made by elected members who can weigh up the benefits and costs and the overall contribution not only to the current generation but to future generations, and be accountable for them. Local Government New Zealand's research on rate capping (NZIER, 2009) shows that long-term planning models, in

We need cities and towns that are vibrant and innovative because without these qualities they will fail to attract the investment and the new citizens the country needs in order to prosper.

which elected members are responsible for making decisions in consultation with their citizens, are the most sustainable decision-making approaches.

How would, for example, the private sector work if Parliament determined what products it could produce and then required all shareholders to vote before major expenditure investments could be made? I suspect the answer is poorly, as historic international examples could illustrate. We need cities and towns that are vibrant and innovative because without these qualities they will fail to attract the investment and the new citizens the country needs in order to prosper. We cannot afford a standardised approach to governing our communities and rigid central dictates cannot fit or know best in all circumstances.

While the minister's challenge addresses the question of whether or not councils should have a core of services defined by Parliament (other than those which are currently mandatory), it raises a more fundamental question. That question concerns the relative roles of central and local politicians. The minister's focus on core services is actually an attack on local representative democracy and the role and competence of local politicians. His charges that local politicians are responsible for silly and outlandish expenditure decisions are not justified and his solutions to this non-problem will erode their decision-making authority by a combination of greater centralisation and direct participation. Changes of

this magnitude, which have implications for the constitutional balance between local and central government and the way in which citizens traditionally perceive local government, require the involvement of the full community, as their implications for local government, and by extension local communities, are probably more important than the introduction of MMP was for Parliament.

The core service debate is a solution looking for a problem. Existing checks and balances appear to be working well and focusing elected members' attention on the big essential infrastructure items, to the effect that today councils are arguably more focused on the big items than they were in the past. That was what Parliament intended in 1996 with the Local Government Amendment (No.3) Act, and all the evidence suggests it was successful. The minister's attempts to identify and emphasise a set of core services seem not only unnecessary but, overall, counter-productive.

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1   In a later interview the minister informed the interviewer that libraries would be a core service as well, otherwise his mother would stop talking to him. Rumour has it that librarians from Waitakere City sent Mrs Hide flowers.
2   Coincidentally with the release of the TAFM paper the prime minister and government contributed to the purchase of Auckland harbour land to enable the council to develop 'party central' for visitors to that city – hardly a fit with the minister's more narrow list of core services.
3   For example, the former chief executive of Rodney District is advising the United States military on how to develop effective asset management plans utilising the methodologies based on those developed at his former council.
4   The Rotorua survey was undertaken by National Research Bureau (NRB) and is available from www.rdc.govt.nz; the Rodney survey was carried out by International Research

Consultants Ltd and is available from www.rodney.govt.nz; the Waikato survey was undertaken by NRB and is available from www.waidc.govt.nz; the Ashburton survey was carried out by NRB and is available from www.adc.govt.nz; the Southland survey was undertaken by Polson Higgs and is available from www.southlanddc.govt.nz; the Porirua survey was carried out by NRB and is available from www.pcc.govt.nz.

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Appendix: Mandatory functions: territorial local authorities

Roads:
• Council has statutory responsibilities under the Local Government Act and Land Transport Management Act to provide services for this activity.

Rubbish and recycling:
• Council has legal responsibilities, in relation to the activity, under the Health Act 1956 and the Local Government Act 1974 to improve, promote and protect public health through providing effective and efficient waste management.

Wastewater:
• Council has statutory responsibilities under the Health Act 1956 to improve, promote and protect public health within the district. This includes identifying the need for waste and stormwater services and either providing these directly, or overseeing the service if it is provided by others. The Local Government Act 2002 requires the ongoing waste and stormwater services by council, unless specific approval is sought to withdraw from this.

Water:
• Council has statutory responsibilities under the Health Act 1956 to improve, promote and protect public health within the district. The Local Government Act 2002 requires the ongoing operation of water supplies by council.

Community planning and consultation:
• Council has statutory responsibilities under the Local Government Act 2002 to produce a large number of plans, strategies, policies and statements.

District planning:
• Council has statutory obligations under the Resource Management Act 1991 (RMA) to provide the services for this activity. The RMA requires the sustainable management of natural and physical resources.

Animal control:
• Council has statutory responsibilities under the Dog Control Act 1996 and the Impounding Act 1955 to provide services for this activity.

Building control:
• Council has statutory responsibilities under the Building Act 2004 to provide the services for this activity. The Building Act provides for the regulation of building work, a licensing regime for building practitioners and the setting of performance standards for buildings.

Emergency services:
• Council has statutory responsibilities under the Civil Defence Act 2002, the Fire Services Act 1975 and various other acts and regulations to provide the services for this activity. Rural fire and civil defence are core activities required through various acts and regulations to ensure we can respond quickly and effectively to local emergencies.

Regulatory and environmental health:
• Council has statutory obligations under numerous statutes including the Health Act 1956, Resource Management Act 1991, Food Act 1981, the Sale of Liquor Act 1989, the Gambling Act 2003 and the Prostitution Act 2003 to provide services for this activity.

Gardens and green spaces:
• Council has statutory responsibilities to administer reserves under the Local Government Act 2002 and the Reserves Act 1977. Councils also have statutory responsibilities

to provide certain types of public spaces. Council must provide cemeteries for the district under the Burials and Cremation Act 1964 (and amendments).

Community buildings:
- Community housing and community buildings are discretionary activities; however, the Local Government Act 2002 defines community housing as a strategic asset.

Representation:
- Council has statutory obligations under the Local Electoral Act 2001, the Local Government Act 2002 and other statutes to provide the services for this activity (council and community boards).

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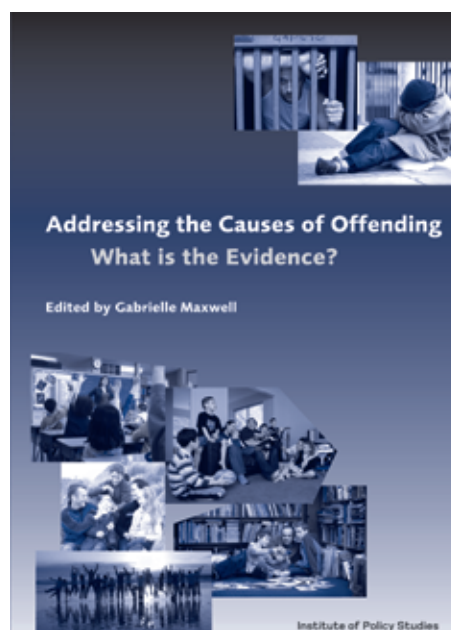
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Human-induced climate change over the coming century is likely to threaten not only physical ecosystems, but also the security of individuals, societies, and states. By precipitating natural disasters, and by affecting the livelihood of communities, climate change may exacerbate existing social tensions, create incentives for illegal actions, place unbearable strains on the capacities of states, and lead to resource disputes and struggles between and within states. This edited volume is the result of a symposium in Wellington in November 2008 that was convened to consider the factual bases for these claims, and to explore how New Zealand can and should respond.
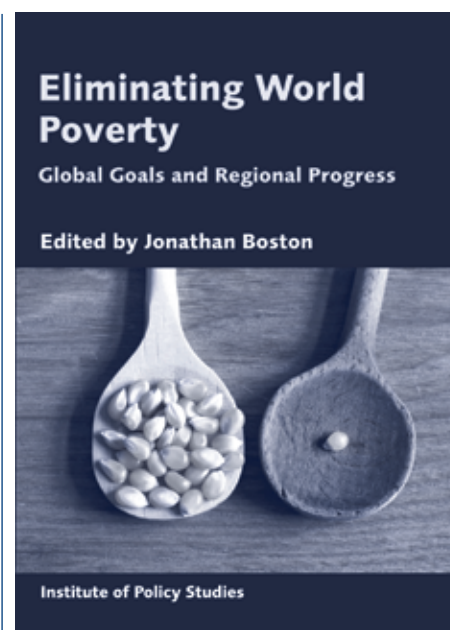
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Edited by Jonathan Boston
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Len Cook and Robert Hughes[1]

Driving Improved Value for Money
in the New Zealand Public Sector

Introduction

The new, National-led government is seeking a significant lift in productivity and economic growth. Raising the performance of the public sector is central to achieving such an objective. In our view, improving public sector performance is unlikely if we rely solely on the management tools and approaches introduced some 20 years ago. Nor will periodic budget cuts and reductions in 'back office' resources result in the level of improvement desired (Cook and Hughes, 2009). Rather, the focus should be on how the public sector can stimulate innovation and economic transformation through its critical role as the leader of several large, pervasive value chains,[2] such as health, education, science, justice and social services.

