The Dollar-Wall Street Regime and New Zealand: The Political Implications of Financial Market Liberalisation for Macroeconomic Management in New Zealand, 1994 to 2011

Byron Richards

A thesis submitted in fulfilment of the degree of Doctor of Philosophy

at the University of Otago, Dunedin,

New Zealand.

December, 2015
Abstract

This is a study of New Zealand’s retention and entrenchment of a neoliberal policy regime, focusing on the role played by international finance. The study examines the influence that international private financial markets and institutions exerted over the macroeconomic policy formulation of New Zealand governments during the period from 1994 to 2011. It is argued that the emergence of international private financial markets and New Zealand’s subsequent integration into these markets was instrumental in successive governments retaining and entrenching all of the core features of a neoliberal macroeconomic policy nexus. This includes, most prominently: a monetary policy regime focused on maintaining low, stable inflation; an independently floating foreign exchange regime; and a conservative fiscal policy oriented towards surplus-generation and public debt reduction.

The study utilises a sophisticated neopluralist theoretical framework that also draws on neo-Marxist analyses developed in the field of international political economy. Within this theoretical framework, neopluralism identifies the key sources of business power within contemporary liberal democracies. Respectively, neo-Marxist international political economy identifies the major sources of the power of private financial capital within an increasingly interconnected global economic system. This theoretical approach provides a coherent and empirically-grounded explanation of the crucial role played by international private financial markets in successive New Zealand governments’ retention and entrenchment of all of the key features of the neoliberal macroeconomic policy nexus.
A critical realist methodology is used to apply the theoretical framework deployed in this thesis. This entails the use of primarily, but not exclusively, qualitative data - such as historical company reports, official government policy statements, official statistics, and interviews with key actors involved in the process - to develop a robust analysis of the influence that international private financial markets exercised over macroeconomic policy formulation in New Zealand during the period from 1994 to 2011. This analysis highlights the causal significance of the political activities of individual human agents, while also identifying the broader underlying causal mechanisms that were at play.

The central finding of this study is that the comprehensive programme of financial market liberalisation and financial sector deregulation implemented by the Fourth Labour Government between 1984 and 1990 effectively served to integrate New Zealand into the Dollar-Wall Street Regime. Comprising the current system governing contemporary international financial relations, the Dollar-Wall Street Regime accords a central role in public macroeconomic management to international private financial markets. The major political effects of New Zealand’s integration into the Dollar-Wall Street Regime during the period from 1994 to 2011 derived from a transformation of the underlying structural relationship between the state and internationally-mobile financial capital. This resulted in a curtailment of the operational autonomy of the state, the ability of citizen voters to exert democratic political influence, and, ultimately, the retention of a neoliberal macroeconomic policy agenda.
Acknowledgements

I would like to acknowledge the support provided by my supervisors during the process of writing this thesis. To my primary supervisor, Brian Roper, and secondary supervisors, Greg Rawlings and Chris Rudd, thank you for the years of encouragement, intellectual support, and guidance. Your commitment and professionalism are truly appreciated. I would also like to express my gratitude to my family, so often neglected during my candidature. Thank you for your steadfast belief in my ability to complete this study. The emotional support and understanding you all provided made this sometimes difficult journey much more bearable. More than anyone else, however, I have to thank my wife, Amanda. For all of the encouragement, gentle reassurance, and loving support you provided over the years I am truly grateful. I doubt this thesis could have been completed without you.
## Contents

Declaration .......................................................................................................................... i
Abstract .............................................................................................................................. ii
Acknowledgements ........................................................................................................... iv
Table of Contents .............................................................................................................. v
List of Figures ...................................................................................................................... vii
List of Tables ....................................................................................................................... ix
List of Abbreviations and Acronyms ................................................................................ x

**Introduction** .................................................................................................................. 1

1. **Towards a Critical Analysis of Business-State Relations** ........................................ 13
   1.1) Critical Realist Methodology ................................................................................ 15
   1.2) Classical Pluralism .............................................................................................. 36
   1.3) The Critics of Classical Pluralism ......................................................................... 44
   1.4) Neopluralism ....................................................................................................... 58
       Conclusion .................................................................................................................. 64

2. **Globalisation, the Dollar-Wall Street Regime, and Global Neoliberalism** ............... 69
   2.1) Capitalism and Globalisation ............................................................................... 71
   2.2) The Dollar-Wall Street Regime ........................................................................... 76
   2.3) The Establishment of the Dollar-Wall Street Regime:
       From Bretton Woods to Global Neoliberalism ....................................................... 88
       Conclusion ................................................................................................................ 110

   3.1) The Fourth Labour Government: A Political Overview ...................................... 114
   3.2) Financial Market Liberalisation and Monetarist Macroeconomic Reform ........... 120
   3.3) Explaining the Shift to Neoliberalism in New Zealand ...................................... 129
       Conclusion ................................................................................................................ 144

   4.1) The Fourth National Government: A Political Overview .................................... 147
   4.2) Fiscal Austerity .................................................................................................... 156
   4.3) Explaining Fiscal Austerity .................................................................................. 187
       Conclusion ................................................................................................................ 215
5. The Fifth Labour Government and Macroeconomic Policy, 1999 to 2008 ........218
   5.1) The Fifth Labour Government: A Political Overview ................................................. 221
   5.2) The Fifth Labour Government’s ‘Third Way’ .......................................................... 232
   5.3) The Fifth Labour Government’s Macroeconomic Policy Nexus .................................. 237
   Conclusion ......................................................................................................................... 265

   6.1) The Domestic Constraints on Government Macroeconomic Policy Formulation, 1999 to 2008 ................................................................................ 269
   6.2) The Dollar-Wall Street Regime’s Constraints on Macroeconomic Policy Formulation, 1999 to 2008 ................................................................................ 276
   6.3) Explaining the Constraints: The Political Implications of Financial Market Liberalisation in New Zealand ................................................................. 289
   Conclusion ......................................................................................................................... 300

   7.1) The Global Financial Crisis .......................................................................................... 304
   7.2) The Fifth National Government: A Political Overview ................................................ 319
   7.3) The Fifth National Government’s Macroeconomic Policy Response to the
        Global Financial Crisis ................................................................................................. 324
   7.4) “A Dark Cloud on the Horizon”: The Dollar-Wall Street Regime and the
        Fifth National Government’s Macroeconomic Policy Agenda .................................. 337
   Conclusion ......................................................................................................................... 354

Conclusion .......................................................................................................................... 356

Bibliography ......................................................................................................................... 368
List of Figures

1.1 ‘Voluntarism’ ................................................................. 23
1.2 ‘Reification’ ................................................................. 24
1.3 The Transformational Model of Social Activity ....................... 26

3.1 The New Zealand Monetary Policy Transmission Mechanism: The Theory of Monetary Disinflation ............................................... 126
3.2 The New Zealand Monetary Policy Transmission Mechanism: The Evidence ................................................................. 126
3.3 The Onset of Stagflation in New Zealand ................................... 140
3.4 The Emergence of Mass Unemployment in New Zealand ............... 141

4.1 Real Economic Growth in New Zealand, 1990 to 1999 .................... 153
4.2 Comparison of Actual, Forecast and Projected Paths of Net Debt Reduction contained in the 1994 and 1995 Budgets ....................... 172
4.3 Comparison of Actual, Forecast, and Projected Operating Balances contained in the 1994 and 1995 Budgets ................................ 172
4.4 Total Annual Government Expenditure, 1990 to 1999 ...................... 180
4.5 *Budget 1995* Debt Reduction Forecast versus Actual Path of Public Debt Reduction ................................................................. 182
4.7 New Zealand’s Current Account Deficits, 1984 to 1994 ................. 204
4.8 Total New Zealand Overseas Debt, March 1994 ............................ 207
4.9 New Zealand’s Current Account Deficits, 1991 to 2000 .................. 211
4.10 New Zealand’s Net External Liabilities, 1991 to 2000 .................... 211
5.1 Real Economic Growth in New Zealand, 1998 to 2008 ......................... 223
5.2 Official Rate of Unemployment in New Zealand, 1998 to 2008 ............... 224
5.3 Daily Changes in New Zealand Overnight Interest Rates, January
    1995 to January 2000 .................................................................................. 243
5.4 International Volatility of Three Month Interest Rates .......................... 244
5.5 The Transmission Mechanism of New Zealand Monetary Policy .......... 248
5.6 CPI Inflation, 2000 to 2008 ...................................................................... 260
5.7 Gross Sovereign-Issued Debt and Net Debt, 1994 to 2008 ................. 261

6.1 Movement in the New Zealand Dollar Trade Weighted Index and
    Real Exchange Rate, 1985 to 2009 .............................................................. 283

7.1 Real Economic Growth in New Zealand, 2005 to 2011 ..................... 322
7.2 Forecast Impact of FNG’s medium-term Fiscal Strategy on Future
    Government Operating Expenses, 2009 to 2023 ..................................... 330
7.3 Forecast Impact of FNG’s medium-term Fiscal Strategy on Future
    Government Debt, 2009 to 2023 ................................................................ 330
7.4 New Zealand Bank and General Government Offshore Debt, March
    2001 to March 2008 .................................................................................. 341
7.5 Forecast Increase in Gross Government Debt Contained in Budget
    2009 ........................................................................................................ 343
7.6 Forecast Impact of FNG’s Austerity Measures on the Future Track of
    Net New Zealand Government Debt Contained within Budget 2009....... 350
List of Tables

1.1 Bhaskar’s four-phase ‘RRRE’ Schema for Practical Explanation in Open Systems.................................................................................................................. 30

2.1 Distribution of Reported Foreign Exchange Market Turnover by Currency, 1995 to 2013.................................................................................................................. 80

2.2 Annual Changes in Official Foreign Exchange Reserves, 2008 to 2013...... 85

2.3 Global Long-Term Growth, 1820 to 1973......................................................... 88

2.4 Comparing the Long Boom and the Long Downturn: Average Profit Rates.................................................................................................................................. 89

2.5 The US Trade Imbalance with Germany, Japan, and the World................. 91

2.6 Estimated Global Annual FX Market Turnover during the Neoliberal Era............................................................................................................................... 101

2.7 Average Daily Global FX and Derivatives Trading, 1998 to 2013............. 101

3.1 Financial Liberalisation in New Zealand......................................................... 122


4.2 Key Components of the Budget 1996 Tax Reduction and Social Policy Programme ........................................................................................................... 175

4.3 Treasury’s Projected Fiscal Deficits, 1990......................................................... 194

4.4 New Zealand’s Net International Investment Position, March 1994....... 205
5.1 The Main Features of New Zealand’s OCR Monetary Policy Regime ...... 242
5.2 The Key Features of New Zealand’s Expectations-Augmented Phillips Curve .................................................................................................................. 249
5.3 Exchange Rate Arrangements in Developed Market Economies .......... 252
5.4 A Statistical Overview of the FLG’s Fiscal Policy Stance .................. 259
5.5 Overview of the 2008 Personal Tax Reforms .................................. 263

7.1 World Economic Growth, 2005 to 2011 ........................................ 321
7.2 Details of the FNG’s April 1 2009 Tax Cuts ..................................... 325
7.3 Details of the FNG’s October 1 2010 Tax Cuts .................................. 333
7.4 Christchurch Earthquake Costs and Funding Sources ...................... 334
7.5 Summary of Budget 2011 Spending versus the Operating Allowance .... 334
7.6 New Zealand’s Net International Investment Position at March 2008 ...... 338
7.7 Asset Structure of New Zealand Banking System, December 2008 ....... 340
<table>
<thead>
<tr>
<th>Abbreviations and Acronyms</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACC</td>
</tr>
<tr>
<td>ACT</td>
</tr>
<tr>
<td>AGC</td>
</tr>
<tr>
<td>ANZ</td>
</tr>
<tr>
<td>APRA</td>
</tr>
<tr>
<td>APS</td>
</tr>
<tr>
<td>BIS</td>
</tr>
<tr>
<td>BNZ</td>
</tr>
<tr>
<td>BPS</td>
</tr>
<tr>
<td>BWS</td>
</tr>
<tr>
<td>CBA</td>
</tr>
<tr>
<td>CDO</td>
</tr>
<tr>
<td>CEE</td>
</tr>
<tr>
<td>CERF</td>
</tr>
<tr>
<td>CHE</td>
</tr>
<tr>
<td>CHRANZ</td>
</tr>
<tr>
<td>COFER</td>
</tr>
<tr>
<td>CPI</td>
</tr>
</tbody>
</table>
DFC  Development Finance Corporation
DWSR  Dollar-Wall Street Regime
ECA  Employment Contracts Act
ECB  Employment Contracts Bill
ECE  Early Childhood Education
EEC  European Economic Community
ERA  Employment Relations Act 2000
ESI  Economic and Social Initiative
EQC  Earthquake Commission
FDI  Foreign Direct Investment
FF  Federated Farmers
FIRE  The Finance, Insurance, and Real Estate Industries
FLG  Fifth Labour Government
FNG  Fifth National Government
FPP  First Past the Post
FRA  Fiscal Responsibility Act
FSR  Fiscal Strategy Report
FX  Foreign Exchange
GAAP  Generally Accepted Accounting Practice
<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>GATS</td>
<td>General Agreement on Trade in Services</td>
</tr>
<tr>
<td>GCS</td>
<td>Government Computer Services</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>GFC</td>
<td>Global Financial Crisis</td>
</tr>
<tr>
<td>GMFI</td>
<td>Guaranteed Minimum Family Income</td>
</tr>
<tr>
<td>GRI</td>
<td>Guaranteed Retirement Income</td>
</tr>
<tr>
<td>GSID</td>
<td>Gross Sovereign-Issued Debt</td>
</tr>
<tr>
<td>GST</td>
<td>Goods and Services Tax</td>
</tr>
<tr>
<td>HSBC</td>
<td>Hong Kong and Shanghai Banking Corporation</td>
</tr>
<tr>
<td>IFTC</td>
<td>Independent Family Tax Credit</td>
</tr>
<tr>
<td>IIP</td>
<td>International Investment Position</td>
</tr>
<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
</tr>
<tr>
<td>IPFM</td>
<td>International Private Financial Markets</td>
</tr>
<tr>
<td>JSS</td>
<td>Job Support Scheme</td>
</tr>
<tr>
<td>LIBOR</td>
<td>London Inter-Bank Offered Rate</td>
</tr>
<tr>
<td>LTCM</td>
<td>Long Term Capital Management</td>
</tr>
<tr>
<td>MBS</td>
<td>Residential Mortgage-Backed Security</td>
</tr>
<tr>
<td>MMP</td>
<td>Mixed Member Proportional</td>
</tr>
<tr>
<td>MNC</td>
<td>Multi-National Corporation</td>
</tr>
<tr>
<td>Abbreviation</td>
<td>Full Form</td>
</tr>
<tr>
<td>--------------</td>
<td>-----------</td>
</tr>
<tr>
<td>MP</td>
<td>Member of Parliament</td>
</tr>
<tr>
<td>MPTM</td>
<td>Monetary Policy Transmission Mechanism</td>
</tr>
<tr>
<td>NBR</td>
<td>National Business Review</td>
</tr>
<tr>
<td>NBFI</td>
<td>Non-Bank Financial Institution</td>
</tr>
<tr>
<td>NGO</td>
<td>Non-Governmental Organisation</td>
</tr>
<tr>
<td>NIFA</td>
<td>New International Financial Architecture</td>
</tr>
<tr>
<td>NSW</td>
<td>Bank of New South Wales</td>
</tr>
<tr>
<td>NZBR</td>
<td>New Zealand Business Roundtable</td>
</tr>
<tr>
<td>NZCTU</td>
<td>New Zealand Council of Trade Unions</td>
</tr>
<tr>
<td>NZD</td>
<td>New Zealand Dollar</td>
</tr>
<tr>
<td>NZEF</td>
<td>New Zealand Employers Federation</td>
</tr>
<tr>
<td>NZIER</td>
<td>New Zealand Institute of Economic Research</td>
</tr>
<tr>
<td>NZMF</td>
<td>New Zealand Manufacturers Federation</td>
</tr>
<tr>
<td>NZSF</td>
<td>New Zealand Superannuation Fund</td>
</tr>
<tr>
<td>NZX</td>
<td>New Zealand Stock Exchange</td>
</tr>
<tr>
<td>OBEGAL</td>
<td>Operating Balance Before Gains and Losses</td>
</tr>
<tr>
<td>OCR</td>
<td>Official Cash Rate</td>
</tr>
<tr>
<td>OECD</td>
<td>Organisation for Economic Cooperation and Development</td>
</tr>
<tr>
<td>OPEC</td>
<td>Organisation of the Petroleum Exporting Countries</td>
</tr>
<tr>
<td>Abbreviation</td>
<td>Description</td>
</tr>
<tr>
<td>--------------</td>
<td>-------------</td>
</tr>
<tr>
<td>OTC</td>
<td>Over the Counter</td>
</tr>
<tr>
<td>PIE</td>
<td>Portfolio Investment Entity</td>
</tr>
<tr>
<td>PFA</td>
<td>Public Finance Act</td>
</tr>
<tr>
<td>PFMA</td>
<td>Public Finance Management Amendment Act</td>
</tr>
<tr>
<td>PPP</td>
<td>Purchasing Power Parity</td>
</tr>
<tr>
<td>PTA</td>
<td>Policy Targets Agreement</td>
</tr>
<tr>
<td>RBA</td>
<td>Reserve Bank Act</td>
</tr>
<tr>
<td>RBNZ</td>
<td>Reserve Bank of New Zealand</td>
</tr>
<tr>
<td>SDC</td>
<td>Southland Development Corporation</td>
</tr>
<tr>
<td>SIV</td>
<td>Structured Investment Vehicle</td>
</tr>
<tr>
<td>SME</td>
<td>Small and Medium-Sized Enterprise</td>
</tr>
<tr>
<td>SSA</td>
<td>State Sector Act</td>
</tr>
<tr>
<td>TAF</td>
<td>Term Auction Facility</td>
</tr>
<tr>
<td>TMSA</td>
<td>Transformative Model of Social Activity</td>
</tr>
<tr>
<td>TRSPP</td>
<td>Tax Reduction and Social Policy Programme</td>
</tr>
<tr>
<td>UDC</td>
<td>United Dominions Corporation</td>
</tr>
<tr>
<td>UDT</td>
<td>United Dominions Trust</td>
</tr>
<tr>
<td>UIP</td>
<td>Uncovered Interest Rate Parity</td>
</tr>
<tr>
<td>USD</td>
<td>United States Dollar</td>
</tr>
<tr>
<td>Abbreviations</td>
<td>Description</td>
</tr>
<tr>
<td>---------------</td>
<td>-------------</td>
</tr>
<tr>
<td>WB</td>
<td>World Bank</td>
</tr>
<tr>
<td>WFF</td>
<td>Working For Families</td>
</tr>
<tr>
<td>WPC</td>
<td>Wellington Policy Community</td>
</tr>
<tr>
<td>WTO</td>
<td>World Trade Organisation</td>
</tr>
</tbody>
</table>
Introduction

In 2007, a mounting wave of defaults on loans in the US ‘subprime’ mortgage market triggered a Global Financial Crisis (GFC). After initially appearing largely unaffected by rapidly rising foreclosures in the US housing market, Wall Street was suddenly overwhelmed by bad debts. Indeed, by the end of the following year all of the major Wall Street investment banks - Bear Stearns, Lehman Brothers, Merrill Lynch, JP Morgan, and Goldman Sachs - had either collapsed, undergone a forced merger, or had their regulatory status fundamentally revised.¹ The tumult on Wall Street rapidly proliferated throughout the global financial system. International credit markets, including the key inter-bank lending market, effectively became frozen, thereby engendering a global ‘credit crunch.’ Subsequently, the deep malaise affecting the global financial system spread to the rest of the global economy. The resulting economic downturn was by far the worst experienced since the Great Depression.

The events surrounding the GFC and the ensuing global economic recession demonstrated the significant impact that developments in the international financial arena are capable of having on states and their formulation of public policy. In the immediate aftermath of the US ‘subprime’ crisis, for example, many states undertook substantive policy measures in order to prop up significantly weakened domestic financial systems. In the case of the

UK and the US, this involved the provision of massive publicly funded bailouts of privately owned banks. For other states, such as New Zealand, it involved the implementation of new regulatory measures (such as increased minimum capital reserve requirements for banks) and the introduction of wholesale and retail deposit guarantee schemes. In addition, while many of the advanced capitalist economies sought to stave off recession via the introduction of large fiscal stimulus packages in 2009, New Zealand’s newly-elected Fifth National Government (FNG) found its own fiscal policy options considerably stymied. Due to the threat of a national credit rating downgrade, the FNG could introduce only modest expansionary fiscal measures in Budget 2009.2

It is thus important that scholarly accounts of New Zealand’s political economy consider the influence that international private financial interests are capable of wielding over government policy formulation. Indeed, failure to do so ultimately renders such accounts incomplete. This reality is clearly acknowledged within the extant literature. From 1984 onwards, New Zealand underwent a major shift from social democratic Keynesianism to a radical brand of market-oriented neoliberalism. Since then, the hard core of this policy framework has been retained and entrenched by successive New Zealand governments. Existing explanatory accounts highlight a number of important underlying causes of New Zealand’s historic shift to, and subsequent retention and entrenchment of neoliberalism. Included amongst the identified causes is the key role played by international private financial capital.

Existing Explanatory Accounts

Prominent amongst existing explanatory accounts of the shift to a neoliberal policy framework in New Zealand are those based on either Marxist

\[^{2}\text{Despite its apparent fiscal moderation, the Fifth National Government's operating deficit was nevertheless substantial. The Financial Statements of the Government of New Zealand reveal that the combination of significantly reduced revenues and increasing expenses resulted in a NZ$10.5 billion operating deficit for the year. See Treasury 2009, Budget 2009 (Wellington: Treasury), 6.}\]
or neopluralist analyses. Possibly the most sophisticated Marxist account to date is that of Roper. Roper’s explanation centres on four distinctive, but interrelated, components. First, the collapse of the ‘long boom’ and the subsequent onset of prolonged economic stagnation greatly increased the economic pressures on the state and, consequently, significantly increased the pressure on New Zealand governments to formulate public policy in the interests of business. Second, a shift in the balance of societal power in favour of business in the late 1970s and early 1980s occurred in part because “employers became increasingly industrially militant” and also more politically active. Roper argues that this activism has since been primarily directed “towards lobbying successive governments” to maintain and extend “the neoliberal policy agenda.” Third, the historical shift in the international economic orthodoxy from Keynesianism to neoliberalism in the mid-1970s influenced the shift in the societal balance of power between the working class and business in favour of the latter. It also “subsequently...provided the broad intellectual and ideological paradigm for policy making” in New Zealand. Finally, the institutional structure of the state or, more specifically, “the strategic location of Treasury and the Reserve Bank”, the ‘unicameral’ parliamentary system, and the “institutional dominance” of cabinet, are seen to be important in explaining why neoliberalism was implemented so rapidly and comprehensively in New Zealand, and why the hard core of the neoliberal programme has subsequently been retained and entrenched.

---

5 Ibid.
6 Ibid.
7 Ibid.
8 Ibid.
Roper subsequently elaborated on his explanatory account in work published separately.9 A “central concern” of this additional work was to highlight that external “global forces” were also of considerable explanatory importance in relation to New Zealand’s historic shift in policy-making from Keynesianism to neoliberalism.10 External forces associated with international private financial capital figured prominently amongst those discussed. Indeed, according to Roper, one of the most important dimensions of contemporary ‘globalisation’ is that which encompasses “the New Zealand financial system and its relationship to shifting patterns of global finance, foreign investment, and the size of public and private offshore debt.”11 However, for Roper, while “at a high level of generality it [was] possible to identify broad dimensions of the process of globalisation and its impact on New Zealand”, extensive additional research focusing on the impact of each of the various dimensions of the globalisation process on the historic shift in New Zealand politics from Keynesianism to neoliberalism was ultimately required.12

Foremost amongst neopluralist explanatory accounts is that of Mulgan. To a significant extent, Mulgan’s account largely accords with that of Roper. The influence of Treasury, the role of business political activism, and the state of the economy are highlighted as important, as well as the underlying structure of government in New Zealand and the central position of cabinet within it.13 Where Mulgan’s account differs significantly, however, is in its explicit acknowledgment of the role played by international private financial markets (IPFMs) in the entrenchment of neoliberalism. The structural constraint presented by a “fear of adverse market reaction” is cited, for example, as a key reason why substantive social democratic policies such as greatly increased

---

11 Ibid, 29.
12 Ibid, 30.
“public expenditure on health and education” or significant wealth redistribution measures are “kept off the [political] agenda.” Mulgan observes that underpinning “the increasing political power of financial interests is the greater mobility of capital” that has resulted from “the process of financial deregulation...undertaken in the mid-1980s.” Financial assets can now be moved rapidly in and out of the country and “such movement critically affects the value of the New Zealand dollar and also interest rates, both of which are key components of any government’s economic strategy.” As a result, Mulgan points out that IPFMs now represent a “central participant in government decision making in New Zealand.”