The public sector reforms of the 1980s were an important catalyst for the revitalisation of the national economy at that time, in retrospect perhaps more because of the opportunity they generated to rethink longstanding practices and structures, than because of the qualities of the new public management model that was the central focus of the changes. With government expenditure accounting for 45%

of GDP, and few options for managing the huge increases anticipated in health, retirement provision and justice, the need for revitalisation is just as strong today as it was 25 years ago.

The aim of this paper is to highlight the potential for sustained increases in innovation and transformation of systems in the public sector through effective leadership of the most critical value chains, in health, education, science, justice and social services. Sustainable quality improvement and transformation requires innovation supported by insightful, informed leadership and far-sighted engineering of complex systems and processes. Significantly and sustainably improving value for money from the public sector will require redesigning large, sector-wide service delivery value chains from end to end, and making strategic shifts in the resource base, systems and mandate of organisations.

Len Cook is the former National Statistician for the United Kingdom and prior to that was the Government Statistician for New Zealand. Since 2006 he has undertaken a number of reviews involving public administration in New Zealand, particularly in the health sector, as well as building on his interests internationally in official statistics.

Robert Hughes is a career management consultant with a particular speciality in the review and improvement of organisational systems. Before founding Hughes Consulting Limited in 1991 he was a partner in KPMG.

Approach

The area of interest in this paper is government-owned organisations that deliver public services. This includes ministries and departments, the non-public service departments such as the New Zealand Police and New Zealand Defence forces, and Crown entities including the district health boards (DHBs).[3] All public sector entities have a responsible minister, or, in a number of cases, multiple ministers.

At an institutional level oversight of these entities is provided by the 'central agencies', namely the Treasury, State Services Commission (SSC) and the Office of the Prime Minister and Cabinet (DPMC). The three central agencies work closely together, and initiatives to increase this cooperation have been expanded since the review of coordination among the central agencies in 2006. Outside of this arrangement, the Office of the Controller and Auditor General, as an officer of Parliament, plays an important role in addressing issues of accountability for value for money within the public sector.

Against this background, the question we have asked ourselves is why, with the institutional and governance structures in place, the high degree of short-term monitoring of public sector organisations by central agencies, and the analysis that takes place in the public policy agencies, are there such persistent difficulties in achieving high value-for-money public services? Our experience, from working in and with public sector entities, is that an important source of inefficiency is the inadequate attention given to leadership of the major public service value chains, and the oversight of that leadership. Poor leadership in service delivery value chains can dramatically reduce value for money, create resistance to systemic change that would bring productivity and quality improvements over time, and stifle the adoption of new opportunities for improvement in the quality and quantity of outputs.

In the complex sectors of health, justice, education and welfare, the value chains involve multiple organisations, yet we are not aware of any attempt to measure the degree of fragmentation in leadership in public service value chains, or the quality of leadership over them. For example, oversight and leadership of the network of parties which make up the public health value chain does not appear to be recognised within the governance roles and structure of the public health sector. We have only the proxy measure of New Zealand's poor record in increasing productivity (The Treasury, 2005).

Overall, it is New Zealand's place in the world that is vital to us, and in comparative terms we continue to slip (The Treasury, 2008). This most vital benchmark of our position in the world highlights the consequences of poor productivity, but gives little diagnostic indication.

Without insightful and effective leadership of the large value chains involved in the delivery of some public services, fragmentation in leadership can result in variable service quality and increased costs. To illustrate this, we have considered two inputs to the public health value chain;[4] one is an example of integrated leadership and the other of uncoordinated and devolved, fragmented leadership. The procurement of pharmaceuticals is provided as an example of a streamlined system with effective leadership across this part of the value chain, while the training of the medical workforce is used as the example of a highly fragmented approach, which has been subject to considerable attention at ministerial level since 2007 because of this, with strong value chain leadership finally being proposed only recently.

We believe that the findings of this analysis reflect issues with value chain leadership or its absence across the New Zealand public sector. Along with observations from other fields, these findings are also proposed as a basis from which to formulate a strategic approach to driving value-for-money improvements from public services.

Medical workforce training: a highly fragmented approach

The training of the medical workforce in New Zealand follows a widely adopted model in which graduates trained at recognised universities progress through prescribed training programmes to gain registration with the industry body, the Medical Council of New Zealand. Vocationally-trained medical specialists including general practitioners are employed as senior medical officers (SMOs) primarily in DHBs, the providers of hospital services, and in providing health services funded through the DHBs, for example in general practice. In addition to New Zealand-trained SMOs and general practitioners (GPs), an important source of SMOs is from overseas, and these people make up for the undersupply of medical graduates from New Zealand universities who remain in the New Zealand workforce. In 2008, 6,446 doctors and doctors in training were New Zealand medical school graduates and 4,106 were overseas medical school graduates (Medical Council of New Zealand, 2009).

… there is no role in the health system for strong leadership across the DHB network, yet the Medical Training Board (2009) reports huge shifts in the size and age mix of DHB populations which will place the viability of many services at risk if they continue to be operated separately on a DHB specific basis.

Centralising the evaluation and purchase of medicines has enabled the development of specialist competencies, which arguably could not be maintained by DHBs evaluating and purchasing medicines individually.

Of the total expenditure of $15.4 billion on health care in 2006, 78% was through the public health system, with the balance being private expenditure (District Health Boards New Zealand, 2009). The public expenditure is delivered through 21 DHBs. DHBs in turn fund GPs to deliver some services. There is a remarkable range in size between the smallest DHB and the largest. The smallest, in terms of the number of SMOs and doctors in training, is the West Coast DHB with 30, and the largest is Auckland DHB with 1,079 (Medical Council of New Zealand, 2009). Whilst there is a well-established process in place for training medical staff, under the current institutional arrangements there is a significant discrepancy in the ability of different DHBs to participate in that process.

For example, in most fields of medicine there is no clear strategy for national or regional service delivery, apart from some specifically designated national services, often based in Auckland or another of the largest DHBs.[5] Size matters in being able to develop and maintain a clinical speciality, making it very difficult, even impossible for some DHBs to maintain the critical mass of staff necessary to satisfactorily undertake clinical services. In particular, they struggle to sustain training positions at registrar level, with follow-on implications for the recruitment at SMO level. Even if more funding was available, the potential patient base for many medical conditions would be insufficient to prevent huge differences in the quality of care, when the relevance of experience of medical staff is taken into account. Apart from smaller DHBs in places where lifestyle benefits are well recognised (Nelson and Hawke's Bay), most stand-alone clinical services in small DHBs have a very high turnover of SMOs, with consequent effects on service availability, leadership capacity and innovation. While there are examples of adjacent DHBs establishing collaborative arrangements (Southland and Otago, the West Coast and Nelson, and the central region DHBs) there has been no capacity to systematically set out a strategy for regional service delivery in the long-term interest of providing relevant national public health service.