Alongside these distinctively Marxist and neopluralist explanations stand a number of other important accounts lacking any overt theoretical orientation. Most prominent amongst these are the accounts provided by Jesson (1999) and Kelsey (1999, 2015). Jesson openly states that he believes that it has been the spread of what he terms a “finance culture” within both the state and society that has primarily underpinned the shift to and subsequent entrenchment of neoliberalism in New Zealand. Jesson contends that as a result of the spread of this finance culture, any government that “seriously” attempts to revise the neoliberal policy framework will face immense opposition from the business elite and government bureaucracy.

Jesson locates the source of this new finance culture within the collapse of the post-war ‘Bretton Woods’ international monetary system (BWS) and the

---

14 Ibid 314, 317.
16 Ibid, 318
17 Ibid.
18 B. Jesson 1999, Only Their Purpose is Mad: The Money Men Takeover New Zealand (Palmerston North: Dunmore Press); J. Kelsey 1999, Reclaiming the Future (Auckland: Auckland University Press); 2015, The FIRE Economy (Wellington: Bridget Williams Books). It is important to note that, while not overtly stated, these analyses are nevertheless based on various theoretical assumptions. Jesson, for example, explicitly states (1999, 153) that he is a socialist, and thus his account can be characterised as broadly (but not strictly) Marxist in nature.
20 Ibid, 7-8, 16, 210-212.
massive increase in speculative financial activity this engendered. The collapse of the BWS is seen to have ultimately “magnified the power of...finance” within the New Zealand economy, which, in-turn, tipped the balance of societal power “decisively in favour of finance” and led to the “phenomenal” rise of a finance-oriented business and bureaucratic elite in New Zealand. Jesson argues that this finance-elite “now dominates political discourse” within New Zealand’s political economy and thus presents a serious obstacle to any meaningful retrenchment of the neoliberal reforms.

In terms of their treatment of the role of international finance in cementing New Zealand’s shift to neoliberalism, Kelsey’s respective explanatory accounts are possibly the most sophisticated. In her 1999 work Reclaiming the Future, for example, she notes, that “perhaps the most powerful barrier to deviating from the free market path...is fear of how ‘the markets’ would respond.” Kelsey locates the genesis of this important barrier to substantive retrenchment of neoliberalism in the breakdown of the BWS in the early 1970s. The shift to floating foreign exchange (FX) regimes, increased financial market deregulation, and financial ‘innovation’ resulting from the collapse of the BWS are seen to have led to the creation of “a predatory,...speculation-driven global financial system” that now poses “a major threat to [New Zealand’s] economic stability.” Kelsey argues that as a consequence of this major shift in the global economic environment, “the prospect of a downgrade in New Zealand’s credit rating” has emerged as a key “justification for keeping the neoliberal programme on track.”

Respectively, in her 2015 work, The FIRE Economy, Kelsey outlines how this significant barrier to the substantive retrenchment of neoliberalism has

---

21 Ibid 46-59.  
22 Ibid, 39, 46, 48.  
23 Ibid, 58.  
24 Kelsey 1999, 77.  
26 Ibid, 147, 153.  
27 Ibid 77, 80-83.
been locked into place via a host of international free trade and investment agreements. New Zealand is bound by “the WTO’s Financial Services Agreement” (also known as the General Agreement on Trade in Services (GATS)), as well as “a raft of [other] commercial treaties”, states Kelsey.\(^\text{28}\) Driven by powerful private US financial interests, these various “agreements apply to the broad spectrum of financial services – from banks, insurers and derivatives traders to credit-rating agencies and financial media – as well as cross-border flows of capital.”\(^\text{29}\) Kelsey argues that a key function of these international financial services agreements has been to effectively constrict the “policy space” available for domestic financial regulation and control.\(^\text{30}\) Fundamentally, New Zealand governments are now, to a significant extent, legally precluded from implementing substantive revisions of the country’s highly liberalised regulatory regime.\(^\text{31}\) As Kelsey observes, crucially, this includes regulation of the capital account; the ability of New Zealand governments “to control the volume or makeup of capital flows in and or out of [the] country” has been severely curtailed.\(^\text{32}\) As a result, the significant IPFM-derived constraints faced by the state in New Zealand have been effectively embedded.\(^\text{33}\) International financial capital is guaranteed a high degree of operational flexibility and kinetic freedom within the New Zealand economy,
thereby ensuring the ongoing reproduction of external financial disciplines on the broad spectrum of state policy formulation.

**The Approach of this Study**

This thesis extends these existing accounts by providing an original explanatory account focusing on the important (but sometimes underappreciated) role played by IPFMs in the retention and entrenchment of the neoliberal policy regime. Building on an earlier study published in 2010, this thesis investigates the major political implications of financial market liberalisation in New Zealand. It does this by undertaking a detailed historical exploration of the significant influence that IPFMs have exerted over the public policy formulation of successive governments. The focus of the investigation is limited in two important ways. First, while its overall scope is much broader, the main chronological focus of the investigation is on the period from 1994 to 2011. That is, it is primarily concerned with the period after the major neoliberal reforms had been implemented (and the chief political architects had left government) up until and including the immediate aftermath of the GFC. Second, the principal focus of the investigation is on core macroeconomic policy; monetary, foreign exchange, and fiscal policy. This is because of its central importance in determining the overall shape of broader government policy agendas. Fundamentally, the way in which it is formulated has considerable bearing on virtually all other aspects of public policy.

The investigation draws extensively on the rich body of literature published in the field of critical international political economy that examines the closely intertwined relationship between the global economic dominance of private international finance and the ongoing prevalence of neoliberalism. In

---

particular, it integrates the analysis developed by Peter Gowan in his seminal (1999) work, *The Global Gamble*. Centrally, Gowan’s analysis contends that since the breakdown of the BWS in the early 1970s, international financial relations have operated under what he refers to as the ‘Dollar-Wall Street Regime’ (DWSR). Under the DWSR, extensive power in international monetary affairs is accorded to the US state. In addition, Wall Street-centred IPFMs play a core role in the public macroeconomic management of most governments around the world.

This thesis develops a sophisticated neopluralist theoretical framework. This approach maintains that, due to the nature of the capitalist system of economic organisation, business interests possess a disproportionate capacity to exert influence over the modern liberal democratic state. It upholds that, in comparison to other societal interests, business generally has access to superior economic resources, enabling more effective engagement in the liberal democratic political process. More importantly, however, neopluralism also maintains that business possesses significant structural power, while also acknowledging that it is ultimately historically contingent and contested by other groups in society.

A neopluralist theoretical framework offers a strong conceptual foundation on which to base the following empirical study of the relationship between internationally-mobile financial capital and the state in contemporary New Zealand. In particular, it provides a coherent, empirically-grounded way to explain the crucial role played by IPFMs in successive New Zealand governments’ retention and entrenchment of all of the key features of the neoliberal macroeconomic policy nexus. It also provides a rigorous analytical foundation on which to base a critical evaluation of the extant political arrangements that allow internationally-mobile financial capital to exert

---

significant influence over public macroeconomic policy formulation in New Zealand.

This thesis adopts a critical realist methodology. Critical realism constitutes a distinct alternative to the naturalist and hermeneutical traditions that have traditionally dominated social scientific investigation. It refutes the methodological individualism associated with naturalist methods, which effectively reduces social scientific enquiry to an examination of the activity of individual human agents isolated from their discrete historical contexts. Simultaneously, it rejects the methodological holism that is characteristic of the hermeneutical tradition, which over-emphasises the causal significance of broad structural factors in determining historical outcomes, and also critically understates the importance of individual agents. Instead, the critical realist methodology employed in this thesis upholds the fundamental importance of considering both individual agency and the influence of broader social structures when explaining social and historical phenomena.

Centrally, this thesis argues that the comprehensive programme of financial market liberalisation implemented by the Fourth Labour Government effectively served to integrate New Zealand into the DWSR. Continued integration into the DWSR subsequently placed considerable constraints on the macroeconomic policy formulation of successive New Zealand governments throughout the period from 1984 to 2011. In particular, all of these governments, regardless of party composition or ideological orientation, faced significant implied pressure from IPFMs to closely adhere to all of the key features of the neoliberal macroeconomic policy regime. This included, most notably: a ‘monetarist’ approach to monetary policy primarily aimed at maintaining low, stable levels of inflation; a freely-floating FX regime; and a conservative “surplus-driven, low debt” approach to fiscal policy. From this, the thesis

---

36 Gowan 1999.
contends that the major political implication of financial market liberalisation in New Zealand has been a transformation of the underlying structural relationship between the state and internationally-mobile financial capital. It is argued that this development has refined the structural constraints on the state, resulting in a curtailment of both the operational autonomy of the state, and also of the ability of citizen voters to exert democratic political influence.

Organisation of the Thesis

The study is organised into seven chapters. Chapter One begins by delineating the key features of the critical realist methodology being used to apply the neopluralist theoretical framework developed in this thesis to the critical analysis of New Zealand’s retention of all of the key features of the neoliberal macroeconomic policy nexus. The chapter then outlines the underpinning neopluralist theoretical framework necessary in order to guide the following empirical and historical study. This entails an examination and critical assessment of the major theoretical perspectives that seek to explain business-state power relations in contemporary liberal democratic states. Through this process, I establish that a neopluralist theoretical perspective is the most useful to adopt for the empirical study that follows. The focus of Chapter Two is on the regime governing contemporary international monetary relations, Gowan’s DWSR. The chapter examines the underlying nature of globalisation, the structure and function of the DWSR, and how the DWSR became established. This latter issue specifically involves a detailed discussion of the global rise and spread of neoliberalism. Chapter Three describes how New Zealand became integrated into the DWSR through the neoliberal policy reforms implemented by the Fourth Labour Government during the period from 1984 to 1990. Subsequently, it outlines the major existing explanations of New Zealand’s historic shift to neoliberalism and suggests that additional causal factors should also be considered. Appendix A contains an expanded
account of New Zealand’s historic shift to neoliberalism, building on the existing explanations outlined in Chapter Three.

Following Chapter Three, the focus of the thesis shifts. The principal subject of attention becomes the political effects of New Zealand’s integration into the DWSR. Chapter Four analyses these in relation to the Fourth National Government (in power from 1990 to 1999). The key features of the Fourth National Government’s fiscal austerity strategy are discussed in detail and then the key explanatory factors are considered. The DWSR is highlighted as an important factor driving both its initial implementation and its subsequent retention. Chapter Five outlines the so-called ‘Third Way’ approach to public policy making pursued by the Fifth Labour Government (FLG) during the period from 1999 to 2008. This involves a detailed examination of the core features of the FLG’s macroeconomic policy nexus – monetary policy, fiscal policy, and FX policy. In Chapter Six, the key constraints on the macroeconomic policy formulation of the FLG are examined. Particular attention is paid to the impact that integration into the DWSR had on the New Zealand state’s operational autonomy during the period from 1999 to 2008. This comprehensive account is subsequently used to discern the value that Gowan’s DWSR analysis provides for a neopluralist model of the New Zealand state. Chapter Seven corroborates the overall importance and explanatory power of this DWSR-based analysis for our understanding of the operation of the New Zealand state during the neoliberal-era. It does this by examining the influential role played by IPFMs in determining the overall shape and scope of the FNG’s macroeconomic policy response to the GFC during the period from 2008 to 2011.
Towards a Critical Analysis of Business-State Relations

Introduction

Ongoing research into the nature of business-state power relations in modern liberal democratic societies highlights the need for theoretical models to account for the significant and inequitable political power that private financial capital derives from its dominant position in both the domestic and global economic systems. This is an important issue to study as it raises serious questions about how effective contemporary liberal democratic systems are at expressing the actual political will of an electorate due to the potential for interest groups based on financial capital interests to exert disproportionate influence over state policy formulation. This chapter will seek to examine and critically assess the key theoretical perspectives seeking to explain the power dynamics operating in modern liberal democratic political systems. These theoretical perspectives comprise classical pluralism and the main paradigms critical of classical pluralism; Marxism, the Neo-Weberian state-centred perspective, and neopluralism. Although each of these perspectives afford valuable insights into the power dynamics operating within the bounds of the modern liberal democratic state, neopluralism is the most useful to adopt for this study.

The overall theoretical approach developed in this study combines neopluralism with some of the central theoretical insights of neo-Marxist critical
international political economy. Centrally, it draws on the work of Gowan, especially his influential Dollar-Wall Street Regime (DWSR) analysis developed in *The Global Gamble*. It also draws extensively on the work of authors influenced by Gowan. This includes, most prominently, the analyses developed by Panitch and Gindin. Within this theoretical framework, neopluralism identifies the key sources of business power within contemporary liberal democracies. Respectively, neo-Marxist international political economy identifies the major sources of the power of private financial capital within an increasingly inter-connected global economic system. Fundamentally, utilising a sophisticated neopluralist theoretical framework in conjunction with the central insights of critical international political economy enables us to explain why private financial capital holds such a powerful position (both domestically and globally) within the hegemonic neoliberal capitalist system. It also provides a rigorous conceptual framework on which to base a critical evaluation of the current political arrangements that allow financial capital to exert frequently dominant influence over government and public policy formulation.

---

1 The overall theoretical approach developed in this thesis could thus be accurately described as constituting a kind of hybrid “neopluralist-neo-Marxist” theoretical approach. For the purpose of simplicity, however, throughout this thesis it will generally be referred to as a sophisticated neopluralist theoretical approach.
2 Gowan 1999.
1.1) **Critical Realist Methodology**

In broad terms, Roy Bhaskar’s critical realism consists of two core elements. The first of these, termed ‘transcendental realism’, comprises Bhaskar’s philosophy of the natural sciences.\(^4\) As such, in isolation, it is not of central relevance to the methodology being developed for use in this thesis. However, as Toby Boraman observes, “transcendental realism...provides the foundation for his philosophy for the social ‘sciences’.”\(^5\) Therefore, while it will not be accorded extensive treatment at this juncture, a brief sketch of the core features of Bhaskar’s transcendental realism will nevertheless be undertaken here. Principally, this will allow for a fuller understanding of the philosophical underpinnings of the social scientific methodology being deployed in the body of this thesis.

As Andrew Collier observes, “no philosophy exists in a vacuum; there are always particular opposing philosophies which coexist in any historical period, and every philosophy engages, implicitly or explicitly, in controversy with its opponents.”\(^6\) Transcendental realism is no exception to this. It stands as a distinctly ‘middling’ philosophical course running between the comparatively polar competing theories of the natural sciences of ‘classical empiricism’ and ‘idealism’.\(^7\)

Classical empiricism can be most effectively conceived of as entailing “a ‘clean slate’ approach” to ontological thought.\(^8\) It upholds “a conception of people as passive sensors of given facts and recorders of their given constant conjunctions”, and a parallel contention that “knowledge can always be


\(^8\) Collier 1994, 71.
analysed in a purely individualistic way.”9 Respectively, and in stark contrast to classical empiricist perspectives, an idealist approach to the philosophy of science is based around an ontology contending that “the objects of scientific knowledge” are, ultimately, “a construction of the human mind.”10 In other words, they “are artificial constructs and though they may be independent of particular men, they are not independent of men or human activity in general.”11

At heart, transcendental realism accepts the key classical empiricist contention that the world exists independently of human perception.12 However, simultaneously, transcendental realism categorically denies the classical empiricist contention that individuals have the ability to view the world objectively as entirely detached and impartial observers; it fundamentally objects to the notion that “the edifice of knowledge” can in any way have wholly “indubitable foundations” entirely “abstracted from any historical and social context.”13 The key problem, as Bhaskar points out, is that classical empiricism “never enquires for a moment into its [pre-existing] conditions... (In this it is irredeemably pre-critical)” and thus “amounts to a systematic repression of the fact that we learn from others how we learn from nature.”14 Classical empiricism quite simply fails to “recognise that what we experience is determined not just by what is there, but by what we have already learned.”15

In contrast to classical empiricism, Bhaskar’s transcendental realism notices the necessarily subjective perceptions of human observers. It upholds that knowledge is fundamentally “a transient historical phenomenon” resulting

---

11 Ibid.
13 Collier 1994, x. See also Gosden, 10.
14 Bhaskar 1989, 64.
15 Collier 1994, 72.
from a taught interpretation and thus also constitutes a more general social ideology. However, this is not to say that transcendental realism accepts the idealist assertion that subjective perception is the sole determinant of truth/knowledge. Bhaskar argues that such a perspective would involve upholding what he terms the ‘epistemic fallacy’.

The epistemic fallacy is, in essence, the mistaken analysis of statements about being “in terms of statements about knowledge.” This fallacy is symptomatic of a tacit conflation of the ‘intransitive’ and ‘transitive’ domains. The ‘intransitive domain’ consists of a space where, Bhaskar claims, “things in general exist and act independently of their descriptions.” Correspondingly, as Boraman outlines, “the ‘transitive domain’ refers to theories, models, paradigms and facts that seek to describe, measure and explain the material things and structures of the ‘intransitive domain’.” In-effect, the failure to establish a clear division between these two realms leads to an explicit or implicit denial that “knowledge follows existence, in logic and time” and, as Bhaskar argues, “any philosophical position” that fails to recognise this has in-fact “got things upside down.”

In opposition to idealism and its epistemic fallacy, for transcendental realism “it is not a necessary condition for the existence of the world that science occurs. But it is a necessary condition for the occurrence of science that the world exists and is of a certain type.” Thus, it can be seen, Bhaskar’s transcendental realism forms a sort of ‘hybrid’ school of thought containing key

---

16 Bhaskar 1989, 64.
17 Boraman, 93.
18 Bhaskar 2008, 36-45.
19 Ibid, 36.
21 Boraman, 94.
23 Ibid.
elements derived from both classical empiricism and idealism. As Bhaskar summarises:

It regards the objects of knowledge as the structures and mechanisms that generate phenomena; and the knowledge as produced in the social activity of science. These objects are neither phenomena (empiricism) nor human constructs imposed upon phenomena (idealism), but real structures which endure and operate independently of our knowledge, our experience and the conditions which allow us access to them.

As noted above, this transcendental realist philosophy of the natural sciences forms the basis of his respective philosophy for the social sciences. Indeed, as Andrew Collier observes, Bhaskar’s philosophy of the social sciences ultimately “refers to [Bhaskar’s] development of the possible implications of transcendental realism for the human sciences.” This philosophy, forming the second (and, for the purposes of this thesis, more important) core element of Bhaskar’s critical realism, is entitled ‘critical naturalism’.

The history of the philosophy of the social sciences has been dominated by two main, polarised epistemological and ontological positions. At one end of the spectrum, a dominant ‘naturalist’ (or ‘realist positivist’) tradition has argued for a virtual “unity of method between the natural and social sciences.” According to this school of thought both the natural and human sciences are considered to concord with a positivist model of science, which sees science as “value-free, atomistic, [and] discovering causal laws of a

---

24 Boraman, 92.
26 Collier 1994, xi.
27 Ibid.
28 R. Bhaskar 1998, The Possibility of Naturalism: A Philosophical Critique of the Contemporary Social Sciences (3d ed.) (London; New York: Routledge), 1, 17; G. Steinmetz 1998, “Critical Realism and Historical Sociology”, Comparative Studies in Society and History, Vol. 40, 170. However, as Steinmetz points out, it is important that such a “dichotomous model” does not conceal the actual underlying heterogeneity of each of these groupings. For further discussion see ibid, 170-171.
29 Bhaskar 1998, 2.
“constant conjunction” model (whenever A happens, B happens).” As a result, those subscribing to such a perspective argue that social science should primarily function to isolate objective causal laws capable of being expressed in the form of “universal statements” of a constant conjunction type.

In diametric opposition to this ‘naturalist’ tradition is an anti-naturalist ‘hermeneutical’ tradition. The hermeneutical tradition centrally upholds “an absolute contrast between the science of the physical non-human world of nature and the science of the [social] world of mind, of culture, and of history.” As Bhaskar observes, followers of a hermeneutic philosophy of the social sciences usually accept the positivist explanation of the natural sciences or “at least its implicit ontology”. However, the hermeneutic tradition contends that the nature of the subject matter (that is, social realities) precludes the discovery of causal explanations in the social sciences. Consequently, subscribers to a hermeneutic school of thought uphold that the results of social science are instead, by necessity, “non causal and often tied to the views of the people being studied.”

Bhaskar’s critical naturalism stands as a distinct alternative to both of these dominant traditions within the philosophy of the social sciences. At its heart stands a rejection of what is perceived to be the problematic shared ontology of the positivist and hermeneutic schools of thought; the assumption of a ‘constant conjunction’ model of the natural sciences. As Collier outlines, Bhaskar’s critical naturalism argues “that natural laws should be expressed not
as constant conjunctions...but as tendencies,” and that “this applies even to the most rigorous and basic laws of nature.” It follows from this that critical naturalists maintain that social science should not look for strict regularities but instead look for tendencies and that “these tendencies (contra the hermeneutic philosophers) are causal.”

It is fundamentally on this basis that critical naturalists agree with the basic underlying view of a naturalist philosophy of the social sciences, “insofar as it argues for the possibility of an explanatory social science (that is, a social science whose basic goals are similar to the natural sciences).” It is also fundamentally on this basis that critical naturalists categorically reject the hermeneutic claim of “a radical division between the methodology of the social and the natural sciences.” Critical naturalism, however, stands as a ‘tempered’ or ‘qualified’ version of naturalism. More specifically, it upholds a number of important “limits on the possibility of naturalism” that derive from inherent characteristics of the social world that are perceived to restrict the efficacy of the methods of the natural sciences when applied to the study of society. The various sets of limits on naturalism delineated by Bhaskar are characterised as ‘epistemological’, ‘relational’, and ‘ontological’ respectively.

The principle epistemological limit on naturalism derives from the fact that “the objects of social scientific enquiry...only ever manifest themselves in open systems.” The central implication of this inherent impossibility of closed systems for social scientific methodology is that the social sciences are prevented, in principle, from being able to “shut off the effects of processes which are not being tested in order to isolate and test a single mechanism” and,

---

37 Ibid, 329.
38 Ibid, 330.
39 Steinmetz 1998, 175.
40 Boraman, 95.
41 Steinmetz 1998, 175; Poata-Smith, 22.
44 Ibid, 45.
as a result, they are “denied... decisive test situations for their theories.”

According to Bhaskar, this ultimately requires “that the criteria for the...development...of theories in social science cannot be the discovery” of causal laws of a constant conjunction-type. Instead, the criteria can only be the discovery of tendencies that must by necessity be purely “explanatory and non-predictive.”

The principle relational limit on naturalism is that the social sciences are in essence internal to their subject matter. “They are themselves an aspect of, and causal agent in, what they seek to explain.” This subject-object relational condition contrasts directly with the natural sciences where, as Bhaskar observes, “in general...the objects of knowledge exist and act independently of the process of the production of the knowledge of which they are the objects.”