As previously noted, there is no role in the health system for strong leadership across the DHB network, yet the Medical Training Board (2009) reports huge shifts in the size and age mix of DHB populations which will place the viability of many services at risk if they continue to be operated separately on a DHB specific basis. A recent commission appointed by the director-general of health also highlighted this concern in its recommendations.[6]

Many critical decisions about the health workforce have been made without relevant information. It is only recently that in-depth information about doctors in training has been made available (by the Medical Training Board and District Health Boards New Zealand) in a form which might be used to develop informed approaches to more effectively managing the training of one of the country's most critical professional workforces. This is at a time when New Zealand will be doubling the number of medical graduates and without managed training there is a high risk of losing more of this highly mobile group.

Protecting the conditions under which doctors in training work has been a longstanding concern, and what goodwill existed in the past was severely undermined by poorly managed employment relations during the 1990s, characterised by the imposition of managerialism which undervalued clinical operational knowledge. As a consequence of this loss of goodwill, employment arrangements for doctors in training have become more highly formalised. The breakdown in trust has expanded the content of industrial agreements, and similar tends are occurring for senior doctors. There are two industrial organisations representing doctors in the DHB system, the New Zealand Resident Doctors Association and the Association of Salaried Medical Specialists.

A diversity of local management responses to a chronic national doctor shortage has led to the pay on temporary locum posts rising so much that a large number of doctors in training have opted for this and chosen to delay entry into vocational training. This has reduced the number of doctors in training in some areas below a critical mass to maintain the training in that speciality in a number of hospitals. SMOs have a similar degree of dissatisfaction, although the cause differs.

Over a lengthy period of significant budget surpluses, it has been politically less costly to maintain the status quo than to change how the medical training system operates. We now have a clear strategy to shift from a highly fragmented approach to the training of future SMOs. While the sector has, in areas, demonstrated a huge capacity to change, it is only recently that a decision has been taken to address the obvious problems with the medical training system.

Pharmaceutical Management Agency: a streamlined approach
In contrast to the fragmented approach to training doctors, the acquisition of drugs is a streamlined process, managed across the health sector value chain. The essential step in streamlining this process was the creation of the Pharmaceutical Management Agency, Pharmac. It was set up in 1993 as a joint venture company owned by the four regional health authorities for drug purchasing. Pharmac is now a Crown entity responsible to the minister of health, and has the twin tasks of making arrangements for access

to medicines and promoting the optimal use of medicines. It does this by managing the pharmaceutical budgets for the DHBs and evaluating which medicines should be funded by government. As the centralised pharmaceutical agency, Pharmac also assists DHBs to assess the cost effectiveness of new medicines. In 2009 the total expenditure on prescription drugs was $635 million. Medicines are manufactured by private sector companies and a detailed understanding of the market for the supply of drugs is vital to being able to operate effectively as a purchasing agent.

Centralising the evaluation and purchase of medicines has enabled the development of specialist competencies, which arguably could not be maintained by DHBs evaluating and purchasing medicines individually. Coordinating the purchase of all medicines across the DHB network has also enabled the health sector to take advantage of its size, using the combined purchasing power of the DHBs to reduce costs. Importantly, the streamlining of pharmaceutical purchasing has enabled Pharmac to take an active role in educating consumers in the use of some medicines, especially antibiotics. Pharmac is active at three points in the value chain: evaluation, purchasing and education about the use of medicines.

What does this tell us about institutional structure and value for money?

The processes for training medical staff and purchasing medicines are both complex, but markedly different approaches have been taken, with one fragmented and devolved and the other integrated, with centralised leadership. These two examples illustrate two different approaches to acquiring inputs; clearly there are a range of other approaches that could be taken to managing other aspects of the health sector value chain. What these examples highlight are the advantages of taking an integrated approach, not just to realising value for money but to facilitating stakeholder engagement, including, if relevant, public education and debate. This will not be possible without leadership and oversight across the major components of public sector value chains.

In summary, our analysis highlights that:

1 *There are complex service delivery value chains associated with many public services.* Fragmentation in complex value chains has negative performance ramifications for all involved in the delivery of public services. Fragmentation can result in a significant reduction in value to consumers and it is disempowering for those working in the sector because it is too difficult to make changes to the system. From the perspective of the entire value chain, fragmentation results

in: (1) diminished opportunities to build a critical mass of expertise, bringing not only inertia but also building barriers to innovation and service delivery improvement; (2) forgone opportunities of economies of size and other means of gaining economic advantage; and (3) a larger burden of bureaucratic oversight obligations that come as expensive substitutes for standards and systems. Achieving sustained value for money from these public services will require leadership focused across an entire value chain (including the various inputs, transformation systems and outputs).

2 *These service delivery value chains are strongly dynamic, and imposing rigidities on them through fragmentation in value chain leadership has a significant impact on innovation, adaptability and dynamic efficiency.* There is a narrow and rigid approach to role and structure which is presented as a choice on a rigid continuum which ranges from government department to Crown agency through to SOE. Associated with this is an over-simplification of the market/public sector boundary which is seen as a preparedness for privatisation, this being indicated by where an entity is placed on this continuum. More signs of the excessive focus on institutional structures comes from the creation of artificial markets and fragmentation of value chains, sometimes as a consequence of the so-called funder/provider split, when one agency allocates the resources applied by other government entities at various stages of the value chain. A consequence of this excessive focus on institutional structures and of assigning the allocation of resources to agencies that do not have a deep understanding and leadership role across the value chains they fund is that the public sector has become detached from the reality of what is required to make New Zealand's public sector globally competitive. This detachment is manifested through excessive reliance on departmental outputs as a central indicator of performance, without regard for markets or systems, nor even the appropriateness of the end services delivered by public sector value chains. The creation of fictional markets to support atomised contestability, and relationships focused on financial contracts and compliance obligations, has reduced the ability of entities to respond to changing circumstances.

3 *Current institutional structures, legal authorities and budget delegations do not facilitate, and in some cases prohibit, the effective value chain leadership necessary to bring about sustained improvements in value for money in the provision of public services.* Value chain leadership requires clear acknowledgement

Value chain leadership requires clear acknowledgement that one authority has the mandate to gather information and engage in establishing a systems-wide view of the sector that they are part of.

There is no independent commentator on the value for money from public services.

that one authority has the mandate to gather information and engage in establishing a systems-wide view of the sector that they are part of. How this mandate is allocated and overseen may well need to be unique to the sector, as will the partners engaged in this work. Given the depth of concern about public sector performance, in the context of policy failings about productivity in the wider economy, delays in obtaining such a mandate should not prevent leadership initiatives within the public sector itself. We would also comment that, in our view, the policy/operations split has contributed to the current state of affairs. With the policy/operations split there has been a massive loss of information and increase in ignorance about the nature, direction and ongoing operation of our major public sector value chains.

4   *To lift service quality and improve value for money, it is certain that in any complex sector there will be some key standards or systems and it will be essential to have the mechanisms to oblige all institutions within a particular public sector system to adopt them.* The breadth and scale of internal production by formerly large government departments was extensive, but value chain leadership (or managing co-production) was simply not recognised before or after 1988 as an activity vital to dynamic and allocative efficiency that would add value, drive productivity gains and stimulate innovation. Even worse was the failure to identify anywhere the increased significance of effective value chain leadership in capitalising on the rise of global and national services and infrastructure. In New Zealand, 97% of GPs have electronic patient records and the capability to electronically deliver diagnostic information (compared to 25% of GPs in the USA), and yet the public health system has failed to put in place a common New Zealand-wide patient management system, or even common capacity for readily obtaining and exchanging diagnostic information, such as x-rays, across all centres. Concepts of core competencies and critical mass have slipped by unnoticed by the central agencies in New Zealand. The functional organisational form and contractual focus of the New Zealand reforms of the 1980s provided no vehicle, informal or otherwise, for ensuring common approaches to matters where an integrated approach across government entities could offer economies of scope or scale or efficiency gains.