The methodological significance of this is that the process of knowledge production in the social sciences is characterised by an in-built “hermeneutic dimension” that Bhaskar terms “causal interdependency.” This refers to the fact that the objects of social scientific enquiry “may be causally affected by social science and in some cases not exist independently of it”, and, conversely, the social sciences themselves may be conditioned by developments in wider society. It is to be observed, however, that for Bhaskar (in contradistinction to hermeneutic schools of thought) such causal interdependency does not enervate the underlying transcendental realist assertion of the object’s existential intransivity. The existential intransivity of an object is maintained as an a priori “condition of any investigation” applying uniformly to both the social and

46 Bhaskar 1998, 46. It is to be observed that this is not seen by critical naturalists to denigrate the ultimate validity of social scientific results. Indeed, Bhaskar argues that: as long as “a social scientific theory or hypothesis has been independently validated (on explanatory grounds) then one is in principle just as warranted in applying it transfactually as a natural scientific one” (1998, 46).
47 Ibid, 47.
48 Bhaskar 1998, 47. See also Steinmetz 1998, 181.
49 Bhaskar 1998, 47.
50 Ibid.
51 Ibid.
natural sciences, but the “categorical properties” of the objects under study are seen to qualitatively differ between the social and natural sciences. That the social sciences “are themselves an aspect of, and causal agent in”, the objects they seek to explain is one such key qualitative difference.52

The principle ontological limits on naturalism derive from “the activity-, concept-, and space-time-dependence of social structures.”53 To quote Bhaskar at length, critical naturalists contend that:

1. Social structures, unlike natural structures, do not exist independently of the activities they govern.
2. Social structures, unlike natural structures, do not exist independently of the agents’ conceptions of what they are doing in their activity.
3. Social structures, unlike natural structures, may be only relatively enduring (so that the tendencies they ground may not be universal in the sense of space-time invariant).54

As a result of these apparent specificities of social structures, critical naturalists suggest that the study of social structures is unlikely to result in the uncovering of universal laws of causality, but rather only to succeed in exposing temporary causal tendencies.55

The key social scientific theory that operationalises the methodological insights provided by a critical naturalist philosophy of the social sciences is Bhaskar’s Transformative Model of Social Activity (TMSA).56 In The Possibility of Naturalism, Bhaskar argues that philosophical conceptions of society have tended to be divided along lines of being either broadly individualist or collectivist.57 As Bhaskar details, “methodological individualism is the doctrine

52 Ibid.
53 Ibid.
54 Ibid, 38.
55 Boraman, 96; Steinmetz 1998, 182.
56 Bhaskar’s TMSA is developed into a more detailed theory of social and individual being by Margaret Archer as the ‘Morphogenetic approach’. See M. Archer 1995, Realist Social Theory: the Morphogenetic Approach (Cambridge: Cambridge University Press).
that facts about societies, and social phenomena generally, are to be explained solely in terms of facts about individuals.” Bhaskar identifies the work of Popper, Watkins, and Weber most closely with this tradition. Respectively, a collectivist conception of society (which Bhaskar associates most closely with the work of sociologist Emile Durkheim) upholds that fundamentally “the ideas and practices of individuals are determined by society.” Stylised conceptions of these two polar views of society are presented in Figures 1.1 and 1.2 below. Through his TMSA, Bhaskar seeks to synthesise these broader conceptions of society.

**Figure 1.1) ‘Voluntarism’**

![Voluntarism Diagram]


---

58 Ibid, 27.
60 Bhaskar, 1998, 30; Boraman, 97.
61 Ibid.
Centrally, the critical realist TMSA acknowledges a limited degree of validity for each of the individualist and collectivist conceptions of society. Each conception is observed, for example, to derive “plausibility from the fact that it seems to touch on an important truth.” However, both conceptions are simultaneously observed to be fundamentally problematic. Methodological individualism, for instance, is seen to entail an excessive measure of voluntarism and social atomism that quite obviously understates the methodological importance of the material social conditions that routinely impede the free, independent action of individuals. Correspondingly, the methodological holism of the collectivist conception of society is seen to involve overt ‘reification’ or a simplistic socio-structural determinism that neglects the reality of human agency.

---

63 Boraman, 97.
Bhaskar’s synthesised TMSA seeks to avoid both the excessive voluntarism and the excessive reification of its predecessors. Following Marx, it does this by developing a unique relational conception of society.\textsuperscript{64} A relational conception of society constitutes an understanding of the social world as “essentially consisting in or depending upon [enduring and persistent] relations.”\textsuperscript{65} As Collier explains, according to the TMSA’s relational conception of society, “there have to be two distinct kinds of being: social institutions that pre-exist the agent and are independent of him or her, and an intentional agent whose action presupposes and makes use of those institutions but is not explained by them.”\textsuperscript{66} However, under the TMSA, individual agents and societies are simultaneously observed to be related in several key ways. First, society is considered to be “entirely the effect of human actions.”\textsuperscript{67} It effectively constitutes “an ensemble of structures, practices and conventions which individuals reproduce or transform, but which would not exist unless they did so.”\textsuperscript{68} Second, “every human action presupposes society with its relations and institutions as a condition of its possibility”; and third, “human intentional activity, in addition to producing (when successful) what is intended, reproduces [and/or transforms] society (usually unintentionally).”\textsuperscript{69} It (social reproduction and/transformation) is fundamentally “an achievement, a skilled accomplishment of active subjects, not a mechanical consequent of antecedent conditions.”\textsuperscript{70} A stylised representation of the TMSA as a conception of society is presented in Figure 1.3 below.

\textsuperscript{64} Bhaskar 1989, 73.
\textsuperscript{65} Ibid, 3. See also Bhaskar 1998, 28, 30.
\textsuperscript{66} Collier 2005, 333.
\textsuperscript{67} Ibid.
\textsuperscript{68} Bhaskar 1998, 36.
\textsuperscript{69} Collier 2005, 333-334. For an extended discussion see Bhaskar 1989, 3-4.
\textsuperscript{70} Bhaskar 1998, 36.
In this way, the TMSA effectively resolves "the division between society and the individual, and between structure and agency." \(^71\) It allows the possibility of avoiding both the simple reduction of individual agents to social effects characteristic of methodological holism, and the simple reduction of society to the activity of individual human agents that is characteristic of methodological individualism. \(^72\) Moreover, as a direct consequence of its stressing of what Bhaskar terms "material continuity", the TMSA is also capable of upholding a strong notion of social transformation.\(^73\) Not only do the actions of individual human agents serve to reproduce social structures and relations, the TMSA, in essence, also entails that the actions of these same discrete agents are ultimately capable of the fundamental transformation of the existing social structures and relations that underpin contemporary society. \(^74\) As Bhaskar

\(^71\) Boraman, 96.
\(^72\) Collier 2005, 334.
\(^73\) Bhaskar 1989, 37 (my emphasis).
\(^74\) Boraman, 99.
observes, neither of the previously discussed methodological stereotypes, nor Berger and Pullberg’s ‘dialectical’ conception of society, are genuinely capable of recognising and conceptualising this possibility.\textsuperscript{75}

As the adopted methodological approach, Bhaskar’s critical realism and the TMSA make a number of important contributions to this thesis. The first of these is an emphasis on the development of specifically historical explanations. Centrally, and in contrast to the competing holistic and individualist methodologies outlined previously, Bhaskar’s TMSA allows the possibility of examining both individual agents and social structures as causes when developing possible social scientific explanations. This aspect of Bhaskar’s ‘explanatory schemata’ is primarily a reflection of the TMSA’s cognisance of the ultimate complexity of social reality. “At any given moment, there is always a structured complex of intra- and interrelated entities: actors, actions, rules, resources, practices and social systems” operating in the social world and “any outcome is typically codetermined by the numerous parts of a complex.”\textsuperscript{76}

However, in addition to recognising their overarching complexity, the TMSA also recognises the previously discussed chief ‘epistemological limit’ placed on the naturalist conception of social science; that social systems are inherently open. As Patomaki observes, “firstly, the relationship between the causal complexes and those of its external conditions is typically not constant; and, secondly, change and qualitative variation in the objects possessing causal powers – including social actors – are ubiquitous.”\textsuperscript{77} As a consequence, in addition to emphasising the importance of considering both human agency and social structures when developing social scientific explanations, the adoption of


\textsuperscript{77} Ibid. For a detailed discussion see A. Sayer 1992, Method in Social Science: A Realist Approach (London; New York: Routledge). 118-38.
the TMSA also emphasises the importance of analysing causes in their historical context. This means, for example, that in order to produce an adequate account explaining the ‘re-emergence’ of global financial markets following the collapse of Bretton Woods in this thesis, I will be required to take into account several overlapping factors. I will have to consider not only the important role played by the particular imperial aspirations of the US state and capital (and to a lesser extent the supporting aspirations of the UK state and capital), but also how the historic re-emergence of global financial markets related to the onset of a major crisis of global capitalism and the coincidental rise and rapid geographic spread of global neoliberalism.78

The second important methodological contribution made by Bhaskar’s critical realism and the TMSA is an emphasis on the inherent ‘non-neutrality’ of explanations in social scientific enquiry. This emphasis on non-neutrality stems from the fact that, as previously shown, “social structure and human agency are existentially interdependent.”79 Social structure is considered to be “both [an] ever-present condition and continually reproduced outcome” of praxis (human activity), while human activity is upheld as being “both... (normally conscious) production, and (normally unconscious) reproduction of...society.”80 Such a view implicitly entails that social scientific endeavour is, by nature, normally conscious work undertaken by a human agent all the time mediated by underlying material social conditions. In other words, “social science always only happens in a context which is at once always understood, preconceptualised, and codetermined” by a complexity of both praxian and structural factors.81 It is fundamentally for this reason that the social scientific enquiries contained within this thesis are

79 Bhaskar 1989, 92.
80 Ibid.
81 Bhaskar 1986, 170.
Necessarily non-neutral; that they are intrinsically critical (both of beliefs and their objects) and self-critical; that accounts of social reality are not only value-impregnated but value-impregnating, not only practically-imbued but practically imbuing; and that in particular they both causally motivate and logically entail evaluative and practical judgments \textit{ceteris parabils}.\textsuperscript{82}

As Patomaki observes, ultimately, “the [methodological] point” of this notion of inherent ‘non-neutrality’ in social scientific explanations is to require the construction of “explanatory models more systematically and reflectively.”\textsuperscript{83} In practical terms, this means that the neopluralist theoretical framework developed in this thesis will act to mould the nature of the particular historical facts presented and discussed throughout this thesis. However, these same historical facts will, in-turn, also potentially feedback into the deployed theoretical framework in order to inform it, or even promote its alteration.\textsuperscript{84} So, for example, while neopluralism will guide this study in its endeavour to uncover the policy constraints imposed on the Fifth Labour and Fifth National Governments by highly mobile international financial capital, the same empirical evidence assembled to expose these major international financial constraints will simultaneously serve to expose previously unperceived gaps in the guiding neopluralist framework.

However, Patomaki also observes that as part of the process of constructing systematic and reflective explanations, “different possible...causal hypotheses” must be articulated, and that the related process of eliminating weaker hypotheses requires significant empirical work.\textsuperscript{85} This view is founded on the basic critical realist ‘RRRE’ “scheme of explanation in open systems” set out by Bhaskar in \textit{The Possibility of Naturalism}.\textsuperscript{86} The key features of this are outlined in Table 1.1 below.

\begin{table}[h]
\centering
\begin{tabular}{|c|c|c|}
\hline
Feature & Description & Reference \\
\hline
Impression & & \\
\hline
Information & & \\
\hline
Categorisation & & \\
\hline
Reduction & & \\
\hline
Specification & & \\
\hline

\end{tabular}
\end{table}

\textsuperscript{82} Ibid, 169.
\textsuperscript{83} Patomaki 2003, 210.
\textsuperscript{84} Boraman, 102.
\textsuperscript{85} Patomaki 2003, 210.
\textsuperscript{86} See Bhaskar 1998, 129.
Table 1.1) Bhaskar’s Four-Phase ‘RRRE’ Schema for Practical Explanation in Open Systems

<table>
<thead>
<tr>
<th>Resolution</th>
<th>The resolution of a complex event into its components (causal analysis).</th>
</tr>
</thead>
<tbody>
<tr>
<td>Redescription</td>
<td>The redescription of component causes in terms of idealisations, abstractions, and appropriate categories of social ontology.</td>
</tr>
<tr>
<td>Retrodiction</td>
<td>The retrodiction to possible (antecedent) causes of components via independently validated normic statements.</td>
</tr>
<tr>
<td>Elimination</td>
<td>The systematic interpretive empirical assessment of these hypotheses, together with the elimination of the weaker hypotheses.</td>
</tr>
</tbody>
</table>

Sources: Bhaskar 1998, 129; Patomaki 2003, 208.

As Patomaki notes, ultimately, both quantitative and qualitative empirical data can be employed for the purposes of the final elimination phase of explanation in open systems. “Quantitative data”, for example, “may be indispensable...in deriving research problems and estimating how common structures and tendencies are.”\(^87\) Ontologically, however, “given the contextual nature of efficient causes (= reasons for actions) – and the ubiquity of qualitative change and variation”, Patomaki argues that qualitative evidence must be primary.\(^88\) Fundamentally, it is “qualitative languages and methods [that] are needed to identify relevant structures and causal powers, and to show how and why objects possess these causal powers.”\(^89\) Consequently, in addition to constructing explanations more systematically and reflectively, the TMSA’s contribution of a notion of non-neutrality also entails that qualitative data will

---


serve as the dominant factor in determining the strength of prospective causal hypotheses in this thesis. So, for example, when developing my own account of the historical shift to neoliberalism in New Zealand alongside those that already exist, I will mainly rely on qualitative primary materials such as historical company reports, official government policy statements, and interviews with key actors involved in the process as my key sources of empirical data.

A further important methodological contribution made by Bhaskar’s TMSA is the lending of an ‘emancipatory impulse’ to the explanation developed in this thesis. As Bhaskar outlines in his work *Reclaiming Reality*, ‘emancipation’ is to be conceived here as:

Paradigmatically, a process of structural transformation – as a transformation *in* structures rather than a marginal adjustment of states of affairs and as a transformation *to* other (needed, wanted and empowering) structures rather than to a realm which magically escapes determination. Associated with this is a notion of freedom as consisting not merely in decreased restrictions, nor merely in these plus enhanced capacities under existing structures, but in emancipation from those unnecessary, undesired and oppressive (including exploitive) structures of power, domination and distorted need recognition, opportunity and communication.90

Underpinning the ‘emancipatory impulse’ lent to this thesis is Bhaskar’s contention that social science, in addition to possessing an obvious explanatory function, also has “a necessarily evaluative function, entailing critical value judgments.”91 This contention is based on the fact that critical evaluation is a vital precondition of producing sufficiently robust explanations of social institutions. As Sayer observes, “social science must be critical of its object. In order to be able to explain and understand social phenomena we have to evaluate them critically.”92 As Patomaki details, when a proposed “explanatory

90 Bhaskar 1989, 187.
91 Boraman, 102.
model can be extended to also explain [the competing account] T and its reproduction, both conditions for social criticism are fulfilled: the critical condition (‘T is an inferior account’) and the explanatory condition (‘T can be explained’).”\textsuperscript{93} Bhaskar argues that when both these explanatory and critical functions of social science have been fulfilled, and that it has been acknowledged that (due to the previously discussed inherent non-neutrality of social scientific explanations) “truth is a normative notion” in the social sciences, the possibility that explanatory social theory can be “intrinsically emancipatory” is implied.\textsuperscript{94}

Moreover, Bhaskar also argues that beyond the mere possibility of an ‘emancipatory impulse’, in some particular circumstances, critical social scientific explanation necessarily implies emancipation.\textsuperscript{95} In order to illustrate Bhaskar’s point, Collier, a prominent proponent of critical realism, provides several examples of ‘false belief.’ These include the classic neoliberal notion that ‘fecklessness’ causes unemployment and, drawing on Marx’s account of the wage form, the ideology that under the capitalist wage system, wages constitute payment for labour.\textsuperscript{96} In the latter case, Collier argues that the apparent prevalence of this belief within contemporary advanced capitalist societies can be explained by the fact that “not only does the institution of wage-labour cause false beliefs about itself, it also protects itself from the wrath of the workers by this illusion. To expose this, Collier continues, “is to criticise the wage system”, and, ultimately, also to instigate opposition to it.\textsuperscript{97} The essential contention is,

\textsuperscript{93} Patomaki 2003, 215.
\textsuperscript{95} Boraman, 93.
\textsuperscript{96} Collier upholds this as a false ideology because “what is actually paid for is labour-power” (1994, 172).
\textsuperscript{97} Ibid, 171-173 (original emphasis).
then, that once individuals are made aware of underlying structures of oppression, they will naturally pursue their transformation.\textsuperscript{98}

Fundamentally, by lending it an ‘emancipatory impulse’, the adoption of the critical realist TMSA “enables the making of inferences from explanation to criticism and transformations explicit” in this thesis.\textsuperscript{99} As Collier outlines, Bhaskar’s TMSA allows this thesis to generate a concrete emancipatory project “by showing there to be (a) a need, (b) some obstacle preventing its satisfaction, and (c) some means of removing this obstacle.”\textsuperscript{100} In specific terms, this means that this thesis seeks to develop an explanatory critique of New Zealand’s contemporary liberal democratic political system. It contends that, perhaps contrary to popular perception, substantive democracy is significantly (although not entirely) curtailed under current political economic conditions, and that integration into the US-dominated global financial nexus known as the Dollar-Wall Street Regime (DWSR) is a major factor contributing to this. Ultimately, it proposes that a fundamental alteration of the current arrangements governing international monetary relations that establishes a rigorous, collaborative Keynesian-style system of capital and exchange controls in support of financing real economic activity is the key means of removing this obstacle to substantive liberal democracy.

The final important contribution made by critical realism to this thesis is that it enables one to navigate the major intellectual rift between objectivism and subjectivism in social scientific methodology.\textsuperscript{101} On the basis of their transcendental realist philosophy of the natural sciences, for critical realists there can exist no objective universal truth beyond temporal bounds that can

\textsuperscript{98} Boraman, 103.
\textsuperscript{99} Patomaki 2003, 215.
\textsuperscript{100} Collier 1994, 183.
\textsuperscript{101} As Boraman observes (105), “numerous attempts” have been made to surmount this “polarity” between objectivism and subjectivism. See, in particular, P. Abrams 1980, “History, Sociology, Historical Sociology”, \textit{Past & Present}, 87, 3-16; R. Bernstein 1983, \textit{Beyond Objectivism and Relativism: Science, Hermeneutics and Praxis} (Oxford: Basil Blackwell).
assert the superiority of one explanation over a contender. Critical realism instead “entails the acceptance of...the principle of epistemic relativity, which states that all beliefs are socially produced, so that all knowledge is transient, and neither truth-values nor criteria of rationality exist outside historic time.”

As Bhaskar outlines, this subsequently entails the rejection of the epistemic absolutism of objectivist methodologies. However, this does not mean that critical realists support the adoption of an undifferentiated intellectual eclecticism either; critical realism also simultaneously rejects the subjectivist doctrine of judgmental relativism, which maintains that all beliefs are equally valid, in the sense that there can be no rational grounds for preferring one to another.”

Critical realists aver that, in terms of determining the salience of one explanation over another, theories can in-fact be “hierarchically ranked.” As Outhwaite argues, for example, “we can say a theory is better than another if it explains (under its descriptions) most of what the second theory explains (under its descriptions) plus some further things which are not explained by the second theory.” Consequently, when explaining the retention and extension of the neoliberal policy framework by the Fourth National Government during the period from 1990 to 1999 (Chapter Four), a review of the most potent explanatory accounts developed to date will first be undertaken. Only after this has been completed will an alternative explanation (acknowledging and integrating the most important aspects of the previous explanations) be posited. Similarly, when seeking to determine the extent to which the DWSR constrained the macroeconomic policy formulation of the Fifth Labour Government (FLG) during the period from 1999 to 2008 (Chapter Six), a section

---

105 Ibid, 3.
106 Outhwaite, 34 (original emphasis).
outlining the prevailing political context and its resulting constraints on the FLG will precede my own detailed explanation accounting for the role of the DWSR.

Thus, a critical realist methodology will be employed to apply the theoretical framework developed in this thesis. But which theoretical approach should be adopted to guide the following empirical and historical study? Determining this is the primary focus of the remainder of this chapter. Several main competing theoretical perspectives seek to explain the power dynamics operating in modern liberal democratic political systems. Classical pluralist approaches are probably the most commonly adopted in studies of New Zealand’s contemporary political economy.¹⁰⁷ Therefore, classical pluralism makes an appropriate point of departure for our discussion.

1.2) Classical Pluralism

Classical pluralism is a theoretical model of the state that conceptualises representative democracy as comprising “an ‘ideal type’ of democracy in which political equality is maximised.”\(^{108}\) It fundamentally upholds that citizens in contemporary liberal democracies are able to effectively exert influence over government or, in other words, that functional polyarchy prevails.\(^{109}\) Classical pluralist analyses of power relations within nation states emerged and coalesced into a relatively coherent school of thought during the 1950s and 1960s. The work of authors such as Dahl and Truman was particularly prominent and influential.\(^{110}\) The classical pluralist model of the state is now widely considered to constitute a relatively naïve conception of power relations within advanced capitalist societies. “Even the most sophisticated models of pluralism” are seen to be lacking sufficiently robust explanatory power in relation to public policy outcomes.\(^{111}\) Despite this, however, classical pluralism remains steadfast in its position as the dominant perspective pertaining to analyses of government decision-making in contemporary New Zealand.\(^{112}\) As Roper observes, “much writing on interest group influence on public policy in New Zealand continues to be doggedly committed to a broadly classical pluralist…orientation.”\(^{113}\) Consequently, the key features of classical pluralism will be outlined here. This will enable a critical assessment of whether or not it comprises a robust theoretical model capable of effectively guiding an analysis of the influence that international financial markets exert over government macroeconomic policy formulation in New Zealand.

---


\(^{112}\) Dunleavy and O’Leary, 23.

\(^{113}\) Roper 2006, 180.
According to the relatively unsophisticated version of classical pluralism that, historically, has tended to dominate studies of New Zealand politics, the state in capitalist society essentially “acts as a neutral arbiter of societal conflict.” 114 As Dunleavy and O’Leary elaborate, the state is regarded as a largely “passive vehicle through which inputs are processed. The state resembles a weathervane. It simply mirrors or responds to the balance of pressure group forces in civil society.” 115 It is important that the classical pluralist conception of state neutrality is properly understood. While they are often inaccurately characterised as upholding such a relatively crude conception of state neutrality, pluralists do not generally consider the state to constitute an essentially timeless, “mainly inert [recipient] of pressure from interest groups.” 116 Instead, the classical pluralist neutral state is responsive - both in terms of policy output and structure - to the pressures exerted on it. 117 Thus, as Smith observes, “the [‘neutral’] state for pluralists is in a Poulantzian sense the condensation of groups’ forces. It does not hold the ring but reflects the pressures on it.” 118

The essence of the classical pluralist theoretical model is consequently relatively straightforward. Centrally, the political process in contemporary liberal democracies is considered to involve the *demos* freely interacting with the state to express a variety of demands. 119 The state, erstwhile conceived as essentially comprising a collection of neutral institutions which are highly responsive to the myriad political pressures exerted on them, responds to this plurality of democratic influences via the formulation of public policy. 120 As Dunleavy and O’Leary observe, pluralists do not maintain that citizens have the

---

115 Dunleavy and O’Leary, 43.
117 Dunleavy and O’Leary, 43.
118 Smith 1990, 304.
120 Roper 1993, 148.
capacity to “directly control policy-making in polyarchies.”\textsuperscript{121} Such capacity is deemed to be effectively precluded by the size of modern nation-states.\textsuperscript{122} Instead, pluralists articulate four major channels of influence through which the citizen body exercises power over the state policy-making apparatus.\textsuperscript{123}

The primary channel through which citizens are deemed to exercise power in liberal democracies is the parliamentary system whereby the citizen body exercises ultimate discretionary power in the political sphere by periodically determining the formation of party-based governments.\textsuperscript{124} Largely “undeferential citizens” are seen to independently appraise the existing government’s performance and weigh it against alternative “personalities, parties, and policy packages.”\textsuperscript{125} Free elections are subsequently held at regular intervals through which the citizens select a preferred political leadership that is “temporarily entrusted with state power.”\textsuperscript{126} Between elections, pluralists maintain that a high level of party competition in parliament, combined with a strong inherent motivation to retain power, effectively constrains the governing party’s scope for autonomous action.\textsuperscript{127} As a result, governments in contemporary liberal democracies closely adhere to a programme of public policy that genuinely reflects the expressed preferences of the electorate.\textsuperscript{128}

The interest group system is also considered to be especially important. Indeed, as Smith observes, “most pluralists would ascribe a central role to pressure groups in the political process.”\textsuperscript{129} Pluralists conceive of the interest group system as consisting of a multitude of competing “semi-public or private groups” freely organised within civil society.\textsuperscript{130} The size, number, and

\textsuperscript{121} Dunleavy and O’Leary, 23.
\textsuperscript{122} Ibid.
\textsuperscript{123} Ibid, 23-41; Mulgan 1989, 39.
\textsuperscript{124} Ibid.
\textsuperscript{125} Dunleavy and O’Leary, 26.
\textsuperscript{126} Ibid.
\textsuperscript{127} Mulgan 1989, 39.
\textsuperscript{128} Dunleavy and O’Leary, 28.
\textsuperscript{129} Smith 1990, 302-303.
\textsuperscript{130} Mulgan 1989, 39.
sophistication of these groups are historically dynamic. Some of these groups are effectively permanent and extremely well resourced (such as business associations and non-governmental organisations (NGOs), while others are comparatively “ephemeral”, forming and dissolving in response to specific policy issues (anti-Iraq War protest groups, for example). However, as Mulgan observes, they all share a uniformity of purpose. “Their function is to articulate the interests which their members share on particular areas or questions of government policy, and to attempt to influence government in their direction.” Ultimately, citizens in contemporary liberal democracies are seen as exerting significant continuous influence over government via the interest group system. Thus, for pluralists, public policy is not only explained by the outcome of episodic elections and party competition in parliament, but also by the [government’s] steady appeasement of small groups.

It is crucial to observe that, for pluralists, the interest group system fundamentally operates as a “level playing field.” As encapsulated by Dunleavy and O’Leary, “the system is permeable, capable of being penetrated by any group which can build up its size, mobilise its members, and motivate them to express strong feelings.” Pluralists acknowledge that groups representing business interests generally occupy a “favoured position” in the interest group system. Superior resources deriving from their constituents position within the economy logically translates into more effective engagement with the state policy-making apparatus. Thus, despite the contrary claims of many of their critics, sophisticated pluralists do acknowledge an explicit link

---

131 Ibid.
132 Ibid.
133 Dunleavy and O’Leary, 32.
136 Dunleavy and O’Leary, 37.
137 Truman, 225.
138 Smith, 303-304.
between economic and political power.\textsuperscript{139} However, pluralists maintain that, in contemporary liberal democracies, the relative power of business is effectively curtailed by strong “countervailing” influences.\textsuperscript{140} For pluralists, powerful interest groups are usually (eventually) matched by rival groups representing competing interests. Where no such ‘counter-groups’ emerge, powerful countervailing influences are still considered to exist in the form of “potential groups.”\textsuperscript{141} As Smith elaborates, according to pluralists, “people have multiple membership of unorganised groups.”\textsuperscript{142} Fundamentally, these “are groups with shared interests but which do not actually become organised.”\textsuperscript{143} Due to their previously mentioned assumed inherent desire to achieve re-election, political leaders take account of the interests of both these organised and potential counter-groups largely to the same extent that they take account of the interests of powerful organised groups.\textsuperscript{144} Thus, for pluralists, powerful countervailing influences essentially function as a pro-democratic counterweight that offsets the significant practical advantages accruing to business interests, thereby ensuring overall balance in the interest group system.

The third major channel through which citizens exercise power in contemporary liberal democracies is comprised of the institutions of local government. Indeed, for pluralists, “legally autonomous sub-national governments are indispensable to polyarchy.”\textsuperscript{145} In broad terms, the means by which the institutions of local government allow citizens to influence government action are usually largely identical to those of the parliamentary channel. The key difference is ultimately one of geography. As Mulgan


\textsuperscript{140} Smith, 305.

\textsuperscript{141} Ibid.

\textsuperscript{142} Ibid.

\textsuperscript{143} Ibid.

\textsuperscript{144} J. Curran 2002, Media and Power (London: Routledge), 151-155; Smith, 305.

\textsuperscript{145} Dunleavy and O’Leary, 25.
elaborates, whereas the parliamentary system enables citizens to exercise
democratic power at a national level,

the various institutions of local government – general-purpose
bodies, such as city, borough and country councils, and special
purpose bodies, such as catchment boards, harbor boards and
electric power boards – allow members of each local community
to share in controlling their own activities.146

According to pluralists, the final major channel through which citizens
exert influence over government is the modern mass media. The institutions of
the private news media constitute “the chief watchdogs guarding the ‘public
interest’ against governments.” 147 For pluralists, professional
“journalists…pursue the ‘truth’ in a relatively disinterested manner.” 148
Through this process, the media uncovers, and subsequently relays to the demos,
“accurate and full information about politics.” 149 Thereby, a fully informed
citizen body is invested with the capacity to effectively scrutinise the conduct of
their elected leaders.150 This provides for extensive public oversight of the
government’s policy agenda. Thus, the modern mass media operates “as a
critical check upon the power of the…government of the day.”151 It ensures a
high level of electoral accountability, essentially precluding the possibility of a
government pursuing a policy agenda radically at odds with the preferences of
the citizen body.

As can probably already be surmised, the major channels of influence
delineated by pluralists are seen to be “closely [inter-]connected with one
another.”152 As Mulgan explains at length:

---
146 Mulgan 1989, 40.
147 Dunleavy and O’Leary, 25.
148 Ibid, 38.
149 Ibid.
150 Ibid.
151 Dunleavy and O’Leary, 37.
152 Mulgan 1989, 40.
The parliamentary and the interest group systems have the same focal point, the cabinet, those members of the ruling parliamentary party who are ministers in charge of government departments and who together form the most authoritative body in central government. Lower down there is also considerable interpenetration: interest groups try to influence the views of political parties and MPs as well as those of government departments, and MPs present the parties’ views to sectional interests. Similarly, the institutions of local government interact with the parliamentary system, through contact with political parties and local MPs. Local bodies are also active within the interest group system, and have their own national associations competing for government attention alongside other interest groups.¹⁵³

Therefore, for pluralists, the four major channels through which citizens exercise power in a classical pluralist model of the state are not sharply delineated. Instead, they operate in a complex, interdependent manner. Each core set of institutions complements the operation of another, thereby “ensuring that the different demands of different sections of the people are translated into political action.”¹⁵⁴

Thus, the classical pluralist model of the state can be characterised as a theoretical framework that maintains that citizens in contemporary liberal democracies exercise effective power over a ‘neutral’ state “which simply reflects the balance of forces…in society.”¹⁵⁵ The citizen body exercises this power through four distinct (but nevertheless inter-related) channels of influence - the parliamentary system; the interest group system; the institutions of local government; and the media – without one group or set of interests in society consistently dominating the process. Classical pluralism does cite a link between economic and political power and, thus, is somewhat more sophisticated than is commonly acknowledged by its critics. However, as will

¹⁵³ Ibid.
¹⁵⁴ Ibid.
be shown in the following sections of this chapter, significant weaknesses with the model persist. Fundamentally, classical pluralism fails to properly account for the observable dynamics of political and economic power in contemporary liberal democracies. Most notably, this includes the significant capacity of the state itself to function as an autonomous actor and the disproportionate influence that business is consistently able to exert over government policy-making.
1.3) The Critics of Classical Pluralism

This section exposits the central conceptual themes of the Marxist and Neo-Weberian paradigms and the critique they make of classical pluralism. At the same time, however, the discussion also involves an evaluation of the usefulness of these approaches for the analysis of the dynamics of power within the liberal democratic system. It is important to note from the outset the inherent diametrical opposition to which these perspectives are oriented. Callinicos, referring to Weber as the “Bourgeois Marx”, observes of the situation that “their political stances represent a dramatic opposition, Weber’s championship of the bourgeoisie...starkly confronting Marx’s socialist internationalism.” 156 Despite the intrinsic theoretical tension between these perspectives, however, both present robust opposition to the classical pluralist paradigm. As will be demonstrated, both Marxist and Neo-Weberian scholars present analyses that effectively counter the core principles of the classical pluralist model; that political power is fully and equally vested in the democratic polity.

Marxism

Marxist theories of the state are clearly differentiated from other theoretical perspectives.157 This is most notable because, as Callinicos states, the fundamental characteristic of Marxism is an “insistence on accounting for social inequalities and political struggles in terms of the master concepts of the forces and relations of production.” 158 Furthermore, Marxism goes beyond the mere outlining of a model of the state by also entailing praxis; a practical political

157 A number of different approaches exist within the broader Marxist tradition. Useful discussions of the key distinctions between these varied approaches are provided by Clarke and Jessop. See S. Clarke 1991 (ed.), The State Debate (London: MacMillan); B. Jessop 1990, State Theory: Putting Capitalist States in their Place (Cambridge: Polity Press). The specific approach outlined here is a contemporary classical Marxist approach to analysing the relationship between capitalist society and the state.
program reflecting the reality that the only way out of inevitable and enduring class-conflict is a “total transformation of the mode of production.” Marxists view modern advanced-capitalist societies as a complex system of interacting political, economic and social phenomena. This perception of society motivates the central “holistic” methodological approach of a Marxist analysis of politics; the relating of the distribution of political power to wider patterns of social and economic inequality. Marxism seeks to reveal the causal patterns of the dynamics of state-society relations and the complex nature of advanced capitalist society, and this must involve the consideration of multiple phenomena.

As alluded to above, pivotal to this perspective is what Marx himself referred to as the “relations of production.” These are considered to be the genesis of political struggle. More specifically, Marxists accord central importance to the “social relations of production”, which are cited as giving rise to the division of society into classes. Due to these social relations of production, a minority of the citizen body, the “bourgeoisie” or “capitalist” class, are able to control the means of economic production and use this control to force the “direct producers” that collectively make up the “proletariat” or “working class”, and, historically, a majority of the demos, to perform “surplus labour” for the generation of profit. As described by Marx, this relationship fundamentally involves the exploitation of workers. While nominally free agents, the structural arrangements of the capitalist system disguise the inherent inequalities that exist between capitalists and workers, especially because “capitalists and workers possess unequal ‘initial endowments’ of the

---

160 Callinicos 1984, 125.
161 Ibid, 125-126.
164 Callinicos 1984, 128; Mandel, 27.
major means of production.” The resulting underlying assumption of Marxism is that exploitation, that is the extraction of surplus labour, is at the centre of social and economic organisation in capitalist societies. As Marx succinctly encapsulates, “it is always the direct relationship of the owners of the conditions of production to the direct producers…which reveals…the…basis of the entire social structure, and with it…the corresponding specific form of the state.”

Such an analysis of capitalist society has significant implications for Marxist conceptions of both politics and the state. With exploitation at the centre of the model the political sphere will necessarily be shaped by the underlying relations of production. Consequently, Marxists see workers and capitalists as having distinct and antagonistic interests, particularly in the spheres of politics, production and the labour market. As Miliband observes, in each of these spheres, “the imperative necessity for the owners and controllers of capital to extract the largest possible amount of surplus value from the labour force comes into conflict with the attempts of workers to introduce reforms in the operation of capitalism” or even “its total transcendence.” In the sphere of industrial relations, for example, this is manifested through the tension over the issue of worker organisation. Capitalists want to maximise profits by minimising costs, including labour costs. In contrast, workers seek higher wages, improved conditions of employment and greater employment security, which can combine to increase labour costs and reduce profit rates. This tension ultimately results in conflicting class-based interests. Consequently Marxists generally conclude that what is good for business is often not good for workers, and exploitation can clearly be seen

---

165 Roper 2005b, 92.
166 Karl Marx, quoted in Callinicos 1984, 129.
167 Callinicos 1984, 129.
168 Miliband, 19.
169 Roper 2005b, 93.
170 Ibid.
to be the genesis of class struggle, the inevitable and fundamental dynamic of the Marxist conception of politics.¹⁷¹

Due to its position as the ultimate coercive institution in capitalist society, with the ability to guarantee a particular class’s domination through its monopoly of legitimate force, the state is a major focal point of Marxist analysis.¹⁷² Centrally, the underlying exploitation inherent in the nature of the free enterprise system is seen to generate significant advantages for business in the struggle for influence over the state.¹⁷³ This is primarily due to the state’s fiscal reliance on the process of capital accumulation, a process the state cannot directly control.¹⁷⁴ In essence, the state’s fiscal dependence on capital entails a requirement to ensure the ongoing viability of the profitable accumulation of capital.¹⁷⁵ Marxist analyses maintain that the result of this is that, over the long-term, the state will often be predominantly influenced by capitalist interests. Marxists emphasise, however, that the balance of political power between capitalists and workers must be understood as dynamic and historically contingent.¹⁷⁶ Therefore, the degree to which the state engages in modifying the process of accumulation in favour of business within its territory can at times be circumscribed.

In addition, Marxists also emphasise the inaccuracy of considering the capitalist class to be a homogenous actor in the public sphere.¹⁷⁷ As Cronin observes, fundamentally the capitalist class is not static, it is instead “constituted and reconstituted continually in the process of production and realisation of value. The flows of value in this process lead to a differentiation of

¹⁷¹ Ibid, 92-93.
¹⁷² Callinicos 1984, 130; Mandel, 26-27.
¹⁷³ Roper 2005b, 89.
¹⁷⁴ Ibid.
¹⁷⁷ Ibid, 165.
the capitalist class into distinct fractions.” 178 Industrial capital, commercial capital, and financial (or ‘bank’) capital form the principal fractions of the capitalist class. 179 These fractions emerge from “the process of circulation of capital.” 180 Further internal differentiation within the principal fractions of capital arises from “the profit-distribution process.” 181 The various fractions of capital are broadly “unified by a...hegemonic alliance among them.” 182 This entails that they share many core overarching values and political objectives including, most notably, the maintenance of and maximisation of the profitability of the capitalist system. 183 However, their internal fractional divisions also mean that different capitalists will have interests that cross-cut the class at the micro-level. 184 Furthermore, the balance of power between the fractions of the capitalist class is dynamic. For example, previously domestically-oriented industrial capital dominated the New Zealand economy. 185 More recently (and mirroring broader international developments), globally-oriented financial capital has become much more dominant within capital accumulation in New Zealand. 186 The key significance of such shifts in the intra-capital balance of power is that the specific content of the political pressures exerted on the state by business will be characterised by noticeable variances over time. Thus, as Roper observes, rather than being “simple, static

179 Roper 2006, 165; van der Pijl, 31.
180 Ibid.
181 Ibid, 3.
182 Cronin, 157.
183 Roper 2005b, 90. See also, van der Pijl, 7.
184 Ibid.
186 Kelsey 2015. The broader financialisation of global capitalism which is a prominent feature of the neoliberal era was clearly foreshadowed by Rudolf Hilferding in his classic (1910) work, Finance Capital. See R. Hilferding 1981, Finance Capital (London; Boston: Routledge and Kegan Paul).
or homogeneous”, for Marxists the political interests of the capitalist class in relation to the state are instead “complex, dynamic, and heterogeneous.” ¹⁸⁷

Furthermore, the structural constraints deriving from the state’s fiscal reliance on the taxation of incomes generated by private enterprise are considered to be historically dynamic in nature. Centrally, the structural pressures exerted on the state change according to the overall health of the economy. The capitalist system is naturally characterised by cyclical swings related to the underlying rate of investment. As a result, in the short-run, circumstances may arise where when the structural constraints imposed on the relative autonomy of the state will be considerably reduced in effect.¹⁸⁸ As will be argued later in the thesis, such situations appear to have arisen in New Zealand during the periods from 1994 and 1997, and also from 2002 to 2008. In-effect, at these junctures “the capitalist context chang[ed], allowing state managers more freedom of action in relation to capitalists.” ¹⁸⁹ However, Marxists also maintain that there is an inherent tendency within capitalism for the rate of profit to fall over time. As will be delineated in more detailed in the following chapter, this long-run tendency ultimately stems from the inherently competitive nature of the relationship between capitalists within the system.¹⁹⁰ For Marxists, the tendency for the rate of profit to fall within capitalism periodically generates economic crises.¹⁹¹ During such crisis periods (which can be prolonged) the structural pressures on the state to intervene in favour of business intensify considerably. Because it has the job of maintaining the overall conditions for capital accumulation, the state is implicitly pressed to mobilise ‘counteracting tendencies’ to restore system-wide profitability.¹⁹²

In summary, then, a central focus of the Marxist model is on the dynamic process of recurring class conflict. Antagonistic class-based interest groups struggle to obtain, retain or influence state power and in which the capitalist class’s dominant influence over government policy-making is open to challenge.\textsuperscript{195} Thus, unlike the classical pluralist perspectives, a Marxist analysis of contemporary liberal democratic societies acknowledges and makes an effective account of the observable inequalities of power between individuals and interest groups, as well as the structural power of corporations in advanced capitalist states.

The Neo-Weberian Model

In comparison to the Marxist perspective, the differentiating feature of a Neo-Weberian model is that it adopts a ‘state-centred’ approach to the analysis of the power dynamics operating within the liberal democratic state. That is, it is a perspective that conceives that the state “is an institutional ensemble or ‘structured field of action’ with a unique centrality in both national and international formations.”\textsuperscript{194} Centrally, exponents of a Neo-Weberian perspective are highly critical of the classical pluralist focus on the system of input politics and their ensuing neglect of the role of the government itself as an independent actor. As Skocpol outlines in the seminal Neo-Weberian volume \textit{Bringing the State Back In}, many classical pluralist studies are seen as lacking the theoretical flexibility to account for government leaders taking primary roles in particular public policy decisions.\textsuperscript{195} As a result, Neo-Weberians seek to demonstrate that the state possesses general operational autonomy. They posit that the state has significant structural and organisational capacity with which

\textsuperscript{193} Roper 2005b, 93.


to shape the formation of the claims of interest groups, as well as to implement public policy against the resistance of these groups.  

Driving the Neo-Weberian conception of the state is Max Weber’s observation that, the “state is a human community that (successfully) claims the monopoly of the legitimate use of physical force within a given territory.” This is interpreted as indicating that it is necessary for theorists to develop a conception of the state beyond “a mere arena in which social groups make demands and engage in political struggles.” The Neo-Weberian model consequently posits several sources of capacity from which the state derives its operational autonomy, but this element of legitimate coercive power forms the effective basis of each.

The first major source of state capacity is a state’s military power. This is also the most obvious manifestation of the state’s possession of a monopoly of legitimate coercion. Neo-Weberians consider military force to serve as an “an independent source of social power” that can be deployed to allow state elites to gain “collective and distributional power.” Ultimately, however, it also comprises a tool enabling state autonomy via the violent repression of society. Thus it can be seen that military power allows the state to pursue paths of action in open opposition to the resistance of politically weighty social forces and so, in-effect, it also forms the primary source of the state’s capacity for autonomous action.

The second major element upheld by Neo-Weberians as contributing significantly to the state’s autonomous operational capacity is the state’s linkage

---

198 Skocpol, 8.
200 Skocpol, 9.
into transnational structures. Particular stress is put on the importance of placing states within a theoretical framework that includes consideration of their position within systemic political, economic and military relations with other states.\textsuperscript{201} As Roper summarises this aspect of the Neo-Weberian model; “transnational linkages of individual states can greatly enhance the capacity of states to implement policy domestically because external support for policy change can strengthen the position of the state in relation to internal resistance.”\textsuperscript{202} Membership of international bodies and being signatory to bilateral or multi-lateral economic or military treaties are exemplary of such linkages.\textsuperscript{203} Neo-Weberians consider these to be capable of generating significant ideological and political-economic forces in support of government officials adopting public policy strategies formulated independently of domestic social and political interests.

In practical terms, however, it is through the bureaucracy that Neo-Weberians argue that the state is actually capable of exercising significant operational autonomy, including that which it derives from both its military power and its transnational linkages. Skocpol asserts that state autonomy is “instances in which unconstitutionally ruling officials attempt to use the state as a whole to direct...society and politics.”\textsuperscript{204} Thus we find that it is the public service or bureaucracy that forms the most comprehensive source of autonomous operational capacity of a state. It has at its disposal multitudes of highly trained career officials nominally insulated from both interest group and electoral pressures, and capable of formulating, implementing and evaluating public policy.\textsuperscript{205} These officials enjoy great organisational strength and often a

\textsuperscript{202} Roper, 2005a, 25.
\textsuperscript{203} Ibid.
\textsuperscript{204} Skocpol, 11.
\textsuperscript{205} Roper, 2005a 25; Skocpol, 9.
unified sense of ideological purpose, in addition to significant administrative resources of information that often includes awareness of foreign precedents and policy developments on which to emulate models of social policy.\textsuperscript{206}

Neo-Weberians conceive state actors (including collective agencies, individual bureaucrats and politicians) as being “collectively...self-interested maximisers, interested in maximising their power, prestige and wealth”, with their preferences noted as likely to diverge from those rooted in society because of the fact that they essentially derive their living from politics.\textsuperscript{207} As such it is argued that they can exercise significant agenda setting capacities, including the manipulation and, ultimately, the legislative or coercive restriction of the media.\textsuperscript{208} The work of Heclo is cited as particularly demonstrative of this atomistic nature of state actors and their ultimately autonomous operational capacity.\textsuperscript{209} Skocpol notes that through numerous studies, Heclo found that “civil service administrators in both Britain and Sweden have consistently made more important contributions to social policy development than either political parties or interest groups.”\textsuperscript{210}

The bureaucracy is maintained by the considerable revenue-raising capacity it derives from the state’s previously mentioned “collective and distributional power”, usually (but not strictly) manifested by the operation of a sophisticated taxation system.\textsuperscript{211} This can be conceptualised as legitimate financial coercion effectively lending the official agents of the state fiscal resources few societal interests could rival and, furthermore, offering state agents particular operational flexibility.

Through its possession of the expansive base of bureaucratic power outlined above, Neo-Weberians argue that the state has significant institutional

\textsuperscript{206} Skocpol, 10, 12.
\textsuperscript{208} Roper, 2005a, 25.
\textsuperscript{210} Skocpol, 11.
\textsuperscript{211} Jessop, 280; Roper, 2005a, 25.
and legislative capacity with which to engage and regulate the interest group system and the entire legal framework underpinning the economy and society.212 In essence the state is conceived “as a force which has an independent effect in social dynamics.”213 Bureaucratic power, then, provides the state with myriad sources of capacity for operational autonomy and, in practical terms for a liberal democratic state like New Zealand it forms the cornerstone of the state’s everyday ability to operate.

The Neo-Weberian analysis offers a particularly strong critique of the classical pluralist perspective. It accurately maps the key sources of a state’s capacity for operational autonomy and emphasises the requirement for a theoretical model of the state to include a comprehensive consideration of the state as an autonomous actor. There is a key weakness in the Neo-Weberian analysis for my purposes, however, and this is derived from their conception of historical causality.

Callinicos summarises the Neo-Weberian position on historical causality as that they “treat as, in general, indeterminate the relative contribution made by the three dimensions of power—economic, political-military and ideological.”214 The operative result of this is that when a sophisticated Neo-Weberian approach is adopted, it makes extensive acknowledgement of how state autonomy must always be viewed as historically contingent.215 Skocpol’s work provides an excellent case in point, noting that “state autonomy’ is not a fixed structural feature of any governmental system. It can come and go.”216 A similar tendency can also be observed in the work of Michael Mann; Callinicos remarks that “for Mann…the various power sources come and go...moving

---

213 Jessop, 280-81; Skocpol, 20-21.
216 Skocpol, 14.
according to the eddies of history, with none able to pretend to a permanent, structurally determined primacy over the others.”  

What becomes apparent after observing this Neo-Weberian conception of historical causality is that, in their rush to delineate the sources from which states are capable of deriving capacity for operational autonomy, they inadvertently exaggerate the functional degree of this autonomy. Specifically speaking, the problem is that, as Roper notes, “while most scholars acknowledge that the state possesses a degree of autonomy with respect to policy formulation and implementation, key questions arise with respect to the nature and extent of the societal limitations to state power.” Of particular concern for my purposes, is the Neo-Weberian treatment of structural power; the cornerstone of both Marxist and neopluralist analyses of the liberal democratic state.