There are also spill-over effects on other sectors. For example, those working outside the public sector are often required to emulate the bureaucratic processes of the public sector. The voluntary sector,[7] for example, has experienced two decades of working with higher compliance costs brought about by extensively detailed but poorly evaluated contracts.

The result has been that the sector itself has increasingly loaded more administrative demands onto its front-line workers by centralising minor decision making and imposing additional compliance obligations. This has reduced for some the spontaneity and community service elements of voluntary work.

An inflexible attitude on the part of public sector entities which advances their own, and not sector-wide, objectives also engenders a high degree of caution amongst potential collaborators on the public/private/voluntary sector boundary. The uncertainty that this type of caution engenders makes it difficult for the private and voluntary sectors to justify investment to build new capacity (both human and physical). This reduces participation by the private and voluntary sectors and shifts the burden for new investment onto the public sector. The impact of this over time is for the public sector to reduce the strength of other potential collaborators in the delivery of public services.

The current structure of the New Zealand public sector does not provide authority to any entity or body to make governance decisions at a sector level, and, importantly, to lead implementation of those decisions, despite it being at this cross-sector level that leadership is most necessary if we are to make serious gains in lifting value for money and service quality.

At the political management level, the ministerial portfolio mix in New Zealand is almost always scattered, poorly linked and unable to provide a concerted focus on the delivery of outcomes. The capacity that ministers have to reach agreement becomes absolutely critical when there is no serious consideration given to how decisions within related ministerial portfolios should be aligned. This system is highly dependent on ministerial competence and predilections. Ministers have increasingly become active project sponsors, without the consequent expense of accepting the breadth of governance relevant to the significance of their decisions. All of this narrows the interest and capacity to focus on sector-wide issues, where success is likely to enhance the performance of your successor and being accountable for large-scale developments with high-risk profiles brings career risks, especially if the trust needed in public sector leaders is still developing. Compounding this is the political dimension to value-perception by ministers, which is driven by considerations of their own understanding of and position on issues, and political advantage.

The Fiscal Responsibility Act 1994 introduced disciplined procedures for the governance of government appropriations, set out in the annual government budget. No equivalent exists for the specification and monitoring of government outcomes. This absence of a nationally-agreed outcome strategy has had a number of ramifications:

Ministers as purchase agents do not necessarily recognise the less tangible accountability of each chief executive to be prepared for future governments or emerging problems.

There is a growing tendency for senior leaders in the public sector to be working in isolated and autonomous roles, and sometimes possibly advocating that they be given responsibility for sector leadership.

There is no independent commentator on the value for money from public services. The Treasury and SSC may have the mandate but, as part of the public sector, they are not independent parties. The Office of the Controller and Auditor General will investigate specific instances where authorities and procedures have not been adhered to.

To begin to redress this will require highly-informed central agencies, more effective understanding of systems and value chains by policy agencies, and much richer and more challenging interrelationships among all parties involved. The strong collaboration we now see among the central agencies may perversely strengthen tacit acceptance of the continued relevance of the approach adopted to public sector reform in the 1980s. Indeed, intense central agency collaboration and interdependence may well diminish contestability and challenge within these bodies.

A new set of rules

The managing-for-outcomes framework could have been a valuable achievement. However, current governance structures focus on chief executive accountability for the delivery of individual agency outputs in the absence of an accountability framework for sector-level outcomes and value chain leadership.

To address these shortcomings we have identified in this article will require:

1 Broadening governance structures and practices to encompass sector-wide solutions to outcomes. This requires both rethinking the performance management framework to give weight to value chain efficiency, and an entirely different and demanding approach to assessing outcomes.

2 Simplifying the major public sector service delivery value chains, centralising functions where appropriate, and continually striving to improve value for money in the delivery of outcomes. This requires identifying the key public service value chains and putting in place the means for their active leadership and oversight.

3 Changing public sector culture and incentives to work in alliances with other organisations in the private and voluntary sectors. This requires the active management of boundaries, which may see more work outsourced.

More effective sector-wide leadership could result from

refocusing roles in the public sector institutional structure, without major structural change. This could be achieved by, first, establishing accountability for the delivery of a national agenda of outcomes – this is one of the two new roles we are proposing. We envisage that there could be between five and ten national outcomes established by government, covering the whole of the public sector, each with a set of supporting goals and performance indicators. Each national outcome would have an outcome leader with responsibility for working with key players to define the most appropriate service delivery value chain, set of players and role for each player.

These value chains would consist of a mix of public sector entities and private and voluntary sector entities. Operational responsibility for how the players work together would remain with the public sector delivery entity (for example, the DHBs and Pharmac).

The outcome leader would not be the chief executive of one of the delivery entities but would be a specially appointed role. Administratively, outcome leaders could be located within DPMC, but would take their mandate from the responsible minister.

Coordination of outcomes and management of the contribution made by public sector entities would be provided by a national outcome forum. This forum would consist of the national outcome leaders and the heads of the SSC and Treasury.

The state services commissioner would chair the forum as head of the public service, an extension to the current role. An extension to the commissioner's role would be necessary to provide the mandate for a focus on performance at sector and not just individual chief executive and agency level, and to coordinate activities across public sector entities.

In assessing outcome performance, the responsible minister(s) would consider the contribution made by all players in the value chains. The strategy for the achievement of outcomes and the role of the participants in the sector value chain would be set out in an outcome transformation plan. The outcome leader would be tasked with facilitating the process of developing the outcome plan in collaboration with key players in the value chain and in consultation with stakeholders, including New Zealanders and service users.

To contribute effectively to the forum, the Treasury would need to broaden its capability to assess the value for money from value chains involved in the delivery of outcomes. The Treasury would need an understanding not only of outcome and output performance but also of the transformation systems and inputs for the major public sector value chains in health, education, science, justice and social services.

Whilst there is a well-established process in place for training medical staff, under the current institutional arrangements there is a significant discrepancy in the ability of different DHBs to participate in that process.

Collaborative network arrangements seek to capitalise on the limited capabilities available in New Zealand and in so doing gain economies, and allocate risk and capital to the parties best able to manage them.

We propose an additional new role be established, that of an independent national productivity commission. The purpose of this body would be to examine and make recommendations on the efficiency and effectiveness of the major public service delivery value chains.[8] It would report to a responsible minister with whom its work plan would be agreed. The reports of the commission would be published.

Under this model there would be no change to the role of the controller and auditor general.

Discussion

This post-bureaucratic organisational form recognises the unique features of public sector entities as well as utilising private and voluntary organisations to deliver government outcomes. An important way in which this new form of organisation differs from that currently found in the New Zealand public service is the active management of the dynamic boundaries between the roles played by all participants in public service delivery. These boundaries are managed and facilitated by the public sector.

Improved analytical capabilities and information will be needed in order to realise benefits from transformation in the major service delivery value chains. The information needed is not only related to organisational performance but also covers activities which constitute the service delivery value chain and its participants, the nature of input and output markets, and insights into how these markets might evolve. External evaluations with a sector-wide focus can play a vital role in challenging the status quo and counterbalancing short-term agency-level output measures which are used to assess public sector performance.

Changes of the type we describe would also put an end in many cases to the split between policy and operations, see consolidated processes in some cases, require improved governance arrangements and spell an end to the artificial competition that has been part of the justification for the fragmentation of sectors, most noticeably the public health sector. The funder/provider splits also need to be revisited.

Interestingly, the use of purchase advisors by the current National-led government could be seen as the embryonic development of the formal role of outcome leaders we are proposing.

There are also numerous examples from New Zealand of the use of commissions and boards to provide advice on specific matters: for example, electricity, telecommunications, retirement, film and medical training. Over the period 1977 to 1991 an advisory body, the New Zealand Planning Council, operated with a cross-sector mandate to advise government on economic, social and cultural planning. In July 2009 a productivity taskforce was appointed to identify how New Zealand can close the income gap with Australia by 2025. Other taskforces have also been appointed to look at improving productivity in specific sectors, such as the Building and Construction Sector Productivity Taskforce established in 2008.

Summary and conclusion

The public sector has long been recognised as operating in a network with other organisations, including those in the private and voluntary sectors. The public sector reforms of the 1980s clarified the outputs that were to be delivered by public sector institutions, and privatised many government-owned and -managed activities. In this article we have put forward the proposition that the poor performance of the public sector is a result of widespread and systemic fragmentation in leadership of key value chains which support the provision of public services in complex sectors of government. We argue that streamlining sector-wide value chains will address recognised deficiencies in the current arrangements and drive improvements in value for money in the delivery of public services. We also argue that operating within collaborative network structures is more appropriate for a small, open economy, like New Zealand's.

Making greater use of networks and collaborative arrangements would require no fundamental changes in the legislative framework within which the public sector operates. Simple institutional structures need to be put in place to provide the governance to drive the adoption of practices for continuous improvement and value-for-money gains. We have advocated that this could be achieved through the creation of two new bodies and honing the roles of the SSC and Treasury. The new bodies are the national outcome forum to provide leadership in lifting value for money from public services, and an independent national productivity commission for monitoring the actual gains achieved.

Collaborative network arrangements seek to capitalise on the limited capabilities available in New Zealand and in so doing gain economies, and allocate risk and capital to the parties best able to manage them. An example of the economic gains that can be realised from taking an integrated approach to managing across a major public sector value chain was provided by the centralised drug-buying activities of Pharmac. In a country of four million people facing severe economic conditions, there are few justifications for the public sector not pushing hard to gain the full benefits from better exploitation of the limited capabilities available.

Despite what seem to us clear benefits from operating within a more systematic network structure, we would

caution that unless these structures are part of a redesign of the entire service delivery value chain with appropriate governance structures, the high costs of coordination and monitoring may make networks unworkable.

Addressing issues of governance, critical mass, leverage of assets and core nationwide systems, and an informed collective view of the future context, are seen as central elements of public sector leadership which will be critical to improving the value for money realised from public services in New Zealand. Addressing these issues will provide important tests of all policies and programmes, including decisions by ministers and central agencies. Unless these issues are addressed then the plethora of old and new approaches we will undoubtedly see brought to bear on the public sector will have little more effect than as rallying calls for change.

Most critically, the central agencies who are accountable for the public sector management system need to show how we are moving from the solutions of the past, given that our economic position has so painfully continued to

decline under their stewardship. This matters because the performance of the public sector is inextricably tied to New Zealand's future.

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Andrew Butcher

Friends, Foreign and Domestic:
(Re)converging New Zealand's Export Education and Foreign Policies

Introduction

While there has been long-standing engagement between New Zealanders and Asia in a variety of ways (Didham, in press), the primary policy engagement has been first through defence and security, and then through foreign affairs.[1] In foreign policy, Asian countries have had official diplomatic representation in New Zealand since the beginning of the 20th century (Friesen, 2009), while New Zealand has been represented diplomatically in Asian countries since the 1950s (Kember, 2009). The convergence of what amounted to (though was never called) 'export education' policy in the 1950s with foreign policy of the same period primarily centered on the Colombo Plan, which, as detailed further in this paper, was essentially the education of (South and Southeast) Asia's élite in Western countries, including New Zealand. But a number of shifts, ideological, strategic and pragmatic, saw these two policies diverge to the extent that by the 21st century they held less common ground. Export education policy developed in its own right, into its own industry with its own institutions (see Lewis, 2005), and ultimately under its own minister. Foreign policy also changed, though in priority rather than substance, reflecting

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the changes of the governments of the day and, more often, within and between New Zealand's allies and neighbours. This article argues, however, that there should be a re-convergence of these two policy areas, largely because the importance of Asia to New Zealand is even greater now, in 2009, than it was in 1950.

Why Asia?

The focus of this article is Asia. It could be argued that one should include the Middle East and South America in an analysis of New Zealand's foreign and export education policies. But there are strong reasons to focus exclusively on Asia. These reasons include:

- As noted below, the vast majority of international students who are in New Zealand are from Asia.
- New Zealand's population in 2006 was 10% Asian and is projected to be 16% Asian by 2026 (Bedford and Ho, 2008), putting New Zealand's Asian population in proportionate terms alongside that of Canada and above Australia's (Spoonley and Meares, 2009).
- Most of New Zealand's foreign policy priority countries are in Asia (McCully et al., 2007; Ministry of Foreign Affairs and Trade (MFAT), 2008).
- Two of the three largest economies in the world are in Asia (Japan and China), and China is set to become the second largest economy in the world after the United States (and already outranks Japan in PPP rankings). According to Xie Hongguang, deputy director of the National Bureau of Statistics of China, 'China will overtake Japan as the world's second largest economy within three years' (China News Agency, 2009).
- Asia is home to ten of New Zealand's 20 top markets for goods exports and is becoming increasingly important for tourism and education (MFAT, 2007).
- What happens with the regional security of the Asian region will affect New Zealand far more significantly than what happens with the regional security of the Middle East or South America. Alongside the loss of US soft power in the Asian region (largely as a result of the Bush presidency and US interventions in the Middle East (Singh, 2004; East West Center, 2007; cf. Nye, 2009), there are concomitant changes in Asia regional security architecture. The strategic regional and political shifts in Asia will invariably affect New Zealand because of both its geographical and its economic proximity to the region (cf. White, 2009).

New Zealand foreign policy

The other focus of this article is New Zealand's foreign policy. This article is not primarily about New Zealand's export education policy, about which there is already a large body of literature. It is recognised that education exports are driven by many factors besides foreign policy objectives, including revenue generation, the desire to recruit migrants, tourism, the labour market, and developing trade and investment links. The vast literature on New Zealand's export education policies cover many of these other factors adequately (e.g. Deloittes, 2007; Infometrics et al., 2008; Merwood, 2007; Ho et al., 2002; Abbott et al., 2006), but what is often neglected in this literature is the importance of foreign policy in New Zealand's export education industry (with some notable exceptions: Bennett, 1998; Tarling, 2004). Even within New Zealand foreign policy-oriented/international relations literature, international students do not feature prominently, with the exception of references to the Colombo Plan (e.g. McKinnon, 1993) (and do not feature at all, for example, in the New Zealand International Review from 1989 to 2009).

Recognising the importance of Asian students in New Zealand (and as alumni in Asia) to New Zealand's foreign policy has been noted by others. For example, the Seriously Asia Conference, held in 2003 (and subsequent similar conferences held in 2005 and 2007), noted the importance of Asian students to New Zealand's relationship with the Asian region (Asia 2000 Foundation, 2004; Asia New Zealand Foundation, 2005; Asia New Zealand Foundation, 2006). But, as New Zealand Herald journalist Fran O'Sullivan pointed out with reference to the 2007 business-oriented conference,

> [I]t's going to take a lot more than exposing Kiwis to inspirational speakers for this country's business people and Government to get around to tackling the Asian challenge. A list of objectives developed by two foundation working parties read like lists from yesteryear. Don't blame them. Blame those that failed to put timeframes and scorecards around the previous objectives to ensure they were achieved by Government Ministers, agencies, business organisations and others ... Which is a pity because the Asian economic game will not stand still while we gear up to walk. (O'Sullivan, 2007)

There is a sense that with this repeated refrain of the importance of Asian students to New Zealand's relationship with Asia we have not progressed too far down the path, but perhaps instead have started going round in circles.