The Neo-Weberian conception of historical causation and resulting uncompromising commitment to the historical contingency of power leads them to an inherent rejection of the structural sources of power. For example, while according to Marxian analyses the “relations of domination...spring from the requirements of class exploitation, and in particular the necessity of ensuring that surplus labour is regularly extracted from the direct producers”, Neo-Weberians, comparatively, insist that “relations of domination are omnipresent and irreducibly multiple.” Thus, as both Jessop and Wickham have observed, Neo-Weberians effectively gloss over giving any in-depth consideration to the implications of the social relations of production and the extractive process, consequently failing to account for the material base of the

---

217 Callinicos, 1995, 112.
218 For example, see M. Mann 2003, “Has Globalization Ended the Rise and Rise of the Nation-State?” in D. Held and A. McGrew (eds.), The Global Transformations Reader: An Introduction to the Globalization Debate (Cambridge: Polity Press), 135-146. Mann makes incisive observations regarding the changing, but nevertheless central, role of the nation-state in the global political arena, however in doing so he also seriously understates the significant and expanding global power of private financial interests.
219 Roper 2005a, 25.
220 Callinicos 1995, 111-112.
domination of workers. \textsuperscript{221} In order to illustrate the underlying historical contingency they see as inherent to the political system, Neo-Weberians focus on showing how state autonomy can be independent of social sources of power. But, as Block observes, by doing this it appears that Neo-Weberians are effectively claiming “that state-centred variables are more important than society-centered variables in explaining particular historic outcomes.” \textsuperscript{222} Subsequently, the model can be seen to give insufficient attribution of causality to society-based sources of power.

Furthermore, steadfast commitment to their conception of historical causality effectively renders Neo-Weberian analyses impervious to empirical challenge, particularly from ‘society-centred’ theoretical perspectives. This point is best illustrated by comparing competing interpretations of the same power relations within a specific timeframe. The example I will employ is that between the New Zealand Business Roundtable (NZBR) and the Fifth Labour Government (FLG) in the sphere of taxation policy during the period from 1999 to 2006. Here the state implemented many policy prescriptions in direct opposition to the preferences of big business, represented by the NZBR.\textsuperscript{223} A Neo-Weberian would interpret this as a demonstration of state autonomy. In contrast, a neopluralist, for example, would posit the central role of other society-based forces in enabling the state’s resistance against the influence of capital interests.\textsuperscript{224} Neo-Weberians could accept that such factors were the most important during this restricted time-frame, but would simultaneously maintain that the state retained ultimate autonomy. The problem is, then, that a Neo-Weberian analysis can reduce the causal importance of the state to a

\textsuperscript{221} C. Wickham 1988, “Historical Materialism, Historical Sociology”, \textit{New Left Review}, No. 171, 77; Jessop, 284.
\textsuperscript{224} Ibid.
wraith-like parody of real autonomy, yet maintain its causal centrality. Such a situation is completely counter-intuitive to the basic denotation of “autonomy.” Clearly in such a context there is little value in maintaining the causal centrality of the state, above all because it serves only to divert attention away from the forces actually driving the power dynamics within a political economy, the economic forces emphasised by Marxists and neoplasuralists being a prime example.

As indicated previously, this thesis aims to explain why financial capital is capable of exerting disproportionate influence over the New Zealand state and seeks to do this by highlighting a network of society-based forces as enabling it. The Neo-Weberian principle of historical causality therefore renders the perspective incompatible with the framework of the power dynamics of the liberal democratic state being developed in this thesis. While state theorists should acknowledge that the state possesses some operational autonomy, due to the significant emphasis placed on a high degree of historical contingency, Neo-Weberianism ultimately exaggerates the degree of this state autonomy and overlooks the role of society-based actors in the determination of specific public policy decisions.

Both the Marxist and Neo-Weberian theoretical perspectives develop particularly strong arguments against the relatively simplistic classical pluralist model of the state. Although each differs markedly from the other, both these analyses poignantly critique the classical pluralist model; Marxism reveals the significant structural power that capital interests possess due to the underlying nature of the capitalist economic system, and Neo-Weberians conceptualise the state’s capacity to be an autonomous actor. In addition, however, each of these perspectives has been shown to have drawbacks in relation to the theoretical framework that this thesis is seeking to develop. The Neo-Weberian position

regarding historical causality renders the perspective fundamentally incongruous with a ‘society-centred’ theoretical framework that upholds the existence of a complex system of structural constraints on the operational autonomy of the state, such as this thesis develops. Comparatively, the Marxist perspective is rejected primarily on the grounds of its principle of *praxis*; I am unconvinced of the practicality of their ultimate solution to the problems of the capitalist system. As is demonstrated below, a neopluralist model can incorporate the strengths and weaknesses of both these perspectives and consequently presents a high degree of theoretical flexibility, a valuable attribute for the empirical analyses undertaken in the latter portions of this thesis.
1.4) Neopluralism

Neopluralism largely consists of the work of liberal scholars reacting to well-founded critiques of classical pluralism’s inability to account for the real dynamics of power in the modern liberal democratic state. Although a comprehensive account is not possible here, core assumptions and principles can be identified to illustrate the general characteristics of a neopluralist analysis. Centrally, neopluralism seeks to describe, in a theoretically coherent manner, modern social organisation “in ways which are empirically realistic,” with a focus on the operations of business and the modern extended state.

A neopluralist methodology has several pivotal features and fundamentally differs from classical pluralist, Marxist and Neo-Weberian methodologies respectively. First, it rejects the classical pluralist’s atomistic level of analysis. Instead they adopt a Marxian macro-level approach and emphasise the importance of analysing the overarching issues of state-society relations, particularly those resulting from the operation of capitalism. Although it retains liberal democratic values, neopluralism recognises a situation of business privilege and is thus pessimistic about the ability of contemporary democracies to deliver an equitable distribution of political power.

Second, neopluralists observe that the structure of modern capitalist economies have shifted away from manufacturing towards service and information delivery. This fundamental shift is seen to have led to a relative decline in citizens identifying themselves according to class distinctions. Thus neopluralists reject Marxist class reductionism as anachronistic (although sophisticated neopluralists should acknowledge the potential for class to be an

---

226 Dunleavy O’Leary, 271.
227 Ibid, 284, 272.
228 Ibid, 285.
229 Ibid, 284; Smith, 316.
influential factor in input politics). Further, some neopluralists also suggest that Marxist class reductionism leads them to focus too much on class-based struggle. Thus, they perhaps ignore the potential for the mobilisation of interest groups within civil society independent of economic interests and, further, for such groups to have significant power in relation to the state or big business. Consequently, contrasting with Marxism, neopluralism also maintains the superiority of the current system of politico-economic organisation, seeking its reform rather than its fundamental transformation. The difference between Marxism and neopluralism should not be over-stated, however, for as noted by Mulgan, we can expect to observe a degree of convergence among “self-critical and empirically minded” scholars analysing the same complex political processes. This point is neatly expressed through their shared macro-level focus; a neopluralist methodology also includes a preference for multi-causal explanations to account for the complexity of power relations in contemporary liberal democracies.

Lastly, as has been indicated previously, neopluralism (like Marxism) rejects the Neo-Weberian state-centred approach to explaining political phenomena. It only acknowledges a limited (although ultimately dynamic) degree of state autonomy.

This reading of the classical pluralist, Marxist, and Neo-Weberian traditions provides the analytical foundation of two key insights that form the core of the neopluralist perspective; the state’s limited power and the privileged position of business. First, in stark contrast to classical pluralism, representative institutions are seen to be of limited effectiveness as controls on the formulation

230 Ibid, 286.
231 Dunleavy and O’Leary, 284.
233 Ibid, 287.
of public policy.\textsuperscript{235} Whereas classical pluralism develops a framework built around the role of interest groups and free and fair elections in influencing the state, neopluralists see the nature of contemporary governmental institutions as essentially pre-empting democratic controls. They observe the development of an “extended state” which has restricted the responsiveness of the state to legitimate democratic inputs.\textsuperscript{236} State power and control has become concentrated in the hands of actors who are not uniformly accountable to democratically elected representatives, such as officials in an operationally independent central bank. This leads neopluralists to acknowledge Neo-Weberian input into state theory and to conceive of the state as an institutional body of heterogeneous interests in regard to political power, consisting of a multiplicity of intra-governmental agencies and officials capable of enacting limited self-interested and significantly autonomous agendas.\textsuperscript{237}

Second, neopluralism also posits an alternate view of the interest group system that forms the heart of input politics. It notes that, in general, compared to other societal groups, business interests can deploy far superior resources to enhance their influence over society and the state. As Roper observes, the economic power of business enables it to:

(i) fund advertising campaigns to improve the public image of business; (ii) maintain well resourced associations to both lobby government and generate public support for the adoption and implementation of desired policies; (iii) extensively fund…major political parties through large corporate donations; (iv) offer substantial inducements (principally in the form of future career advancement in the private sector) to state sector policy analysts to adopt, advocate, and implement policies desired by business interests; (v) fund academic policy research and the publication of books with a pro-business ideological orientation; and (vi) use its ownership of radio stations, television, and newspapers to maintain a general pro-business bias in the media.

\textsuperscript{235} Dunleavy and O’Leary, 288.
\textsuperscript{236} Ibid.
\textsuperscript{237} Mulgan 1993, 131.
Although various classical pluralist ‘countervailing influences’ are acknowledged as capable of potentially offsetting this, these influences are considered to be historically contingent and insufficient to prevent business interests dominating input politics most of the time.

Beyond this consideration of the overt power wielded by business, neopluralism adopts the Marxian perspective that business interests also possess much more important latent and generally unobservable political power. Lindblom’s (1977) work *Politics and Markets* is a seminal neopluralist text in this regard, positing that in the sphere of public policy formulation, market-oriented liberal democracies uphold a system inherently biased in favour of business interests. Lindblom offered two observations, in particular, which are fundamental to neopluralist conceptions of business power.

First, Lindblom noted that business possesses significant “discretionary power”, a situation described as “the business executive as public official in the market system.” 238 This is the recognition that business owners or their appointed executive officers have the power to make decisions over the allocation of resources and the organisation of production processes. Such decisions, although relating specifically to their own business, simultaneously have serious implications for public policy. They directly affect levels of employment and economic growth, both major issues of political debate and of central importance to the welfare of the broader society. Essentially neopluralists see this as entailing that, in modern liberal democracies, significant power over issues of fundamental social and economic importance is actually vested in the hands of individuals external to the democratic process. 239

A centrally important manifestation of this discretionary power is the fiscal dependence of the state on the taxation of incomes generated in the process of

---

239 Ibid, 172.
capital accumulation. Effectively, this forms a structural constraint on state neutrality by forcing policy-making officials to undertake an anticipatory consideration of the interests of business. Further, as this thesis posits later on, specifically in the context of New Zealand, this process has been significantly enhanced by the liberalisation of global financial markets and the consequent increase in the global orientation of capital interests; the government, for example, needs to provide attractive conditions for foreign investment or face the potential risk of reduced investment or capital flight.240

Second, Lindblom observed the phenomenon of “circularity.”241 This essentially entails that corporate interests are able to effectively establish the parameters of discourse in the public sphere. No homogenous capitalist conspiracy-type hierarchical agenda is suggested by this, simply that business interests can effectively prevent questions of alternative modes of production from being placed on the political agenda. The mass media is seen by many scholars of the political economy of the media as playing a key role in the maintenance of this corporate capitalist ideological hegemony, but Lindblom also identifies business domination of the interest group system, and governmental deference as enabling this.242 It should be noted that Lindblom’s identification of circularity is entirely consistent with the idea that, similar to the state, capital too consists of a diverse body of interests. A number of pivotal values generally underpin their unity, however, and it is these that circularity operates to maintain.

Ultimately, then, as these key observations show, business interests are inherently advantaged politically by the structure of the capitalist system. Business possesses significant unobservable power that goes beyond the overt

---

241 Dunleavy and O’Leavy, 294.
influence business is capable of exerting due to its economic dominance. Because of this privileged nature of business power, but also through the operation of the modern ‘extended’ state, neopluralists conceptualise state-society relations, as constituting a “Deformed Polyarchy”, the central aspect of which is termed the “dual polity.” In essence this means that contemporary liberal democratic societies are characterised by a duality of political power in which the state (although necessarily possessing some capacity for operational autonomy) is partly controlled by the classical pluralist conceptions of electoral competition and the interest group system, but to a significant degree the state simultaneously responds to both the overt and latent power of business.

Thus, as we have seen, neopluralism fundamentally differs from each of the classical pluralist, Marxist and Neo-Weberian perspectives. It notes that business has significant power based on the nature of the capitalist system, but still emphasises the diversity of interests in modern societies. It acknowledges the importance of class but does not reduce all conflicts to this basis. It supports a limited degree of state autonomy but does not consider this to be outside the bounds of the structural power of either economic or societal interests. Neopluralism is instead concerned with expressing the complexity and chronologically unique nature of modern society and analysing overarching questions relating to state-society relations.

---

243 Dunleavy and O'Leary, 297.
Conclusion

Thus, in contrast to classical pluralism and the Neo-Weberian tradition, both the neopluralist and Marxist paradigms offer much more sophisticated accounts of the complex power relations that exist between citizens, business and the state in modern liberal democratic societies. This study will adopt a sophisticated neopluralist approach as it can be seen to provide a suitable theoretical framework on which to base an analysis of the implications of financial market liberalisation for the public macroeconomic policy formulation of the Fourth National Government from 1994 to 1999, the Fifth Labour Government (FLG) from 1999 to 2008, and the Fifth National Government (FNG) from 2008 to 2011. This does not entail the outright rejection of Marxism, but instead maintains a degree of skepticism in regards to the case for the revolutionary transformation of the capitalist system.

According to the sophisticated and critical neopluralist theoretical model developed in this thesis (and as will also be shown empirically in this thesis), business possesses significant privilege in the political systems of contemporary liberal democracies. Fundamentally, despite the existence of myriad countervailing electoral and societal influences, business interests are generally able to exert disproportionate influence over government’s formulation of public policy most of the time. The privileged position enjoyed by business in contemporary liberal democracies is due to several key factors. First, business possesses considerable overt economic power. Principally, this means that, compared to competing society-based interests, business is generally able to more effectively engage in the interest group system and thereby exert extensive influence over society and the state. Second, in addition to its overt economic power, business also possesses significant structural economic power. Due to the state’s ultimate fiscal reliance on incomes generated by business activity under a market-driven economy, state-society power relations are inherently biased in favour of business. The state generally faces considerable
ongoing latent pressure to formulate public policy in the interests of business in order to ensure ongoing economic viability. Third, business possesses significant discretionary power. This derives from the direct control that businesses often have over the specific means of implementing key aspects of public policy. The key significance of discretionary power is that it serves to skew state policy making in favour of business. This is due to an effective requirement for government officials to anticipate potential business responses to public policy initiatives and adjust them accordingly. The final key factor contributing to the political privilege enjoyed by business is the phenomenon of circularity. Circularity results from the ability of business to exercise a significant degree of control over the broad parameters of political discourse. Fundamentally, it serves to maintain an overarching pro-capital ideological hegemony within contemporary liberal democracies, thereby helping to preserve the privileged position of business.

The business community is not, however, an entirely homogenous actor within contemporary liberal democratic political systems. Instead, in accordance with Marxian analyses, business is internally differentiated, cross-cut by various fractional divisions. Moreover, the balance of power between the various fractional groupings within the business community is historically dynamic. Consequently, while the business community generally shares wide ranging political interests and objectives within contemporary liberal democratic political systems, groups within business also often possess noticeably divergent views on particular issues of public policy. In addition, the specific policy preferences conveyed to the state by business interests varies over time.

Furthermore, the state retains a limited degree of autonomy. As outlined previously, business possesses major political advantages in contemporary liberal democratic state. Thus, the state is often predominantly influenced by business interests. Business-dominated societal influences, however, are not the
sole driver of state action. Actors located within the state apparatus, including both elected representatives and unelected bureaucrats and officials, also often pursue their own discrete political agendas independent of the electorate and of business (although usually only within the bounds of the constraints imposed by business). Broadly speaking, governmental actors comprise an ensemble of myriad competing interests, which prominently feature variances in power distribution, and which are ultimately capable of simultaneously pursuing widely divergent political agendas within the state itself.

The power of business is also historically contingent. While business indeed enjoys a “structurally determined primacy” within contemporary liberal democratic systems, its functional ability to exert effective influence over the state varies over time. The apparent political dominance of business interests is not, fundamentally, a fixed, inevitable feature of liberal democratic systems. Instead, the specific degree to which business is able to exert influence over the state (and, conversely, the degree to which the state can operate autonomously and respond to other societal influences) is ultimately dynamic. It reflects both the specific prevailing balance of societal power within the nation-state at a particular point in time, as well as the underlying strength of the economy.

Most attempts at articulating theoretical frameworks of the modern liberal democratic state have tended to focus on societal, economic, and state-based forces within a relatively restricted national context. This has been particularly the case for the study of New Zealand’s political economy. Much work has not taken ample account of the important role played by external forces in determining public policy outcomes. Consequently, integrating some of the key theoretical insights of critical international political economy, according to the sophisticated neopluralist theoretical model developed in this

---

244 It is important to note that the sophisticated neopluralist theoretical model developed in this thesis maintains that the state remains accountable to various countervailing influences (most prominently democratic electoral pressures), but not to the significant extent assumed by classical pluralists.

245 Callinicos 1995, 112.
thesis, major international business interests also exert considerable influence within New Zealand’s liberal democratic political system. In particular, as this thesis will subsequently demonstrate empirically, international private financial interests impose considerable structural constraints on the state in New Zealand.

A critical realist methodology is used to apply the sophisticated neopluralist theoretical framework developed in this thesis. Comprising a derivative of Bhaskar’s transcendental realist philosophy of the natural sciences, critical realism forms an alternative social scientific methodology to the naturalist and anti-naturalist hermeneutical traditions that, together, have tended to dominate the philosophy of the social sciences. Critical realism prominently repudiates the crude methodological individualism characteristic of naturalist methods, which effectively reduces social scientific enquiry to an examination of the activity of individual human agents isolated from their discrete historical contexts. At the same time, critical realism rejects the methodological holism that is characteristic of the hermeneutical tradition, which over-emphasises the causal significance of broad structural factors in determining historical outcomes, and also critically understates the importance of individual agents.

Operationalised by Bhaskar’s synthesised TMSA, a critical realist methodology centrally entails that both the activities of individual agents and the influences deriving from broader social structures will be examined in their discrete historical contexts as this thesis progressively develops a detailed explanation of the historic shift to, and subsequent retention and entrenchment of neoliberalism in New Zealand. Due to its adherence to the notion of the inherent non-neutrality of social scientific enquiry, deployment of a critical realist methodology also entails that the construction of a robust explanation of New Zealand’s neoliberalisation will require extensive use of qualitative data. Due to its adherence to the notion of epistemic relativity, meanwhile, a critical realist methodology additionally entails that in order to produce this robust
explanation of New Zealand’s neoliberalisation, the strongest extant social scientific explanations must first be considered and assessed.
Globalisation, the Dollar-Wall Street Regime, and Global Neoliberalism

If on the way to becoming “big time,” consortium banks promote the linking of national and international money and capital markets, and dampen the impact of nationalism and political ideologies on the expansion of world trade and commerce, then they will richly deserve their success.


Introduction

The previous chapter set out a neoplasrlist account of societal influences on the decision-making and policy-making of the liberal democratic state. In doing so it emphasised the importance of investigating the influence of global forces (especially those in the economic sphere) within New Zealand’s political system. Similarly, Roper has argued that extensive research is required that focuses on the political impact of globalisation in New Zealand. Moreover, as noted in the introduction, he points out that one of the most important dimensions of globalisation is that which encompasses “the New Zealand financial system and its relationship to shifting patterns of global finance, foreign investment, and the size of public and private offshore debt.” Indeed, it is important to observe that financial deregulation involving “synergistic”

---

2 Roper 2005a, 30.
3 Ibid, 29.
interactions with “technological change” and an “information revolution” constitutes one of the most important dynamics of contemporary globalisation.\(^4\)

Exploration and critical evaluation of the impact of financial globalisation is thus, quite clearly, of the utmost importance to the proper understanding of New Zealand’s contemporary political economy.

Contemporary financial globalisation has taken place under the auspices of what will be referred to here as the Dollar-Wall Street Regime (DWSR).\(^5\) Consequently, the focus of this chapter will be on providing a comprehensive account of this centrally important financial structure. The chapter describes the key features and functions of the DWSR, and also explains how and why it became established as the overarching structure governing international financial relations. Addressing these latter issues involves, first, a brief discussion of the long post-war economic expansion and its relationship to the collapse of the so-called Bretton Woods System (BWS). Subsequently, the global rise and spread of neoliberalism will be discussed and some of the key changes that have helped cement the DWSR in place are delineated.

Proper understanding of the DWSR and its key features will ultimately enable an effective analysis of the power and political influence that private internationally-mobile financial capital is capable of exerting over New Zealand due to financial globalisation. However, as Roper notes, “any assessment of the impact of global forces on New Zealand society and politics necessarily must clarify and consider what globalisation is.”\(^6\) Therefore, before the core issues relating to the DWSR are addressed, a brief account will be provided of the major underlying facets of the globalisation process and, more specifically, the extent to which it is generated by capitalism.

---


\(^6\) Roper 2005a, 24.
2.1) **Capitalism and Globalisation**

Because it is ground dealt with extensively elsewhere, it is outside of the scope of this study to deal with the broad range of issues encompassed in the so-called “globalisation debate.” Instead, as indicated by the section title, here the discussion is largely restricted to outlining the underlying relationship between the global capitalist economic system and the process of globalisation. As Roper observes, in order to understand the relationship between capitalism and globalisation it is necessary to engage with the sophisticated critical analysis of capitalism developed by the Marxist tradition. This effectively demonstrates that the relationship between capitalism and globalisation is fundamentally rooted in the operation of what are termed the “laws of motion” of the capitalist mode of production.

According to Marx, the capitalist system has two central features, each corresponding to the two sets of relationships that underpin the workings of the capitalist system. The first of these, set out in Marx’s key political-economic work, *Capital*, is the *exploitation of labour-power* (simultaneously demonstrated to be the only commodity input to the production process that, on a system-wide basis, adds new value from the beginning to the end of the production cycle). The second key feature, set out in another of Marx’s key political-economic works, the *The Communist Manifesto*, is the *competitive accumulation of capital*. It is the nature of the latter ‘horizontal’ relationship between capitalists that is of particular importance here.

Marx argues that “capitalism is sufficiently competitive” for each individual capitalist to be under constant pressure to reduce their costs of

---

8 Roper 2005a, 26.
9 Ibid, 27.
production in order to either maintain or expand their market share. In practical terms this refers to a sustained pressure to reduce labour costs (thereby increasing the underlying rate of exploitation) whilst simultaneously endeavouring to increase market share through market leading innovation. In this way, as Callinicos points out, Marx effectively presents us with a “structural” theory of capital accumulation; the competitive pressure of their rivals compels capitalists to improve their productivity and productive capacity via the reinvestment of profits. It is this process that constitutes the “accumulation of capital.”

Conceiving of capitalism as a system of competitive accumulation in this manner enables us to reveal Marx’s underlying “laws of motion” of the capitalist system; the tendency of the average rate of profit to fall, leading to economic crisis and, ultimately, also globalisation. Centrally, for a capitalist firm, improving productivity (and thus profit) depends on increasing productive capital investment. However, when the profit-seeking behaviour of the individual capitalist is applied generally across the breadth of a market, a decline in the overall average rate of profit inevitably ensues. Such activity results in what Marx terms an increase in the “organic composition of capital” or, in other words, an increase in the ratio of constant to variable capital (the principle element of the latter being human labour). Because socially-necessary about time is the ultimate source of surplus value, unless the capitalist simultaneously increases the underlying rate of exploitation in the production process, the ultimate result of the individual capitalist’s endeavours to improve productivity is to require a relatively corpulent concentration of capital to

---

15 Ibid.
operate at a similar level of profitability.\textsuperscript{16} Furthermore, as Mandel observes, when it is extended even further, to encompass the economic system as a whole, the intra-capital competitive relationship in-built into the capitalist system ultimately becomes responsible for an inherent systemic “tendency of the rate of profit to fall.”\textsuperscript{17} “The inner contradictions of the capitalist mode of production come into their own and inexorably lead to...declines in the rate of profit.”\textsuperscript{18}

However, while a tendency towards a falling rate of profit pervades the capitalist system, it is important to note that this tendency can be temporarily offset by the effects of counter-tendencies. These counter-tendencies are often concealed due to their close enmeshment within the day-to-day operation of capitalism and can take a number of forms.\textsuperscript{19} As implied earlier, perhaps the most important counter-tendency to the falling rate of profit takes the form of an increase in the underlying rate of exploitation. If this accompanies further productive investment, additional surplus value is generated for capitalists that can effectively serve to offset some of the effects of a rising ratio of constant to variable capital – the key factor underpinning the tendency for the rate of profit to fall over time. As Panitch and Gindin observe, the tendency towards a falling rate of profit can also be offset by such things as “the development of new technologies and commodities, the emergence of new markets, international expansion, and innovations [and expansions] in credit provision.”\textsuperscript{20} Furthermore, state involvement in the economy can serve to delay a fall in the rate of profit which, as will be discussed in more detail in Section 2.3, is a factor that helps to explain the length of the long post Second World War economic expansion.