Asian students in New Zealand

International students from Asia first came to New Zealand in 1951, under the auspices of the Colombo Plan of 1950. The plan played a strategic role in New Zealand's foreign policy. While the benevolence of the Colombo Plan was more ideologically motivated than substance-driven, there were nevertheless important developmental projects which took place under its auspices; education given to students under the plan was of benefit both to them and to New Zealand long-term (MFAT, 2001). The Colombo Plan introduced Southeast Asians to New Zealand and in that respect played

a significant contribution. It 'laid the foundation for some enduring relationships between New Zealand and the region' (MFAT, 2007, p.28) and even now 'Asian students returning to their home countries with positive firsthand experiences of New Zealand play an important role in promoting New Zealand, as well as forming a valuable pool of potential employees for New Zealand companies' (ibid., p.48). Notably, however, New Zealand has not been as successful as Australia in maintaining and cultivating this educational link. Still, government Cabinets in Southeast Asia (for example, Singapore) boast more Australian university graduates than New Zealand graduates, and while there are exceptions (for example in East Timor: Hoadley, 2005), New Zealand has not actively sought to identify, educate and cultivate relationships with the rising élite in Asia.

In contrast to the six students who arrived in New Zealand in 1951 under the Colombo Plan to study dentistry at the University of Otago (MFAT, 2001; Tarling, 2004), in 2008 there were 21,136 international students at universities in New Zealand from Asia and other continents. Alongside these university students, in 2008 there were 15,207 international students in schools, 16,121 in vocational training and 35,853 doing English language studies (Education New Zealand, 2008a).

Students from the People's Republic of China dominated amongst international students in the early part of the 21st century, though had dropped significantly in number by 2003/04 and have never recovered to the same level, with a continuing and significant drop from 2003 to 2008. In contrast, Indian students have increased significantly in the same period, in particular from 2006/07. Traditional source countries of students, such as Malaysia (from the 1950s) and South Korea (from the 1990s), have both registered a slight decline in numbers over time, though in Malaysia's case this has recently been reversed, with a small increase from 2003. Malaysian-Chinese students were amongst the first private fee-paying students in New Zealand, though their fees were subsidised and the number of students was subject to a quota (Tarling, 2004). New source countries, such as Viet Nam, have also emerged. These trends are graphically illustrated in Figure 1 and, specific to provider groups, in Figure 2.

Export education has also grown to become one of New Zealand's most significant export industries, as shown in Figure 3. According to a 2008 report on the impact of international students on New Zealand's economy (Infometrics et al., 2008, p.1), in 1999 the contribution of export education to New Zealand's gross domestic product (GDP) was estimated at $545 million. By 2001 this had more than doubled to $1.3 billion, while in 2004 the estimated contribution had passed $2 billion, with the industry's value-added estimated at approximately $2.2 billion. Despite a downward trend of foreign fee-paying students since 2003, in 2007/08 the export education industry generated around $2.3 billion of foreign exchange, of which $70 million came from off-shore provision.

Figure 1: Enrolments of Asian International students in New Zealand, by country
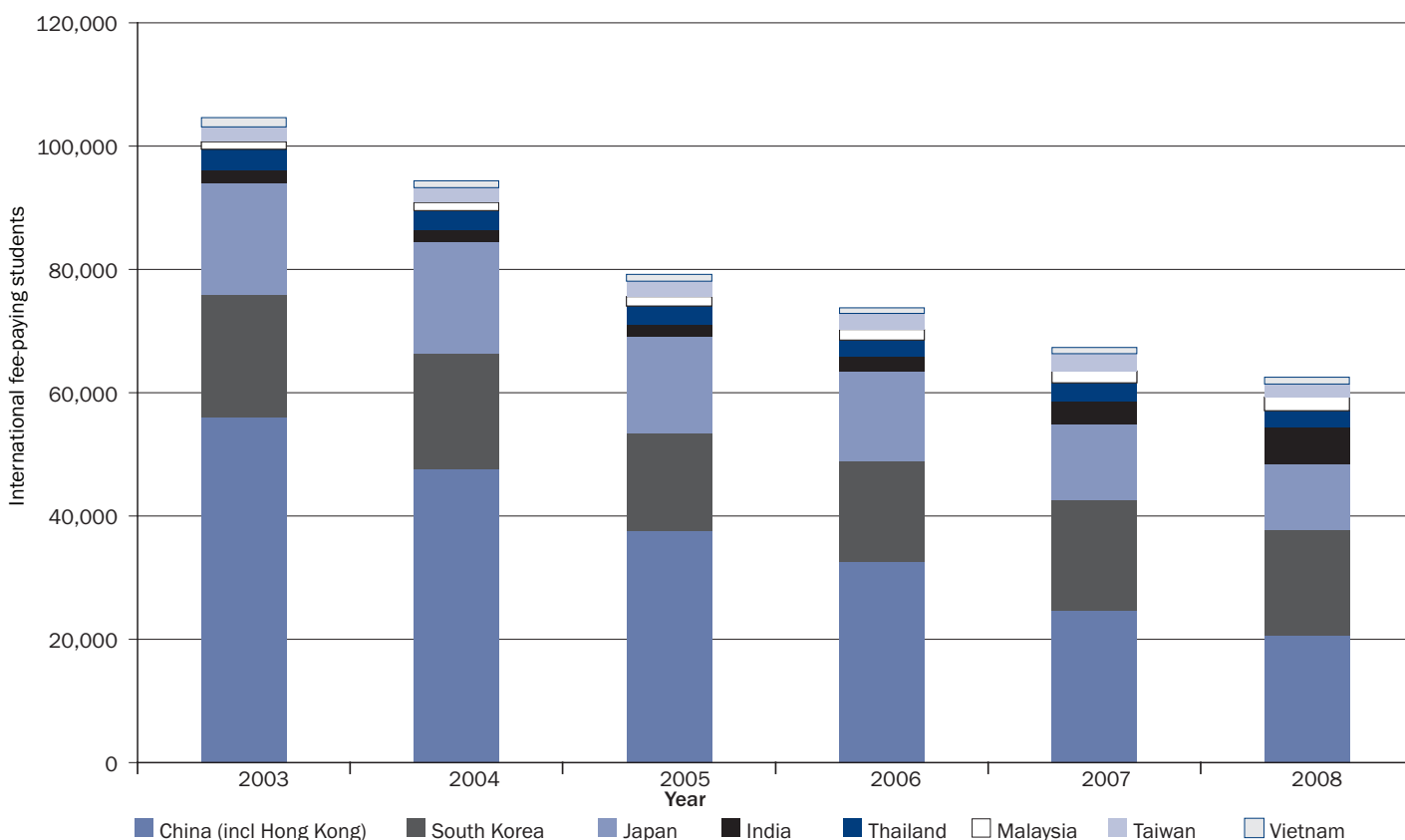
After the Colombo Plan

This significant economic contribution of (and reliance upon) export education to New Zealand starkly demonstrates the shift from 'aid' under the Colombo Plan to 'trade'. Tarling (2004) clearly identifies that the shift from one to the other occurred in principle well before it occurred in legislation in 1989. One significant contribution to the debate leading towards earning foreign exchange through export education was the so-called Hugo Report. Its project leader, Sir Frank Holmes, noted that:

> the conclusion of the report set out the principles of a positive strategy and set of policies that would enable New Zealand educators to earn increasing income from the sale of services overseas, with advantage to their institutions and their domestic students, and to the benefit of the economy and the overall education system.[2]

However, of this report and its authors, Tarling (2004, p.150) is less than complimentary:

> If this was an attempt to escape the control of officialdom, it did not guarantee independent advice … Certainly the Hugo Report offered what [Minister] Moore wanted to

hear and what he hoped to persuade his colleagues to adopt. Its report offered an overall policy, though not an entirely coherent or well-researched one.