\textsuperscript{16} Ibid.
\textsuperscript{17} E. Mandel 1995, \textit{Long Waves of Capitalist Development} (2d ed.) (London: Verso), 7.
\textsuperscript{18} Ibid, 7, 23.
\textsuperscript{20} Ibid.
The long-term tendency of the rate of profit to fall periodically generates serious economic crises within capitalist systems. As Harvey observes:

The historical geography of capitalism is littered with examples of such overaccumulation crises, some local and short-lived (such as the crash of the Swedish banking system in 1992), others on a somewhat larger scale (the long-standing depression that has afflicted the Japanese economy since about 1990), and at times system wide and, latterly, global (as in 1848, 1929, 1973, and 2008).

Fundamentally, the historical propensity of falling capitalist profit rates over the long-term to result in crisis derives from the underlying relationship between profitability, investment, and output growth. Declining profitability progressively undermines incentives for the reinvestment of excess capital. This eventually results in a major blockage in the necessary “circulation of capital” required under capitalism. As Harvey delineates, “growth then stops and there appears to be an excess or overaccumulation of capital relative to the opportunities to use that capital profitably.”

It is from this systemic tendency towards crisis that globalisation stems. As discussed at length by Harman (who draws extensively on the work of Lenin and Bukharin), the systemic economic crises of the capitalist system serve to accelerate a trend of increasing concentration and centralisation of capital ownership. This ultimately spreads beyond national borders and into the

---

22 Ibid, 45-46.
24 Harvey 2010, 45.
25 Ibid.
26 Concentration here refers to the concentration of capital in increasingly large units (factories, for example). Respectively, centralisation refers to the growth of assets held by particular firms and corporations.
international arena.\(^{27}\) Under conditions characterised by a crisis of profitability, the intense market competition being experienced by capitalists results in a major upswing in takeover and merger activities amongst capitalist firms. Alongside this capitalists increasingly endeavour to seize and maintain more profitable production locations, new markets, and sources of raw materials.\(^ {28}\) Thus, we can consider the process known as ‘globalisation’ to be an expression of the micro-level capitalist ‘laws of motion’ at a macro-level; that is, in the arena of international economic relations. Indeed, as Bukharin observes, the imperialistic economic annexation that characterises contemporary globalisation can be considered “only a case of the general application of the general capitalist tendency towards centralisation of capital.”\(^ {29}\)

Although globalisation is popularly conceived as constituting a contemporary cultural-geographic phenomenon, it is apparent that ‘globalisation’ is in-fact an organic constituent dynamic of capitalism. Indeed, the long run tendency for “the geographic expansion of capitalism to encompass the globe” was observed by Marx as early as 1848.\(^ {30}\) In the Communist Manifesto, for example, he remarks that:

> The need of a constantly expanding market for its products chases the bourgeoisie over the whole surface of the globe. It must nestle everywhere, settle everywhere. Establish connections everywhere. The Bourgeoisie has through its exploitation of the world market given a cosmopolitan character to production and consumption in every country.\(^ {31}\)

As Harvey develops at length in his work Spaces of Hope, globalisation is, to a significant degree, merely an expression of an ongoing process of geographic


\(^{28}\) Harman, 2003, 5; Roper, 2005a, 27.

\(^{29}\) Bukharin, Ch. 10.

\(^{30}\) Roper, 2005a, 21.

\(^{31}\) Marx and Engels, 46-7.
reorganisation oriented towards at least temporarily overcoming the tendency towards crisis within the capitalist mode of production. Due to the internal contradictions of capitalist logic, capitalism continuously requires ‘spatio-temporal fixes.’ As a result, via both expansion and intensification, “capitalism...constructs a distinctive geographic landscape...a produced space...that facilitates [further] accumulation.”32 Essentially, it is such a process of spatio-temporal construction that is referred to as ‘globalisation’ in popular contemporary discourses.

Globalisation, then, can be seen to constitute a product of an inherent tendency toward expansion located within capitalism. As McMichael succinctly puts it, ultimately globalisation is “immanent in capitalism.”33 A final important point to note, however, is that the actual historical manifestation of globalisation is not simply the outcome of the unfolding of some sort of mechanical ‘iron law’ of history.34 As suggested in the previous chapter, when analysing historical phenomena it is necessary to consider the role of both structural factors and human agency. Thus, as Panitch and Gindin advocate, it may be useful to also consider actual historical globalisation, as being simultaneously the product of “human agents and the institutions they [have] created [including, most notably, states], albeit under conditions not of their own choosing.”35

32 Harvey, 2000, 54.
34 Panitch and Gindin 2013, 2.
35 Ibid.
2.2) The Dollar-Wall Street Regime

As developed by Gowan throughout his influential work *The Global Gamble*, the ‘Dollar-Wall Street Regime’ (DWSR) comprises the base financial structure under which contemporary financial globalisation has unfolded. A key function of the DWSR is to render unto the US what effectively constitutes “monocratic power over international monetary affairs.”36 Under the DWSR, US-dominated international private financial markets (IPFMs) are now at the very core of public macroeconomic management across the globe. The US government, via the operations of the Treasury Department and Federal Reserve, is capable of exerting unmatchable influence over the political and economic decision-making of virtually all of the other nations of the advanced capitalist and developing worlds. Alternatively, through the financial mechanism of the DWSR, the US can now, to a significant degree, manage the global macroeconomy directly in its own interests.37 As its name suggests there are two central pillars of this latest regime of international financial governance. The first is the adoption and maintenance of a pure US dollar standard in international monetary relations.

A *pure* dollar standard in international financial relations was initially established via the cutting of the official link between the value of the dollar and the value of gold that prevailed under the Bretton Woods System (BWS) on 15 August, 1971.38 From this point on the US Treasury Department was no longer responsible for maintaining a fixed-standard value for the dollar and, thus, established the dollar as the sole anchor of the international monetary

---

36 Gowan, 19.
37 Ibid, 24, 31. This was effectively demonstrated following the Global Financial Crisis (GFC) of 2007-2008. The US Federal Reserve implemented successive episodes of so-called “quantitative easing” ostensibly as a means of stabilising and reinvigorating global capitalism. This entailed introducing massive amounts of new liquidity into the global financial system (thereby devaluing the US dollar), which fundamentally served to boost the US domestic economy and reinforce the position of US-dominated private financial capital in the global economy. Other states were left to deal with the fallout; overvalued exchange rates and inflationary pressures.
38 As discussed in more detail in the following section (2.3), however, the world had effectively operated on a *de facto* USD standard for some time prior to this. See also Panitch and Gindin 2008, 23.
system. However, as Panitch and Gindin point out, it was not until the advent of the so-called ‘Volcker shock’ of 1979-82 that the dollar was firmly entrenched as the sole global monetary anchor. During the 1970s, successive US administrations opted to fund persistent current account deficits via ‘loose’ monetary policy – that is, “printing money, or otherwise increasing the supply of credit.” The prolonged pursuit of a ‘loose’ monetary policy throughout much of the 1970s produced high inflation, an increasingly weak dollar, and large capital outflows.

The large outflows of capital from the US resulted in a commensurate accumulation of dollar-denominated assets in foreign hands. High inflation coupled with a rapidly declining dollar, in-turn, undermined the value of the dollar assets being accumulated offshore, thereby raising the very real prospect of a “market panic over the value of the dollar” resulting in a widespread dumping of the dollar. Thus, by the end of the 1970s, the position of the dollar as the international reserve currency was under serious threat. Foreign holders of dollar were becoming increasingly concerned about the reliability of the dollar as an effective cross-border store of value. The Volcker shock served to remedy this by ensuring “the value of the dollar as the international currency.” Fundamentally, the Volcker shock entailed “limiting the growth in the money supply and allowing interest rates to rise to whatever level – and at whatever short-term economic cost – was necessary to break the back of

---

43 Calleo 2009, 167.
45 As articulated by Cohen, serving as a reliable store of value is a core function of an international currency. See B. Cohen 1971, The Future of Stirling as an International Currency (London: Macmillan).
inflation.” 47 From an average rate of only 8 per cent in 1978, the base US interest rate “rose to over 19 per cent at the beginning of 1981 and didn’t consistently return to less than double digits until after 1984.” 48 This signaled to the world that, from this point on, the US Federal Reserve would take explicit responsibility for the declaration of “an interest rate that would project an unwavering anti-inflationary commitment so as to become the global anchor of a dollar-based world economy.” 49 As Paul Volcker himself put it, it gave the US Federal Reserve the principle “role in stabilising expectation [that] was once the function of the gold standard.” 50 

In the wake of the Global Financial Crisis (GFC), serious questions have been raised about the sustainability of the dollar’s status in the international monetary system. 51 Despite predictions of its imminent demise, however, for now the dollar continues to occupy the preeminent position in international monetary relations. 52 As the latest Bank of International Settlements (BIS) Triennial Central Bank Survey of Foreign Exchange and Derivatives Market Activity states, “the role of the US dollar as the world’s dominant vehicle currency remains unchallenged. FX deals with the dollar on one side of the transaction represented 87% of all deals initiated in April 2013.” 53 In comparison, the dollar’s main potential rivals for currency supremacy - the euro and the yen – were on one side of only 33% and 23% of all FX deals respectively (see Table 2.1). 54 Similarly, as Eichengreen observes, “there has been no discernible
movement away from the dollar as a currency in which to invoice trade and settle transactions.”\textsuperscript{55} Around half of global exports are dollar denominated.\textsuperscript{56} Underpinning this is the ongoing commitment of OPEC to the pricing of petroleum in US dollars.\textsuperscript{57} Correspondingly, as an official unit of account, the dollar is the most commonly used ‘anchor currency’. Amongst countries that operate some form of a fixed – or ‘pegged’ – foreign exchange (FX) regime, around two-thirds use the US dollar.\textsuperscript{58} In addition, the dollar remains the primary currency serving as a store of value in the international financial system. IMF data indicates that dollar-denominated financial instruments (most notably US Treasury bonds) currently comprise 61.2% of global official FX reserves (see Table 2.2).\textsuperscript{59} Respectively, in the private market arena, 48% of international bank deposits and 44% of the global stock of international debt securities are denominated in dollars.\textsuperscript{60} Thus, to paraphrase Richard Cooper, in the decade following the onset of the GFC, the status of the dollar has not been fundamentally altered; the dollar continues to provide “the monetary foundation of the international economy.”\textsuperscript{61}

\textsuperscript{55} Eichengreen 2011, 356.
\textsuperscript{56} Cohen 2009, 146.
\textsuperscript{57} Eichengreen 2011, 123.
\textsuperscript{58} Most of these countries are “in Asia, Africa, the Middle East, and Latin America.” The Euro, however, dominates amongst “non-euro area EU members, EU accession or potential accession countries, and French-speaking African countries.” See A. Bertuch-Samuels and P. Ramoglan 2007, “The Euro: Ever More Global”, Finance and Development, Vol. 44, no 1, 47.
\textsuperscript{59} http://www.imf.org/external/np/sta/cofer/eng/. A significant portion of the global currency composition of official foreign exchange reserves (COFER) is unknown due to the high number of non-reporting countries including, most prominently, China. See Eichengreen 2011, 123-124.
\textsuperscript{60} Bertuch-Samuels and Ramoglan 2007.
Table 2.1) Distribution of Reported Foreign Exchange Market Turnover by Currency, 1995 to 2013

<table>
<thead>
<tr>
<th>Year</th>
<th>USD</th>
<th>Euro</th>
<th>Yen</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995</td>
<td>83</td>
<td>n.a.</td>
<td>24</td>
</tr>
<tr>
<td>1998</td>
<td>86.8</td>
<td>n.a.</td>
<td>21.7</td>
</tr>
<tr>
<td>2001</td>
<td>89.9</td>
<td>37.9</td>
<td>24</td>
</tr>
<tr>
<td>2004</td>
<td>88.0</td>
<td>37.4</td>
<td>20.8</td>
</tr>
<tr>
<td>2007</td>
<td>85.6</td>
<td>37.0</td>
<td>17.2</td>
</tr>
<tr>
<td>2010</td>
<td>84.9</td>
<td>39.1</td>
<td>19</td>
</tr>
<tr>
<td>2013</td>
<td>87</td>
<td>33.4</td>
<td>23</td>
</tr>
</tbody>
</table>


The overarching significance of the dollar’s hegemonic position within the international monetary system is that it bestows upon the US what is sometimes referred to as its “exorbitant privilege.” This comprises its effective freedom from the balance of payments constraints faced by all other states. On the basis of the widespread demand for the dollar (due to its hegemonic position), the US has the capacity to finance its current account deficits via “the sale of Treasury bills...and [therefore] can run its economy without large [foreign exchange] reserves” for a prolonged period of time. Simultaneously, due to its ability to drastically alter the value of its currency without significant economic consequence, the US has the unique capacity “to deflect the costs of adjustment [to its current account deficits] onto foreigners.”

---

64 Panitch and Gindin 2005, 62; H. James 2009, “The Enduring International Preeminence of the Dollar”, in Helleiner and Kirshner, 25; Calleo 2009, 170. As Seabrooke observes, the one prominent caveat to this arrangement is that the US must maintain a robust and highly “liquid financial system” and be able to continue to attract buyers for its securities in the international markets.” See L. Seabrooke 2001, US Power in International Finance (New York: Palgrave), 105.
An additional significant benefit accruing to the US on the basis of the dollar’s international role is what is termed *seigniorage*. By definition, *seigniorage* is essentially “the difference between the cost of creating new money – including interest payments – and its face value.”\(^{66}\) In practical terms, it entails that, as the originator of the dominant international currency, the US pays significantly less to borrow from foreigners than other states. As Helleiner and Kirshner outline,

when foreigners have held dollars, they have provided the equivalent of an interest-free (in the case of Federal Reserve notes) or low-interest (in the case of Treasury securities) loan to the United States. According to some estimates, in recent years the “seigniorage” profit has totaled over $20 billion per year.\(^{67}\)

Significant commercial advantages also accrue to the US private sector on the basis of the global dollar standard.\(^{68}\) US financial institutions, for example, enjoy significant competitive advantages over their overseas rivals due to their enhanced access to the US Federal Reserve.\(^{69}\) American firms that operate in foreign markets, meanwhile, generally do not have to contend with a fluctuating exchange rate and, thus, are spared the necessity of undertaking expensive foreign exchange hedging arrangements.\(^{70}\)

Beyond the economic sphere, the dominance of the dollar serves to enhance “the political influence and capacity of the US.”\(^{71}\) Due to other states’ dependence on US-based financial networks, the US is able “to exercise [an exceptional] degree of coercion internationally” to advance its own foreign

---

\(^{66}\) Kirshner 2008, 422; Eichengreen 2011, 3-4.  
\(^{68}\) Kirshner 2008, 422  
\(^{69}\) Helleiner and Kirshner 2009, 5.  
\(^{70}\) Ibid.  
\(^{71}\) Kirshner 2008, 424.
policy and international regulatory agendas. Simultaneously, involvement in the contemporary dollar-dominated international monetary system (and the accumulation of dollar-denominated reserves in particular), effectively serves to align the discrete economic interests of foreign states, as well as private-sector actors and institutions, with the broader economic, political, and strategic interests of the US.

The second focal pillar of the DWSR is the switch to US-dominated international private financial markets (IPFMs) as the primary site for the conduct of international financial relations. This was established through two key political moves undertaken by the US during the early 1970s. The first of these was Washington’s decision to recycle the vast quantity of petrodollars accumulated by OPEC oil producers as a result of the 1973 world oil crisis exclusively through New York investment banks. As Held et al observe, following the virtual quadrupling of world oil prices in 1973, a massive new body of liquid cash, totaling almost US$50 billion during the period from 1974 to 1976, came into the possession of a relatively small number of OPEC countries (including, most prominently, Saudi Arabia). Despite vehement opposition from Japan, the major Western European powers, and certain sectors in the US, these funds were transferred through to countries experiencing balance of payments difficulties “via bank credits and bond issues” from private Wall Street investment banks. The significance of this to the overarching project of shifting US-dominated IPFMs into the very centre of global financial relations is that by opting to recycle the glut of petrodollars in

---

75 Held et al, 202.
76 Cohen 2008, 36; Gowan, 21; E. Helleiner, “Explaining the Globalization of Financial Markets: Bringing States Back In”, Review Of International Political Economy, 2:2 (Spring 1995). Brazil and Mexico were amongst the most prominent receivers of such funds.
the manner chosen, “the markets came to play a role once reserved (in principle) exclusively for official institutions such as the [International Monetary] Fund.”

In essence, through the process of petrodollar recycling, the private banking system took over the functions proper to an official institution possessed of the power to finance balance-of-payments disequilibria through credit-granting and to create international liquidity...The function of creating international liquidity has been transferred from official institutions to private ones.

The second important political move undertaken by the US was the ending of the so-called financial ‘repression’ of the BWS through the final abolition of the capital and exchange controls that characterised that particular international financial regime. Under the BWS states’ central banks and states’ trade balances were the primary determinants of a currency’s overall stability. As will be discussed in more depth in the next section, the City of London did operate for much of the immediate post-war period as an almost entirely unregulated centre for private financial operations. However, beyond this, financial ‘repression’ was meant to largely exclude the involvement of IPFMs in the international monetary system.

The final abolition of the BWS controls fundamentally transformed the role of private finance in international monetary relations. As Gowan observes, from this point on IPFMs largely took over the roles previously held by the central banks. The bulk of the world’s domestic financial systems and exchange rates became openly vulnerable to developments in Wall Street-dominated

---

77 Cohen 2008, 36. As Cohen points out, “the practice of private lending for balance-of-payments purposes” was not new. However, “up to 1973, the private markets’ role tended to be relatively modest. It was only with the emergence of the petrodollar recycling problem that [IPFMS] came into their own as an alternative source of payments financing.” See ibid 36-37.

78 G. Carli 1976, Why Banks are Unpopular (Washington: IMF), 6, 8.

79 Although as will be discussed in more detail in the following section that ‘repression’ was something of a misnomer.

80 Gowan, 21-22.
IPFMs, with the basis of a currency’s stability becoming the concerned state’s underlying ‘creditworthiness’ in IPFMs.\textsuperscript{81} Moreover, the capacity for public supervision of private international financial operators was significantly reduced and, more importantly, what regulation is undertaken in the realm of international financial relations is predominantly determined by the unilateral decisions of the US government. Due to Wall Street’s pre-eminence amongst IPFMs, any regulatory moves undertaken by the US are transmitted through to the other domestic financial systems integrated into the DWSR. Essentially, the changes undertaken at the core of the system generate significant competitive pressures for similar changes to be undertaken in the periphery.\textsuperscript{82}

It is important to note that the two focal pillars of the DWSR are not to be considered mutually exclusive. Rather, as Gowan observes, they are inherently self-reinforcing.\textsuperscript{83} The international dominance of the dollar, for example, serves to orientate a majority of both states and private operators towards the major US IPFMs for their financial needs. This is primarily because with the majority of important internationally traded commodities being denominated in the dollar, most will likewise seek to hold the bulk of their FX reserves in dollars and also to seek to finance their operations though Wall Street or City of London operators.\textsuperscript{84} But, it is also because under the current prevailing system of floating FX rates there is a significantly increased onus on central banks and private trading firms to maintain more substantial dollar reserves in order to hedge against FX instability.\textsuperscript{85} This pressure is clearly illustrated by the expansion of official FX reserves mapped out in BIS data (see Table 2.2 below). Together, these factors, deriving from the dollar standard, have served to substantially expand both the volume and velocity of capital turnover within the core IPFMs, thereby systematically reinforcing their existing competitive

\textsuperscript{82} Gowan, 26-27.
\textsuperscript{83} Ibid, 24.
\textsuperscript{84} Ibid.
\textsuperscript{85} Ibid, 33.
Advantages. Respectively, the market dominance of Wall Street acts to reinforce the dominance of the dollar in world monetary affairs because its superior scope and resources generally render it both a safer and more competitive market. In principle, this serves as a significant attraction to either deposit and/or raise funds at the heart of the dollar-denominated system.

| Table 2.2) Annual Changes in Official Foreign Exchange Reserves, 2008 to 2013 |
|-----------------|-----|-----|-----|-----|-----|-----|
|                 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 |
| Advanced Economies | 61   | 83   | 194  | 269  | 195  | 55   |
| Asia            | 410  | 715  | 651  | 424  | 239  | 529  |
| Latin America   | 42   | 25   | 81   | 97   | 51   | -6   |
| CEE             | 6    | 13   | 14   | 3    | 15   | 20   |
| Middle East     | 150  | -29  | 50   | 88   | 148  | 79   |
| Russia          | -56  | -5   | 27   | 8    | 32   | -17  |
| World           | 641  | 819  | 1100 | 941  | 747  | 733  |


So, in essence, the key features of the DWSR can be summarised as follows:

1. The DWSR is the current system on which international monetary relations are based. It consists of two central pillars; a global dollar currency standard and US-dominated IPFMs playing a central role.

---

87 Ibid, 25.
88 Includes the US, Euro Zone, Japan, Switzerland, Australia, Canada, Denmark, Iceland, New Zealand, Sweden, and the UK.
89 Includes China, Taiwan, Hong Kong SAR, India, Indonesia, Korea, Malaysia, Philippines, Singapore, and Thailand.
90 Includes Argentina, Brazil, Chile, Mexico, Venezuela, Columbia, and Peru.
91 Central and Eastern Europe. Includes Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, and Slovenia.
92 Includes Kuwait, Libya, Qatar, and Saudi Arabia.
2. The significance of the dollar standard is that it endows the US with considerable balance of payments flexibility, *seigniorage*, commercial advantages for the US private sector, and enhanced influence and capacity in international relations.

3. Correspondingly, the significance of the centrality of Wall Street in international financial relations is that sovereign states and their central banks have minimal control over international financial relations. The key implications of this are:
   - The US has significant control over the regulation of the world’s financial systems.
   - Domestic financial systems and currency values are rendered increasingly vulnerable to developments on Wall Street.

4. The DWSR is also a self-reinforcing system of global financial governance. This is centrally because:
   - Dollar hegemony orientates financial operators towards Wall Street.
   - The size of Wall Street makes it safer to use the dollar in financial interactions.
2.3) The Establishment of the Dollar-Wall Street Regime: From Bretton Woods to Global Neoliberalism

The historic shift from the BWS to the DWSR - initially signaled by the de-linking of the USD from gold - comprised a major development within the post-war global financial system. Indeed, Eatwell and Taylor go so far as to state that, “on 15 August, 1971, the world of international finance was changed forever.”93 From that point onward, the global economy would operate without currencies being anchored to a commodity. The global economy had effectively moved onto a fiat money system for the first time in the history of capitalism.94

Fundamentally, this appears to have signaled the beginning of a major shift in the basis of global US hegemony.95 While finance had certainly been important previously during the decades immediately after World War II (discussed below), US hegemony had primarily been predicated on industrial supremacy and preponderant military power. Now, as Harvey observes, “threatened in the realm of production, the US had countered by asserting its hegemony through finance.”96 It is worth noting that Arrighi contends that this

---

96 Harvey 2003b, 63. This is not to say that the previous bases of US power either disappeared or were supplanted. Overwhelming military power of course remains a cornerstone of US imperial capacity. Rather, it appears that the US has become considerably more reliant on private financial capital as a means of asserting its global hegemony.
shift to financial power signals the onset of a period of hegemonic transition.\textsuperscript{97} Ultimately, he avers, “it is the expression (and a factor) of a relative and absolute loss of the [American] nation’s capacity to retain its centrality within the global political economy.”\textsuperscript{98}

However, the establishment of the DWSR was not simply a case of the US state aggressively pursuing a particular preconceived unilateral imperial political-economic agenda. Instead, the establishment of the DWSR (and its subsequent elaboration through a global process of neoliberalisation, discussed below) was also heavily influenced by a broad range of other factors salient at that particular historical juncture. Most notably, this included (but was by no means restricted to) complex developments both within and between the core advanced capitalist economies.