Comments by Holmes (in his capacity as the first chair of the then-new industry body Consult New Zealand Education) lend weight to Tarling's claim. Holmes noted that '[o]ur market research confirms the Ministers' view that, with enterprise and professional marketing, institutions should be able to earn significant income from overseas students' (emphasis aded).[3] Tarling (2004, p.177) goes on:

> Hugo was the victor: the rhetoric of the report, rather than its research, carried the day. That success – sweeping earlier reservations aside – derived, however, in part from its association with other education reforms for which it had argued and which were put through by the re-elected [Labour] government.

Indeed, the government's willingness to largely accept the Hugo Report's recommendations without taking notice of the critics (Holmes notes that Moore was 'surprised by the resistance he encountered' and that 'there was a good deal of vocal opposition')[4] supports the contention that the

Figure 2: Enrolments of international students in New Zealand by provider groups
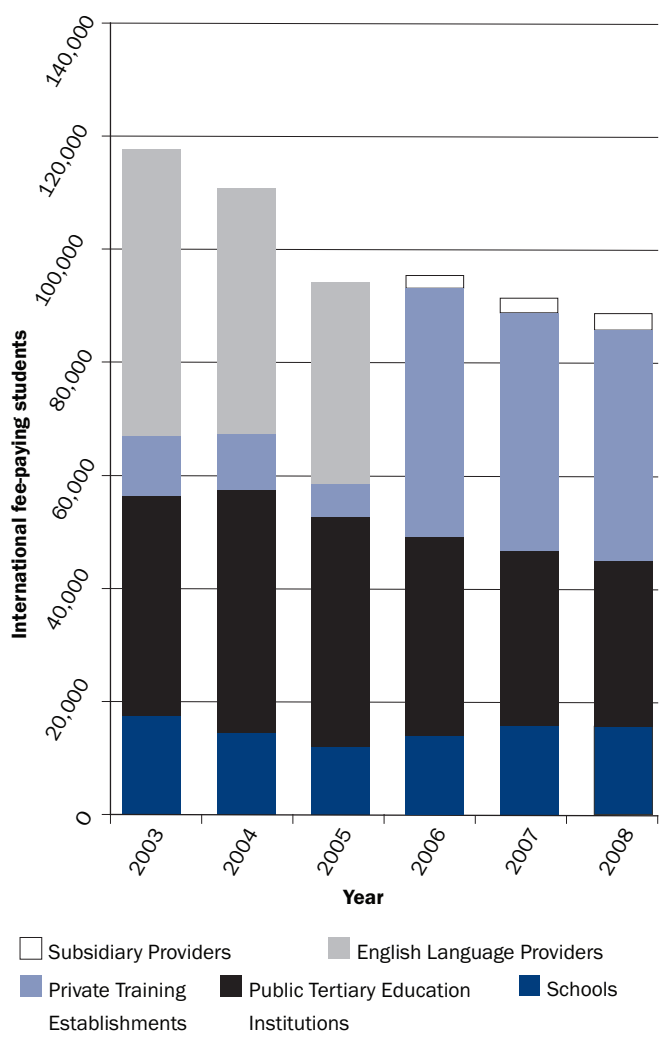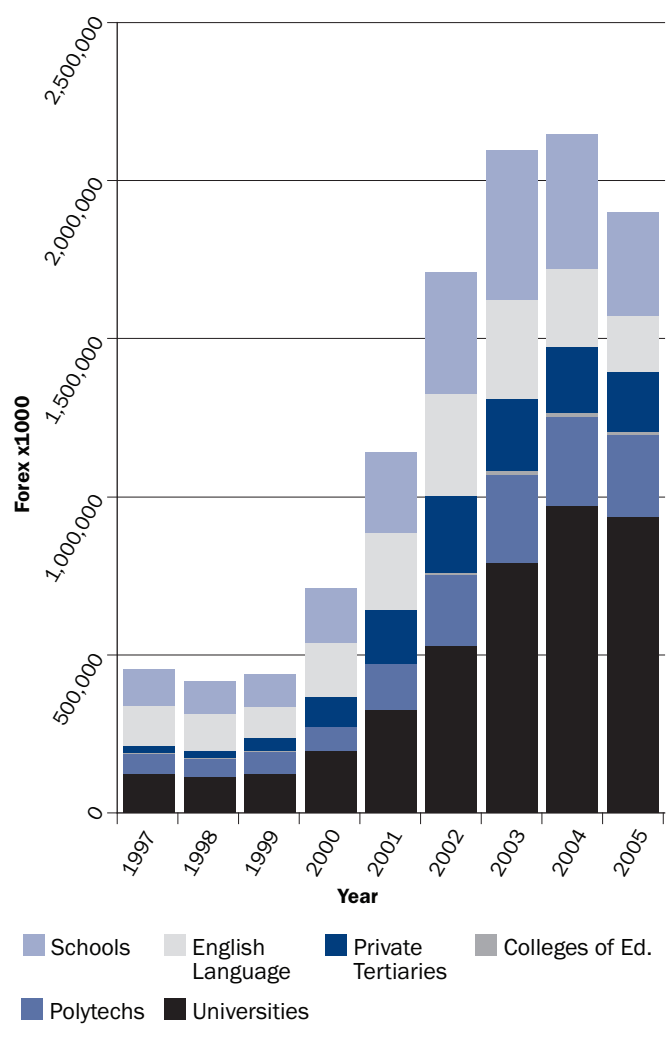

Figure 3: Economic benefits of export education to New Zealand

shift to exporting educational services had begun well before Holmes and others put their report to the minister. (Tarling locates the shift as early as 1980-81, placing the substantive shift in 1984 (Tarling, 2004, pp.100, 130ff).)

This shift away from 'aid' and towards 'trade' was perhaps inevitable, but it is the contention of this article that the shift went too far. It's not that we should return to the days of education-as-aid, but rather we should include New Zealand's long-term foreign-policy objectives in the development of our export education industry. This is discussed in further detail below.

Discussion

The experience of Australia's government in 2009 in responding to difficulties and bad press regarding its Indian student population is salient. The Australian government, as a knee-jerk reaction, has instigated inquiries and is rewriting legislation (Senate Standing Committee on Education, Employment and Workplace Relations, 2009a, 2009b), while others (Wesley, 2009) are putting forward policy prescriptions to address the issue of Australia's 'poisoned alumni'. However, it is not a matter of returning to the heady days of the Colombo Plan, for the regional landscape has changed beyond recognition in the almost 60 intervening years, and the nostalgia felt by graduates of the Colombo Plan and its era may not be felt by contemporary international students. Nor is it a matter of somehow turning back the clock, to the days before the revenue from international students was such a boon to educational institutions. The global financial crisis makes a mockery of any attempt to disconnect export education from revenue generation, especially as export education is, counter-intuitively, performing well during this recession (Education New Zealand, 2008b). Nor is it enough to blame the current ills on the increased marketisation and fragmentation of higher education (cf. Wesley, 2009), though this may well have played its part. These are easy scapegoats, but heaping the responsibility on policy decisions that were made 20 years ago (in New Zealand's case) does not advance the debate, it merely re-litigates it.

The motivation for Australian and New Zealand foreign policy to re-engage actively with export education policy is not just a need to respond to reputational difficulties abroad or economic constraints and imperatives at home, but also that these two countries' futures will be profoundly affected by what happens in the Asian region. As an Australian columnist notes:

> Many of the students of the Colombo Plan returned to become doctors, lawyers and politicians, power elites in the world's most vibrant economies. Australians talk a lot about engagement with the region and this was a form of regional interaction with enormous potential to shape our relationship with the nations to our north. It was replaced by an industry focused on quantity rather than quality, a little like our wine exports. It is an industry, moreover, on which our higher education sector is frighteningly

dependent … The overseas student program needs to be reinvented around an appreciation of these kinds of relationships and an equally keen appreciation of what kind of future we may face in their absence. (Slattery, 2009)

Bringing export education into the wider ambit of foreign affairs will achieve a number of strategic and salient objectives.

First, it will support the new government's ambitions towards a 'New Zealand Inc.' approach off-shore. While the offices of New Zealand's agencies with an off-shore presence are often co-located, the multiple reporting lines, levels of bureaucracy and various agendas present a fragmented New Zealand approach to particular countries and policy areas. The National-led government, formed in late 2008, has made clear overtures towards supporting a 'New Zealand Inc.' approach in its operations abroad, though achieving that in practice will be much more difficult. Indeed, the NZ Inc. approach will only succeed in so far as institutions themselves also take responsibility for ensuring quality in the education and pastoral care provided to international students.

Second, it will serve as a useful contribution to the exercise by the Ministry of Foreign Affairs and Trade in assessing New Zealand's off-shore 'footprint'. This 'footprint' exercise, taken every few years, will assess New Zealand's official presence abroad. It would be worthwhile, however, extending the exercise to include New Zealand's diaspora populations (see Didham, in press), many of whom will include Asia-born New Zealand graduates (see McGrath et al., in press).

Third, it will signal a move away from a fragmented approach adopted by New Zealand universities towards their alumni, where each university vigorously protects its own alumni data and holds independent alumni events throughout Asia, even within weeks of one another. It may be argued that independent institutions cannot be compelled to share their alumni data, and certainly attempts by New Zealand's Ministry of Education to encourage them to do so are frequently blocked by universities. But the lack of rigorous, robust and accurate data on New Zealand's alumni in Asia and elsewhere restricts New Zealand's capability to research, engage with and cultivate its alumni in countries and regions where it has clear foreign policy interests (cf. Fullilove and Flutter, 2004).

Fourth, and most importantly, the greatest benefit to New Zealand's foreign policy in the long term will be to establish these 'friends, foreign and domestic' in a region that is increasingly important economically and strategically for New Zealand's future. The importance of networks in the Asian region cannot be underestimated. New Zealand-trained Asian-born graduates are better placed to advance New Zealand's trade and foreign policy interests in the Asian region than New Zealand bureaucrats who may have no Asia awareness whatsoever. The economic benefits to New Zealand of export education are important to our economic growth. But equally important to that growth is deliberately

'cultivating' Asian students in New Zealand who will go on to become Asia's leaders. In that respect, the Colombo Plan was a resounding success.

Fifth, the corollary to re-converging foreign and export education policies is to amend domestic policy settings. While it is important, clearly, to encourage educational exchange between New Zealand and Asia, domestically we need to make it easier for international students to reside and work in New Zealand. Immigration and labour market settings should be loosened and incentives given so that Asian students in New Zealand can contribute to New Zealand's economic growth and international linkages once they graduate (McGrath et al., in press).

Sixth, while the Colombo Plan began with a security focus and used education as a tool against the spread of communism in and for countries that were poor and developing, these same countries are now developed and wealthy. Whereas it was once a necessity for students from most parts of Asia to study abroad, now it is a choice. So, while export education needs to be a foreign policy adjunct in New Zealand, it also needs to be more than that: New Zealand needs to compete internationally for these students, who can and will choose to study elsewhere. The grounds on which New Zealand competes for international students will differ from the grounds on which other countries do. New Zealand will not realistically be able to compete for students who might aspire to study at the Oxbridge or Ivy League colleges. However, New Zealand can compete against Australia in providing robust pastoral care provisions for international students, for example; particularly at this point in that country's export education experience (cf. Wesley, 2009). There is not an inherent tension between the aims of converging foreign and export education policies, and building and maintaining a competitive export education industry, despite what might appear at face value. New Zealand's export education industry can be competitive because of, amongst other things, the international linkages that are developed between Asia and New Zealand and the opportunities given to New Zealand's Asian students and graduates to contribute to these international linkages generally and to New Zealand's foreign policy interests specifically.

Conclusion

The historic links between international education policy and foreign policy in New Zealand reflect their context. International education 50 years ago was not an 'industry' in the way that it is in 2009. The numbers of Asian students in New Zealand are vastly greater in the 21st century than they were in the 1950s and 1960s. The threat of communism is gone, as has (most of) the political instability in Southeast Asia. The ideologies of government policy between 1950 and 2009 have changed, and these changes have particularly affected the public sector and education policy during this period. These changes may be used to explain why 'export' education is not as much in the frame of foreign policy as it used to be. But other changes can support why it should be more in the foreign policy frame than it is. New Zealand's links with Asia are thicker, wider and deeper than they were in 1950. New Zealand's Asian population has grown from less than 2% of the total population in 1950 to over 10% in 2009. In 2009 New Zealand's primary economic partners are not in Europe, as they were in 1950, but are instead in Asia. The New Zealand government remains focused on Asia, as it was in 1950, but for very different reasons. The future with Asia that was painted through New Zealand government documents of the earlier era was one of conflict, fear and instability, with a touch of humanitarian benevolence. The picture painted in recent government documents is quite different. New Zealand's future is intricately tied up with Asia's prospects. Now, more than ever, there is a need to bridge the gap between international education and foreign policies and act strategically on the awareness that New Zealand's Asian alumni – and its Asian populations generally – constitute New Zealand's friends, foreign and domestic.

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2   Sir Frank Holmes' private papers, J.C. Beaglehole Room, Victoria University of Wellington; and provided to author.
3   Sir Frank Holmes' 1988 press statement as chair of CNZEL, in private papers.
4   Recorded in Holmes' private papers.

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Victoria University's Pipitea Campus, Bunny Street, Wellington

This conference is being hosted by the Institute of Policy Studies, School of Government, Victoria University of Wellington, in association with the Philosophy Programme, Victoria University of Wellington and the Centre for Theology and Public Issues, University of Otago.

Keynote Speakers: Professor John Broome • Professor Tom Campbell • Professor William Galston • Meg Munn MP • Professor Thomas Pogge • Professor John Uhr • Professor Jonathan Wolff • Dr Simon Chapple

Purpose

The new millennium has witnessed a resurgence of interest and research about ethical considerations in government, business and international relations.

This unique conference will bring together an international mix of philosophers, political scientists, legal theorists, economists, religious scholars and public policy practitioners to explore the ethical foundations of public policy.

Over two days there will be more than 50 presentations of the latest research and insights on a range of important topics such as:

- what are the ethical constraints on those involved in different aspects of the policy process?

- how should ethical considerations be incorporated into policy advice and decisions?

- what decision rules should we apply when confronted with policy trade-offs and conflicting ethical imperatives?

- what obligations do we have to people in other countries and to future generations?

- how should we measure societal progress?

- how should we protect the global commons for future generations?

- what is the nature of the good society?

Register early as conference attendance is limited

Programme and Registration

Full programme and registration details can be found on the Institute of Policy Studies website at www.ips.ac.nz

Regisration
ips@vuw.ac.nz

Cost:
Conference Fee $120
Fulltime student Fee $80

Conference Dinner
Thursday 10 December,
Grand Hall, Parliament
$110pp

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