\textbf{The Long Post-War Boom}

As myriad authors have documented, western capitalism entered into a long economic boom following the conclusion of World War II. During the period spanning roughly from the late 1940s through until the early 1970s, the advanced capitalist world experienced a sustained period of historically unprecedented economic dynamism and growth.\textsuperscript{99} The significance of this long post-war boom should not be understated. As McNally observes,

\hspace{1cm}

\textsuperscript{97} Arrighi 1994; 2007, \textit{Adam Smith in Beijing: Lineages of the Twenty-First Century} (London; New York: Verso). A number of authors follow Arrighi on this point, most prominently Krippner. See G. Krippner 2005, “The Financialization of the American Economy”, \textit{Socio-Economic Review}, 3, 173-208; 2012, \textit{Capitalizing on Crisis: The Political Origins of the Rise of Finance} (Cambridge: Harvard University Press). Arrighi’s thesis is, however, also challenged by a number of authors. See, for example, A. Callinicos 2009, 193-4. It is also worth considering, as Harvey points out, that “if financialisation is a likely prelude to a transfer of dominant power from one hegemon to another (as has historically been the case) then the US turn towards financialisation in the 1970s would appear to have see a particularly self-destructive move” (Harvey 2003b, 72).
\textsuperscript{98} Ibid 2007, 203.
The world economy had never seen anything like the Great Boom of 1948-73. For a full quarter century the dominant economies surged ever forward, generating jobs, robust profits, and rising incomes year after year. These were the golden years of western capitalism.\textsuperscript{100}

Table 2.3 (below) provides a statistical overview of the long post-war boom.\textsuperscript{101} As can be seen, western capitalism indeed achieved “levels of sustained growth...without historical parallel before or since”, during the period from 1950 to 1973.\textsuperscript{102} In Western Europe, annual compound economic growth averaged almost 5%, after it had averaged just 2.11% or less since 1820. Meanwhile, annual GDP growth in Japan averaged a remarkable 9.29%. In effect, as McNally observes, “the Japanese economy expanded eight times over during the boom.”\textsuperscript{103} The respective level of economic growth in the US was generally lower than these other two key centres of advanced capitalism. Annual average GDP growth averaged some 3.93% in the US from 1950 to 1973. It is important to note, however, that the US economy began the extended period of economic growth in a significantly more advanced position.\textsuperscript{104}

\begin{thebibliography}{9}
\bibitem{100} Ibid, 27.
\bibitem{101} Extensive additional empirical work relating to the long post-war boom can be found in Armstrong et al.
\bibitem{102} Callinicos 2009, 175.
\bibitem{103} McNally, 27.
\bibitem{104} As McNally observes, “at the end of the war the economy [in Western Europe] lagged a full half-century behind the United States.” In addition, the devastated Japanese economy was “a hundred years behind the United States in 1945.” See ibid.
\end{thebibliography}
The long post-war economic expansion featured a boom in international trade. As Armstrong et al outline,

Between 1951-3 and 1969-71 the volume of world trade in manufactures grew by 349 per cent whereas the volume of output grew by 194 per cent. The ACCs [(advanced capitalist countries)] expanded their exports of manufacturing by 480 per cent between 1950 and 1971. By far the fastest growing part of that enormous growth was in the form of trade between the various advanced countries; their exports to the underdeveloped countries and the Eastern bloc grew far more slowly.

But the expanding flows of international trade were easily eclipsed by a massive increase of foreign direct investment (FDI). As Panitch and Gindin observe, “FDI...increased twice as fast as GDP” during the 1960s, whereas “international trade...grew 40 percent faster than GDP.” The primary driver of this post-war growth of FDI was the international expansion of US

---

105 Armstrong et al, 214.  
106 Ibid.  
108 Ibid.
multinational corporations (MNCs), especially into Europe.\footnote{109} During the period from 1956 to 1966, the number of US corporate manufacturing subsidiaries in Europe tripled (reaching a total of over 9000), with the average size of those subsidiaries also increasing considerably.\footnote{110} Eventually, with their domestic economies recovering from the devastation of World War II, important German and other European manufacturing firms initiated their own countervailing FDI seeking to penetrate the massive US domestic market.\footnote{111} Japanese firms also began to increase their FDI into the US during the 1950s and 1960s. The relative scale of this, however, was not as significant.\footnote{112} Thus, as Panitch and Gindin summarise, throughout much of the post-war boom, “the main action in relation to FDI and the internationalisation of production remained very much a North American-European affair.”\footnote{113}

US financial institutions followed their compatriot MNCs expanding into Europe and elsewhere during the long boom.\footnote{114} Indeed, as Dumenil and Levy observe, “the [post-war] expansion of trade and investment worldwide would have been impossible in the absence of the parallel development of banking activity.”\footnote{115} The international expansion of US banks began earlier, but ramped up particularly from the early 1960s onwards. As documented by Cassis, while there were only 131 individual foreign branches of US banks in Europe in 1960,
they subsequently proliferated.\textsuperscript{116} By the end of the decade the presence of American banks had increased to such an extent that they had become “significant financial actors inside Europe.” \textsuperscript{117} Indeed, US banks were progressively coming to challenge the entrenched UK and European banks for dominance.

The vigorous offshore expansion of US banks during the long post-war boom coincided with (and was fed by), a significant financial expansion within the domestic US economy.\textsuperscript{118} As Magdoff and Sweezy observe, “the financial sector of the economy which had been moribund in the 1930s and under tight control throughout the war experienced a vigorous growth during the next three decades.”\textsuperscript{119} Principally, the post-war domestic US financial expansion was underpinned by the strong growth in the broader economy.\textsuperscript{120} Private finance was, for instance, heavily involved in channeling funds for the prosperous manufacturing sector during the post-war era.\textsuperscript{121} Developing industries required increasing amounts of capital for productive investment and financial institutions inevitably provided a portion of the necessary funding.\textsuperscript{122} US banks also played an extensive role in capital intensive infrastructural ‘project financing’ during this period.\textsuperscript{123} This not only provided considerable opportunities for lending and balance sheet expansion, but also the generation of significant revenues from the charging of fees. The latter, it should be observed, would become an increasingly more important aspect of

\begin{flushright}
\textsuperscript{117} Panitch and Gindin 2013, 118.
\textsuperscript{118} ibid, 119.
\textsuperscript{120} ibid, 146.
\textsuperscript{121} Panitch and Gindin 2004, 52-53.
\textsuperscript{122} As Foster and Magdoff point out, however, many corporations, especially during the earlier stages of the economic expansion were effectively able to self-fund investment from retained earnings. See J.B. Foster and F. Magdoff 2009, \textit{The Great Financial Crisis} (New York: Monthly Review Press), 72.
\textsuperscript{123} Panitch and Gindin 2004, 53.
\end{flushright}
private financial institutions’ overall business, especially during the subsequent neoliberal era.

A strong current of innovation pervaded the “dramatic expansion of US domestic financial markets” that took place during the long boom.124 US financial institutions pioneered, for example, the creation and exploitation of creative new corporate structures and entities. Most notably, this included the invention of bank holding companies. As Panitch and Gindin observe, the use of these structural arrangements “was undertaken explicitly to enable banks to develop the legal and market potential to span commercial, investment, insurance, and mortgage functions”, thereby effectively allowing major financial institutions to circumvent the market segmentation and specialisation regulations implemented via the Glass-Steagall Act as part of the New Deal.125 US financial institutions also oversaw the creation of a host of new financial instruments (and also the creation of increasingly deep markets for the same).126 Particularly crucial here was the US Federal Reserve’s decision to operate monetary policy through private Wall Street banks’ so-called ‘market making’ in Treasury bonds.127 By doing this, the market for US Treasury bonds was deepened considerably, as illustrated by the massive increase in the volume of Treasury securities made available to investors.128 As Panitch and Gindin explain, “the [increased] liquidity of the Treasury bond market…had the subsequent effect of enabling the large banks to invent new financial instruments, such as certificates of deposit.”129

---

124 Panitch and Gindin, 119.
125 Ibid, 120.
126 As Konings delineates, the previously discussed international expansion of American finance during the post-war boom actually relied extensively on this financial innovation, especially the process of securitisation that US commercial banks had initiated. See M. Konings 2008, “The Institutional Foundations of US Structural Power in International Finance: From the Re-Emergence of Global Finance to the Monetarist Turn”, Review of International Political Economy, Vol. 15, 35-61.
127 Panitch and Gindin 2013, 119.
128 Ibid.
129 Ibid.
But the post-war domestic financial expansion was not just restricted to the financial sector itself. It also featured a broader process of financialisation throughout the domestic US economy and society.\textsuperscript{130} Through a “proliferation of employer-sponsored pension plans” and a massive parallel expansion of consumer credit (and consumer credit facilities, such as credit cards), workers became increasingly enmeshed in financial markets as both savers and borrowers during the post-war economic boom.\textsuperscript{131} At the same time, non-financial firms, both large and small, were increasingly engaging in financial operations (and, like the previously mentioned workers, they were doing this as both borrowers and savers). Over the course of the long boom, non-financial firms became the largest originators of consumer credit. Indeed, as documented by White, by the end of the long boom, the three largest industrial firms and the three largest retail firms were (as discrete groupings) issuing more consumer credit than the three largest financial firms combined.\textsuperscript{132} Furthermore, it was major manufacturing firms that were ultimately behind the emergence of a nascent commercial paper market in the mid-1960s. These non-financial corporations were seeking a reliable channel of funds impervious to the state-imposed credit shortages that periodically constrained the lending of the traditional financial system.\textsuperscript{133}

The long post-war boom was also characterised by significant technological progression. This notably included considerable advancements in the areas of electronic computing and telecommunications. The strong expansion of finance during the long post-war boom depended greatly on the

\textsuperscript{130} As will be discussed in more detail later, financialisation is a somewhat ambiguous term. Here it is used to refer to an increased involvement of people in financial transactions in everyday life, coupled with a simultaneous increase in the involvement in financial operations of businesses otherwise primarily concerned with trade and commodity production.

\textsuperscript{131} Panitch and Gindin 2013, 121.


great strides in innovation made in these areas. Ultimately, they provided the necessary technological basis on which increasingly deep and sophisticated IPFMs could actually be created.

There is a widespread view that Keynesian policies were responsible for the extended nature of the post-war capitalist expansion. Centrally, state interventions to raise the level of system-wide expenditures on investment or consumption are considered to have been able to effectively counteract the tendency within capitalism towards overaccumulation (discussed in Section 2.1). Unsurprisingly, this view is most commonly espoused within Keynesian and post-Keynesian analyses. However, a number of Marxists offer similar explanations of the long boom. For Harvey, for example, the post-war expansion of capitalism was underpinned by “a class compromise between capital and labour”, which enabled the state to deploy “fiscal or monetary policies usually dubbed ‘Keynesian’...to dampen business cycles and ensure reasonably full employment.”

This explanation is disputed by a number of other authors (most notably Harman and Callinicos), who instead posit that the key factor underpinning the long post-war boom was the emergence of a so-called “permanent arms economy” in the US (and, to a lesser extent in France and the UK) as part of the Cold War. According to Harman, ultimately “what kept the boom going was not Keynes, but the same thing that had brought the slump of the 1930s to an end – massive arms spending.” While certainly not rivaling the situation during World War II itself, official expenditure on armaments by Western

---

137 Harman 2008, 19.
governments as part of the post-war arms race with the USSR was nevertheless vast. The US, in particular, undertook enormous investments in the development of nuclear weapons and other advanced weapons systems. As Callinicos observes, US military spending jumped from 4.3 per cent of gross national product in 1948 to a high of 13.6 per cent in 1953 and was still 9.0 per cent in 1969 – far above previous peacetime levels.”

Harman and Kidron maintain that such extensive military spending as part of the post-war arms race had the effect of partially counteracting the inherent tendency within capitalism of the rate of profit to fall (discussed in Section 2.1). In their view, military spending absorbed considerable surplus value that would have otherwise been used for productive investment. This effectively slowed down the underlying rate of capital accumulation in the post-war US economy and, consequently, “the organic composition of capital…rose much more slowly than it otherwise would have.” As outlined in Section One, the increasing organic composition of capital – that is, “the ratio of plant and equipment to workers” – ultimately drives a long-term tendency of a falling rate of profit within capitalism. Hence, for Harman and Kidron, by partially offsetting the rising organic composition of capital, military spending by Western governments acted as a countervailing tendency to the falling rate of profit. This, in-turn, helped underpin and extend the long post-war boom.

The Breakdown of the Long Boom

The countervailing effects of government intervention in the form of either Keynesian policies or of a “permanent arms economy” may have thus helped to sustain global capitalism for an extended period of time following the

---

138 ibid.
139 Callinicos 2009, 175.
140 ibid. As Callinicos points out, “this explanation is supported by the evidence that the organic composition of capital rose only very slowly during the 1950s and 1960s from the low level it had reached at the end of the 1940s as a result of depression and war.” See Callinicos 2009, 175.
141 ibid.
142 ibid
conclusion of World War II.\textsuperscript{143} Certainly it appears that, for a time, strong countervailing tendencies enabled the core capitalist economies to achieve, and subsequently maintain, historically high rates of growth.\textsuperscript{144} Regardless of whether or not Keynesianism or the “permanent arms economy” constituted the most significant causal factor, however, the long post-war boom nevertheless ultimately proved to be unsustainable.\textsuperscript{145} As Harvey summarises,

By the end of the 1960s embedded liberalism began to break down, both internationally and within domestic economies. Signs of a serious crisis of capital accumulation were everywhere apparent. Unemployment and inflation were surging everywhere, ushering in a global phase of ‘stagflation’ that lasted through much of the 1970s.\textsuperscript{146}

Figure 2.1 (below), graphically illustrates the breakdown of the long post-war economic boom and the onset of global stagflation in the advanced capitalist economies in the early 1970s.

\textsuperscript{143} Harman 2008, 19. Another prominent explanation for the enduring nature of the long boom centres on the potential countervailing effects of states’ implementation of Keynesian macroeconomic policy prescriptions. As Callinicos points out, however, the explanatory power of this perspective may be somewhat restricted due to the limited and largely uneven way in which Keynesian policy measures were actually employed by states during the post-war period. See Callinicos 2009,\textsuperscript{144} Brenner 1998, 49-63; 2002, 9.
\textsuperscript{145} Harvey 2003, 61.
\textsuperscript{146} ibid 2005b, 12.
There is broad agreement within the radical international political economy literature that a key factor contributing to the collapse of the long post-war boom was the negative trajectory of the underlying rate of profit.\textsuperscript{148} Centrally, from around the mid-1960s onwards, corporate profitability in the advanced capitalist economies began to quickly decline.\textsuperscript{149} The empirical support for this development is considerable. “Indeed, the evidence for declining profits is so overwhelming that”, as McNally observes, “radical political economists of varying persuasions, who can agree on little else, all accept that the profit rate fell persistently from the mid-1960s until the early

\textsuperscript{147} The OECD is here used as an approximation of the “Advanced Capitalist Countries” category used by Armstrong \textit{et al}.

\textsuperscript{148} Brenner 2002, 9; Dumenil and Levy 2011, 17; McNally 2011, 28.

\textsuperscript{149} The reasons for the fall in the world profit rate from the mid-1960s onwards are no doubt highly complex. However, a robust argument can be made that a powerful “profit squeeze” took place in the key manufacturing sector during this period, especially in the US. The influential “profit squeeze” thesis was initially proposed in A. Glyn and B. Sutcliffe 1972, \textit{British Capitalism, Workers and the Profit Squeeze} (London: Penguin). Brenner has advanced the most developed counter to the profit squeeze thesis, see R. Brenner 1998, “The Politics of Global Turbulence”, \textit{New Left Review}, Vol. 1, no. 229. However, Panitch and Gindin argue that Brenner’s critique is highly problematic. See Panitch and Gindin 2013, 385.
1980s.” 150 Figure 2.2 illustrates the overarching trajectory of business profitability in the core centres of capitalism during the long boom. 151 As can be seen, the US economy experienced a gradual decline in profitability during the 1950s after having previously recorded high levels of profitability in the immediate aftermath of World War II. 152 This trend subsequently reversed between 1961 and 1966 with a pronounced spike in corporate profitability being registered. 153 This reversal, however, was only temporary; the US rate of profit fell away rapidly from 1967 onwards. 154 Respectively, profit rates in the major European economies maintained a reasonably “steady downward trend from their very high postwar rates” over the course of the long boom. 155 In all likelihood partially reflecting the extent of international economic competition that developed between the two (in the realm of manufacturing especially), the rate of profit in Japan broadly followed that of the US, albeit in reverse. During the 1950s, business profitability gradually increased in Japan. It then declined at the same time as the US experienced its mid-1960s profit spike. Profitability in the Japanese economy subsequently increased sharply during the late-1960s, before falling away sharply in concert with both the US and Europe in the early 1970s.

150 McNally 2011, 28.
151 Brenner (2002, 39 Figure 1.3) provides a broadly similar empirical illustration, albeit with an extended timeframe.
152 Panitch and Gindin 2013, 135.
153 ibid
154 ibid.
155 ibid.
Businesses responded to the falling rate of profit from the mid-1960s onwards by undertaking extensive new investment.156 As McNally observes, “with competition for sales and profits intensifying”, throughout the late 1960s and on into the early 1970s, “firms frantically built up new capacity at an ever increasing pace.”157 On average, US non-financial corporations’ annual fixed asset investment increased by a historically high rate of 4.3 percent (adjusted for inflation) from 1967 to 1973.158 The upswing in new business investment was even greater in Japan and the major European economies.159 By 1970, increased investment in these ‘later-developing’ economies had dragged the global rate of accumulation up to 5.5 percent.160

Ultimately, this wave of new corporate investment throughout the advanced capitalist world prompted the development of “a serious crisis of
The Shift to Neoliberalism in New Zealand

161 As McNally observes, “while profitability was turning down “during the late 1960s and early 1970s, “over-accumulation was turning up in a classic pattern of over-investment.”162 The crisis of over-accumulation of the 1970s developed broadly in line with the underlying dynamics of capitalist accumulation described in Section 2.1.163 Faced with declining profits (and largely unable to effect meaningful reductions in labour costs due to strong labour militancy), competing businesses sought to improve their productivity and productive capacity through additional capital investment. Following the analysis developed by Harvey, these system-wide efforts resulted in a major blockage in the necessary “circulation of capital” required under capitalism.164 Economic growth subsequently ground to halt and “an excess or overaccumulation of capital relative to the opportunities to use that capital profitably” became manifest.165

The Collapse of Bretton Woods

Coinciding with (and, indeed, causally linked to) the falling aggregate rate of profit, from the mid-1960s onwards sizeable trade imbalances also emerged between the US and its major competitors, Germany and Japan.166 Table 2.5 outlines the evolution of the US trade balance with Germany and Japan. As can be seen, “beginning in 1965, US trade balances with Japan and Germany…fell rapidly.”167 After an initial trade deficit of US$500 million being recorded with Japan in 1965, the combined trade deficit with both major US competitors deteriorated considerably. After falling to an average of around US$2 billion each year from 1968 to 1970, the annual combined trade deficit

\[161\] Harvey 2005, 12
\[162\] McNally 2011, 29.
\[163\] ibid, 29-30.
\[164\] Harvey 2010, 45.
\[165\] ibid.
\[166\] McNally 2011, 90.
\[167\] Brenner 2006, 125.
reached US$4.1 billion in 1971. This was fueled by a US$3.3 billion trade deficit with Japan alone.

Table 2.4) The Annual US Trade Balance with Germany and Japan, 1963 to 1973 (US$ billions)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Japan</td>
<td>0.3</td>
<td>0.2</td>
<td>-0.5</td>
<td>-0.8</td>
<td>-0.3</td>
<td>-1.2</td>
<td>-1.6</td>
<td>-1.4</td>
<td>-3.3</td>
<td>-3.9</td>
<td>-1.3</td>
</tr>
<tr>
<td>Germany</td>
<td>0.6</td>
<td>0.4</td>
<td>0.3</td>
<td>-0.1</td>
<td>-0.3</td>
<td>-1.0</td>
<td>-0.5</td>
<td>-0.4</td>
<td>-0.8</td>
<td>-1.4</td>
<td>-1.6</td>
</tr>
<tr>
<td>Japan &amp; Germany</td>
<td>0.9</td>
<td>0.6</td>
<td>0.2</td>
<td>-0.9</td>
<td>-0.6</td>
<td>-2.2</td>
<td>-2.1</td>
<td>-1.8</td>
<td>-4.1</td>
<td>-5.3</td>
<td>-2.9</td>
</tr>
</tbody>
</table>

Source: Brenner 2006, 125.

The development of this combined trade deficit with Germany and Japan helped underpin a broader deterioration of the overall US balance of payments position. As Brenner outlines, mounting “merchandise trade deficits” combined with “rising foreign investment and bloated military expenditures associated with the Vietnam War” to bring about “skyrocketing US balance of payments deficits.” Ultimately, the underlying “trade deficits were too large to be counterbalanced” by the US and, as a result, in 1971 the external balance “also went negative.”

The emergence of these significant US external macroeconomic imbalances fomented the development of the so-called “world money crisis.” Centrally, they entailed a greatly increased accumulation of USD outside of the US. During the initial stages of reconstruction a USD shortage had

---


169 Brenner 2006, 125.

170 The likely development of such a crisis due to the so-called ‘Triffin dilemma’ had actually been predicted almost a decade earlier. See R. Triffin 1960, Gold and the Dollar Crisis: The Future of Convertibility (New Haven: Yale University Press).

171 McNally, 90. Although it is important to note that a global USD surplus had emerged much earlier due to increasing European and Japanese exports to the US, in addition to expanding US military spending.
prevailed.\textsuperscript{172} Subsequently, as the European and Japanese economies recovered, this shortage transmuted into a surplus. From the mid-1960s onwards, this surplus morphed into a veritable glut. As McNally observes, “so rapid was the growth of foreign dollar holdings that they doubled between 1968 and 1971 alone – from $150 billion to $300 billion.”\textsuperscript{173} Such significant ongoing currency outflows ultimately resulted in a prolonged run on the USD by private international money market operators.

In this regard, it is important to recognise that, despite the rigorous system of capital and exchange controls in place under the BWS, the previously discussed expansion of US banks and MNCs into Europe during the 1950s and 1960s was also accompanied by the creation of major IPFMs. The most important of these was the so-called ‘Eurodollar market’ centred on the UK’s financial hub, the City of London.\textsuperscript{174} As Panitch and Gindin delineate, exploiting “an accounting loophole in the exchange control regulations, and facilitated by the Bank of England without either approval or oversight by the UK Treasury”, in the mid-1950s the merchant bankers of “the City created a completely unregulated international market for the dollar.”\textsuperscript{175} This key financial innovation provided a new way to accommodate the mounting international USD surplus. Excess dollars were deposited in accounts in City of London banks and subsequently loaned out to fund further investment (often at better rates than available through the closely regulated domestic financial systems). The first Eurodollar accounts were set up by the USSR and China as a means of banking outside of the reach of the US.\textsuperscript{176} Later the major depositors became Western European central banks and US MNCs. As Panitch and Gindin observe, the City of London retained its position as a major centre of international finance under the subsequent DWSR arrangements in a large part due to its previous creation of the Eurodollar market.

\textsuperscript{172} As Panitch and Gindin argue, this shortage was counteracted in Europe via the so-called ‘Marshall Plan’ which effectively acted as a form of offsetting financing. See Panitch and Gindin 2004, 50.
\textsuperscript{173} Ibid.
\textsuperscript{174} Panitch and Gindin 2013, 117-118. Ultimately, the City of London retained its position as a major centre of international finance under the subsequent DWSR arrangements in a large part due to its previous creation of the Eurodollar market.
\textsuperscript{175} Ibid, 118. See also Gowan, 22.
\textsuperscript{176} Panitch and Gindin 2013, 380. The US had previously seized the financial assets of Yugoslavia held in the US.
these central banks were major depositors primarily because, following the restoration of currency convertability, “the [Bretton Woods] system of fixed exchange rates made it necessary for Western European governments to have...dollar reserves available for possible intervention in foreign exchange markets to maintain the value of their currencies.”

The latter MNCs, meanwhile, “were directed there by their US banks, which could offer higher rates for short-term deposits in London, due to the continuation of New Deal ‘Regulation Q’ ceilings on the interest banks could pay on deposits at home.”

Led by the innovative Midland Bank, the UK merchant banking community initially controlled much of this important incipient IPFM. Indeed, as Schenk observes, “at the middle of 1956 Midland [alone] probably still accounted for at least half of total Eurodollar deposits.” However, the rapidly expanding Eurodollar market quickly came to be dominated by US commercial banks.

Table 2.6 outlines the relative shares of the Eurodollar market in the early 1960s. As can be seen, while their external activities were hampered by considerable regulations at home, US banks operating in the City of London were certainly not precluded from becoming significantly involved in the Eurodollar market. By the end of 1962 almost a full third of Eurodollar deposits were being made into the nine US banks that were operating in the City of London at the time. Thus, by the early 1960s, the City of London had already effectively become a satellite of Wall Street and, by extension, had become integrated into the nascent nexus of the US Treasury, Federal Reserve,
and Wall Street that would subsequently form the basis of the new regime governing international financial relations during the neoliberal era.

**Table 2.5** UK Banks’ Overseas Liabilities in All Currencies (£m)

<table>
<thead>
<tr>
<th></th>
<th>Dec 1962</th>
<th>Percent</th>
<th>March 1963</th>
<th>Percent</th>
<th>April 1963</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Clearing Banks</strong></td>
<td>46</td>
<td>4.5</td>
<td>58</td>
<td>5.0</td>
<td>58</td>
<td>5.1</td>
</tr>
<tr>
<td><strong>Scottish and Irish Banks</strong></td>
<td>27</td>
<td>2.6</td>
<td>23</td>
<td>2.0</td>
<td>24</td>
<td>2.1</td>
</tr>
<tr>
<td><strong>British Overseas Banks</strong></td>
<td>236</td>
<td>23.0</td>
<td>258</td>
<td>22.1</td>
<td>255</td>
<td>22.2</td>
</tr>
<tr>
<td><strong>Accepting Houses</strong></td>
<td>191</td>
<td>18.6</td>
<td>199</td>
<td>17.0</td>
<td>196</td>
<td>17.1</td>
</tr>
<tr>
<td><strong>US Banks</strong></td>
<td>277</td>
<td>27.0</td>
<td>362</td>
<td>30.9</td>
<td>370</td>
<td>32.3</td>
</tr>
<tr>
<td><strong>Japanese Banks</strong></td>
<td>111</td>
<td>10.8</td>
<td>125</td>
<td>10.7</td>
<td>112</td>
<td>9.8</td>
</tr>
<tr>
<td><strong>Other Foreign Banks</strong></td>
<td>139</td>
<td>13.5</td>
<td>145</td>
<td>12.4</td>
<td>132</td>
<td>11.5</td>
</tr>
</tbody>
</table>

Source: Schenk, 230.

It is worth noting that orthodox accounts of post-war international financial developments often tend to uphold that it was only the global rise of neoliberalism (and the liberalisation and deregulation of finance this entailed) that finally unleashed the untrammelled expansion of IPFM’s that characterises contemporary global capitalism.\textsuperscript{184} Two respective eras of post-war international finance are typically distinguished; an era of financial ‘repression’ under the BWS, followed by an era of financial ‘liberation’ under global neoliberalism.\textsuperscript{185} As the development of the Eurodollar market demonstrates, however, it is, in-fact, quite simply “not the case that deregulation occurred first, followed by a financial explosion. Instead, the flare-up of unregulated markets came first.”\textsuperscript{186} Thus, the BWS era should not be viewed purely in terms of

\textsuperscript{184} Helleiner 1994 exemplifies such accounts.
\textsuperscript{185} Panitch and Gindin 2004, 48.
\textsuperscript{186} McNally 2011, 91.
providing for the international repression of finance.\textsuperscript{187} Rather, as Battilossi points out, it is important that the Bretton Woods years are also “regarded…as the cradle of the global financial order that eventually emerged in the final two decades of the last century.”\textsuperscript{188}

With the massive global USD glut continuing to grow unabated, from the late-1960s onwards, the unregulated international money markets that had been restored (under the so-called ‘repression’ of the BWS) began to significantly undermine the international reserve position of the USD. As Brenner outlines, the money markets placed significant “downward pressure on the dollar and upward pressure on the mark and yen” via successive speculative runs versus the USD.\textsuperscript{189} With their currencies “implicitly strengthened” against the USD, short-term speculative capital inflows into Germany and Japan from the Eurodollar market ramped up. Indeed, they “reach record proportions” by the close of the decade.\textsuperscript{190} This produced rapidly mounting pressures for the revaluation of both the mark and yen.\textsuperscript{191}

The resulting world money crisis culminated in the early 1970s. Centrally, enduring short-term speculative flows caused a blowout of the overall US external payments position. From a level of $10 billion in 1970, the external flow of USD increased to $30 billion in 1971.\textsuperscript{192} This quickly put unbearable pressure on the US government’s gold reserves that still ostensibly backed the value of the USD as international currency. Despite previously ceasing to honour its commitment to sell gold to private parties at $35 per ounce in 1968, US gold reserves nevertheless collapsed to a critical level, representing “less than a

\textsuperscript{189} Brenner 2006, 125.
\textsuperscript{190} Ibid, 126.
\textsuperscript{191} Ibid.
\textsuperscript{192} Ibid, 127.
quarter of its official liabilities.”193 As McNally observes, “once the reality of the 1971 American trade deficit set in, the rush to convert dollars into gold went through the roof, reaching an annual rate of $35 billion that summer.”194

The pressures on the broader BWS framework of fixed exchange rates anchored by a gold-backed USD became insurmountable at this point. As Harvey observes, in essence, “gold could no longer function as the metallic base of international money.”195 For the US, “the combined economic and political costs” of maintaining such an arrangement were, quite simply, unacceptable.196 Consequently, as discussed in the previous section, in August 1971, the US suspended USD-gold convertibility; the signal moment in the establishment of the DWSR.

The suspension of USD-gold convertibility immediately increased the US government’s room for manoeuvre in the realm of macroeconomic policy formulation. As Brenner observes, in-effect, the US was freed “from the requirement to reduce its overseas deficits by deflating the economy in order to decrease imports and increase exports so as to hold the dollar at its assigned value.”197 Subsequently, the US took full advantage of the increased policy flexibility that it had now been invested with to advance its own discrete economic interests. From late 1971 until 1973, it proceeded to “pursue, untrammeled, expansionary monetary and Keynesian budget deficit policies.”198 The objectives of this were multiple: stimulating the domestic US economy by boosting demand; devaluing the currency in order to boost the international competitiveness of US industry; and depreciating the value of the international USD surplus in real terms.199 In-effect, the US sought to exploit the

193 ibid.
194 McNally 2011, 92.
195 Harvey 2005b, 12.
196 Brenner 2006, 126.
197 ibid 2002, 27.
199 ibid.
enduring key role of the USD to deflect some of the costs of adjustment to the mounting global imbalances onto its main economic competitors, Germany and Japan.\textsuperscript{200}

As Brenner outlines, following the detachment of the USD from gold, up until the final scrapping of the Bretton Woods capital controls in 1973, efforts were made “to revive pegged exchange rates and a Bretton Woods-type framework.”\textsuperscript{201} “The other leading capitalist states, led by Germany, France, and Japan, sought through painstaking negotiations between 1972 and 1974 to secure a return to a system of pegged exchange rates to be buttressed by controls over the mobility of capital.”\textsuperscript{202} Following the analysis of Helleiner, Brenner maintains that the US had determined that it was not in its interests to cooperate.\textsuperscript{203} Enhanced capital mobility would allow further devaluation of the USD whilst, simultaneously, it would bolster the strength of private US financial capital in the international arena.\textsuperscript{204} Consequently, in February 1973 it prevailed on its economic rivals “to give up the Bretton Woods system…and go to the float.”\textsuperscript{205}

The underlying macroeconomic situation facing the main economic competitors of the US (and many other states, including New Zealand) now fundamentally changed. Essentially, from this point on, a given country’s capacity to govern their macroeconomy would be considerably impaired.\textsuperscript{206} While the closing of the gold window and the comprehensive scrapping of capital and exchange controls may appear to have freed international financial relations from the institutionalised ‘rigidities’ of the previous BWS, the reality was far different. For the vast majority of the world, the (subsequently

\begin{thebibliography}{99}

\bibitem{200} ibid
\bibitem{201} ibid.
\bibitem{202} ibid, 28.
\bibitem{203} ibid, 27; Helleiner 1994, 111-115.
\bibitem{204} Brenner 2002, 28.
\bibitem{205} ibid, 27. This perspective is challenged by Panitch and Gindin. See 2013, 145-146.
\bibitem{206} Dumenil and Levy 2013, 23. Although, as Panitch and Gindin observe, “how trapped central banks had become by precisely the rapid development of financial markets which they had encouraged” was already becoming evident by early 1970. See Panitch and Gindin 2013, 138.

\end{thebibliography}
established) DWSR acts as a macroeconomic snare. The large-scale private trading of “currencies and government bonds means that exchange rates and interest rates, two critical variables in the formulation of national macroeconomic policy, are determined in the context of global financial markets”, and, consequently, for the bulk of the world’s states, the formulation of macroeconomic policy is effectively subsumed to the vagaries of both IPFMs and US public policy.207

During the remainder of the 1970s, governments throughout the advanced capitalist world followed the example set by the US and proceeded to implement large-scale expansionary macroeconomic policy measures in response to the onset of stagflation. Freed from the policy constraints entailed by the BWS just as the US had been, states greatly expanded public expenditures and monetary policy was rapidly loosened. Adhering to the prevailing Keynesian economic orthodoxy, such measures were ostensibly aimed at simultaneously boosting flagging domestic demand and promoting business investment. It is worth noting that many states (most notably the UK) faced a situation of falling revenues as a result of declining growth combined with rising social expenditures due to rising unemployment. As a consequence, much of the increased public expenditures could not be readily paid for. This inevitably led to a significant expansion of public debt during the decade.

Thus, as indicated above, for many authors, the jettisoning of the USD-gold link (combined with subsequent efforts to enhance the power and mobility of private international financial capital and stamp out inflation) served to perpetuate the global hegemony of the US.208 Gowan asserts in The Global Gamble, for example, that the Nixon administration’s decision to close the gold window effectively constituted “a Faustian bid for world dominance.”209 It is of course important not to overplay “the coherence and clarity with which US

---

207 Gowan, 25.
209 Gowan,
policymakers responded to the crisis of the dollar which developed in the late-1960s (which Gowan may be guilty of doing). Nevertheless, the aggressive, unilateral action of the US in response to the dollar crisis, beginning in August 1971, does indeed appear to have helped ensure its ongoing dominance in world affairs through the key medium of international finance (even if this was not fully appreciated at the time).

However, while the immediate primary motivation of the US certainly appears to have been the preservation of US political and economic power in the international arena, the decision to detach the USD from gold was also in response to significant changes that had taken place in the underlying economy during the prosperous post-war era. In essence, business had become increasingly internationalised (a process that also entailed a significant parallel financialisation of global capitalism), and cross-border flows of private capital had expanded accordingly. This put increasing pressure on the institutional arrangements of the BWS which were ostensibly designed to restrict this very eventuality. These developments were also closely linked to the deeper historical dynamics of capitalism (outlined in Section One). As the war-ravaged economies of Western Europe and Japan were restored, it was the impulses deriving from mounting inter-capitalist competition that saw major firms expand abroad and seek out new means of enhancing their profitability.

Furthermore, while detaching from the dollar-gold link may have constituted a bold assertion of US power in the global economic system, it did “not provide a general solution to the [deeper] problems facing all the capitalist economies.” The major capitalist economies still faced a fundamental problem in the form of a system-wide crisis of profitability. It is to be observed that Keynesianism, in the form it was applied by numerous governments throughout the 1970s, did not appear to provide a viable solution. As, Brenner

---

210 Panitch and Gindin 2013, 13.
211 Ibid.
212 Ibid 2003, 49.
notes, the widespread “resort to Keynesian stimuli proved to be profoundly ambivalent in its effects.” Indeed, widespread application of Keynesian macroeconomic policies seemed to only make the economic situation worse by feeding a wage-price inflationary spiral. The prevailing macroeconomic situation - which combined a high rate of inflation and mass unemployment with a greatly reduced, if not negative growth rate - was contradictory to the wisdom of the existing Keynesian economic orthodoxy. Keynesianism had traditionally upheld that a trade-off always existed in public macroeconomic management between the level of inflation on the one hand, and economic growth and full-employment on the other. As a result, during the 1970s a serious crisis in the ideological hegemony of Keynesianism ensued.

In addition, for a system governing international financial relations based around a de-materialised USD and private financial capital to continue to operate effectively, other important political-economic changes were also required. First, as Harvey delineates, “for this system to work effectively, markets in general and capital markets in particular had to be forced open to international trade.” Second, the balance of power and interests within the bourgeoisie” would have to be shifted “from production activities to institutions of finance capital.” Finally, as discussed in the previous section, inflation would need to be curtailed (because confidence in the USD as the key currency in international financial relations was being rapidly eroded by ongoing devaluation). Ultimately, both a solution to the ongoing crisis of profitability and each of these necessary political-economic changes required for the effective operation of the DWSR were provided by the global spread of neoliberalism.

213 Brenner 2002, 34.
214 McNally 2011, 32.
215 Panitch and Gindin 2003, 49.
216 Harvey 2003, 62-63. See also Panitch and Gindin 2004 59-60; 2013, 119; Seabrooke, 105.
217 Harvey 2003, 63-63.
Neoliberalism

As a political ideology, neoliberalism derives from a mid-Twentieth Century revival of many of the ideas originally encapsulated in classical European liberalism. In accordance with classical liberalism, neoliberalism centrally enshrines individual freedom as its core value. From this it is maintained that the economic freedom of the individual should essentially be inviolable. The individual’s pursuit of their own rational, utility-maximising self-interest comprises “a profoundly political and moral force”, that is a fundamental prerequisite for the existence of a truly free and open society.

Neoliberalism can be readily distinguished from its classical predecessor, however, most notably by its treatment of the free market. Free market exchange is accorded considerably elevated significance within neoliberal doctrine. Indeed, as Treanor delineates, under neoliberalism the free market effectively becomes “an ethic in itself, capable of acting as a guide to all human action, and substituting for all previous held ethical beliefs.” Fundamentally, neoliberalism maintains that the free market operates as the central driving force of human freedom and “that the social good will be maximized by maximising the reach and frequency of market transactions.” Thus, as Harvey summarises,

neoliberalism is in the first instance a theory of political economic practices that proposes that human well-being can be best be advanced by liberating individual entrepreneurial freedoms and skills within an institutional framework characterised by strong private property rights, free markets, and free trade.
Neoliberalism combines its steadfast dedication to principles of individual economic freedom and the free market with a revival of many of the key assumptions of neoclassical economics that had prevailed as the intellectual orthodoxy prior to the emergence of Keynesianism. Most notably, it is assumed under neoliberalism that the free market is inherently efficient and self-regulating. As Roper observes, each of the major “schools of economic thought that have provided the intellectual foundations for neoliberalism” - including the influential Austrian and Chicago Schools especially - “accept the central neoclassical assumption that the economy is always tending toward general equilibrium with full employment of resources.”

With its core ideas upholding individual economic and market freedom (and also the inherent rationality of free markets) as paramount, extensive government involvement in the economy and society is anathema to neoliberalism. As Harvey observes, “neoliberal doctrine...[is] deeply opposed to state interventionist theories, such as those of John Maynard Keynes”, the author of the social democratic/corporatist orthodoxy that prevailed during the long economic boom that followed the Second World War. According to neoliberal theory, the state should only have a minimal role in the regulation of economic activity. This role should be focused on providing and maintaining those specific institutional arrangements that are necessary to ensuring the freedom of the individual. "Beyond these tasks”, however, “the state should

---

225 Roper 2005b, xvii.
226 However, despite often being characterised as being fervently anti-state in ideological terms, in practice neoliberalism has ultimately proven not to be particularly averse to state involvement in the economy. As Albo et al. point out, “rhetoric notwithstanding, [neoliberalism] has not meant a withdrawal of the state from regulating economic activity. Instead, it has signaled the institutionalisation of public policies and state regulation directed as increasing the power of the dominant capitalist firms in industry as well as financial markets and an enhanced role for markets in determining income distribution and public priorities.” See G. Albo, S. Gindin, and L. Panitch 2010, In and Out of Crisis: The Global Financial Meltdown and Left Alternatives (Oakland: PM Press), 27.
228 ibid, 64.
not venture.” Policy decisions involving state intervention in the market are to be avoided because they have an inherent tendency towards political bias. State interventions will inevitably be skewed by the efforts of vested interests seeking to maximise the economic benefits of state actions for themselves. In addition, state economic decision-making is also “bound to be wrong because the information available to the state…[can]not rival that contained in market signals.”

It follows from these guiding philosophical precepts that the key prescriptions of the neoliberal policy agenda are primarily oriented towards establishing and upholding private property rights, maintaining the rule of law, extending the reach of capitalist markets and market mechanisms (including into government and society), and establishing political and economic institutions capable of ensuring that free-market capitalism is able to operate without interruption (including across international borders). In his well-known treatise on the apparent merits of neoliberal globalisation *The Lexus and the Olive Tree*, Thomas Friedman provides the classic summary of the neoliberal policy agenda.

A country must either adopt, or be seen to be moving toward, the following golden rules: making the private sector the primary engine of its economic growth, maintaining a low rate of inflation and price stability, shrinking the size of its state bureaucracy, maintaining as close to a balanced budget as possible, if not a surplus, eliminating and lowering tariffs on imported goods, removing restrictions on foreign investment, getting rid of quotas and domestic monopolies, increasing exports, privatising state-owned industries and utilities, deregulating capital markets, making its currency convertible, opening its industries, stock and bond markets to direct foreign ownership and investment,

---

229 Ibid, 2.
230 Ibid.
231 Ibid.
233 Ibid, 2; Albo et al, 28.
deregulating its economy to promote as much domestic competition as possible, eliminated government corruption, subsidies and kickbacks as possible, opening its banking and telecommunications systems to private ownership and competition, and allowing its citizens to choose from an array of competing pension options and foreign-run pension and mutual funds.\(^2\)

**Global Neoliberalisation**

From the late 1970s onwards a strong and widespread global trend towards neoliberalism took place.\(^2\) Across the world a vast number of states implemented programmes of economic reform broadly in accordance with the neoliberal policy framework latterly codified in the so-called ‘Washington Consensus’.\(^3\) Consequently, facilitated in part by the decline and subsequent collapse of the USSR and its alternative command and control economic system, by the mid-1990s an almost complete international neoliberal order had been established.

It is important to observe that this was not the outcome of an internationally uniform process. Rather, as Harvey observes, the global spread of neoliberalism has been “a process of significantly uneven geographic development” and “on the world stage has evidently been a very complex process entailing multiple determinations.”\(^4\) However, while each individual case of national neoliberalisation was the unique product of the operation of a complex nexus of multiple weakly-acting causal pathways specific to the prevailing political-economic conditions of each respective state, each unique

---

\(^3\) Harvey 2005, 2.
\(^4\) The ‘Washington Consensus’ refers to a core set of neoliberal policies considered to be the bare minimum that countries needed to implement in order to achieve sustained economic growth. By the mid-1990s it had become established as the policy framework espoused by key international economic institutions such as the IMF and World Bank. See Steger and Roy, 19-20; J. Stiglitz 2003, *The Roaring Nineties* (New York: Norton).
\(^5\) Harvey 2005, 9.
case of neoliberalisation should also be viewed as forming a constituent part of a larger global neoliberalisation project.

In broad terms, the global neoliberalisation project has been characterised by a generalised dichotomy between the respective experiences of the states of the advanced capitalist world and the developing world. In the advanced capitalist world, the “drive towards neoliberalisation” was, for the most part, a voluntary process achieved through domestically-based democratic political projects.\(^{238}\) As Harvey outlines, “Neoliberalism…had long been lurking in the wings of public policy” in most Western liberal democracies, yet it largely “remained on the margins of both policy and academic influence until the troubled years of the 1970s.” \(^{239}\) At this point, to some extent motivated by the previously mentioned crisis in the “ideological hegemony” of social democratic Keynesianism, neoliberalism underwent its ascent to ideological and political prominence throughout the advanced capitalist world.\(^{240}\)

In the majority of cases, the rise of neoliberalism in advanced capitalist states was enabled by increasingly powerful pro-neoliberal blocs of social forces. These usually included, most prominently, private financial interests, conservative financial officials and transnational business interests, but also, more generally, domestic business interests, wealthy urban professionals and social conservatives (including in the US specifically, the Christian right).\(^{241}\) As Harvey again outlines, “sufficient popular consent” to formally legitimise the shift to neoliberalism was generated by the exertion of significant influence on

\(^{238}\) Harvey 2005, 11. For a more detailed account of the “construction of consent” in the advanced capitalist world, see ibid, 39-63.
\(^{239}\) Ibid, 19, 22. It can be noted in New Zealand’s case, for example, that neoliberal ideas were becoming pervasive in the Treasury in particular from at least as early as the 1960s. See M. McKinnon 2003, *Treasury: The New Zealand Treasury 1840-2000* (Auckland: Auckland University Press). “The troubled years of the 1970s” are explained in detail below.
behalf of these social bases through a number of key “channels.” “Powerful [neoliberal] ideological influences” were, for example, “circulated through the corporations, the media,... the numerous institutions that constitute civil society – such as the universities, schools, churches, and professional associations”, and the establishment of “various well-financed think-tanks” like the British Institute of Economic Affairs and the American Heritage Foundation.

As a result, from the late 1970s onwards, democratic preference for neoliberalism grew significantly amongst the citizens of the wider advanced capitalist world. This culminated in the consolidation of neoliberalism as the new “orthodoxy regulating public policy...in the advanced capitalist world.”

This was initially signaled by the election of the defining neoliberal governments of Margaret Thatcher in the UK in May 1979, Ronald Reagan in the US in the following year, and a pattern of similar electoral outcomes unfolding across the advanced capitalist world during the 1980s. Later, the ideological ascent of neoliberalism appeared to be confirmed by the collapse of the Soviet Union (USSR) in 1991, an event which effectively brought to an end any other major alternative economic model (with the possible exception of China).

The process of financialisation that, as we have seen, played an important role in the decision of the US to detach from the BWS in the early 1970s was also causally significant to the broader shift to neoliberalism in the advanced capitalist countries that followed. Indeed, it has been asserted that “most, if not all, analysts on the left now agree that ‘neoliberalism’ is the

---

242 Harvey 2005, 40.
243 ibid, 22, 40.
244 ibid, 22.
245 ibid, 2005, 22, 26, 58; Helleiner 1994, 170.
ideological expression of the reassertion of the power of finance.” As outlined in the previous chapter, business is cross-cut by various fractional divisions, and the balance of power between these fractions can shift over time. The ongoing process of financialisation within global capitalism appears to have eventually resulted in such a shift. The research of Krippner suggests that around the mid-1970s finance became the ascendant power within capital – at least in the US. It is of course important not to overplay the extent that private financial interests were able to dictate subsequent policy decisions, but neoliberalism nevertheless appears to be, to some extent, an ideological response to an underlying “shift in gravity of economic activity from production to finance.”

Dumenil and Levy have developed what perhaps comprises the most influential thesis along such lines. Centrally, they argue that while neoliberal “ideology was a crucial political tool in the establishment of neoliberalism”, “ideology was not the engine of the neoliberal revolution.” Instead, they maintain, what took place essentially constituted a sort of “financial coup.” In their widely cited work The Roots of the Neoliberal Revolution they empirically outline how the onset of stagflation had posed a serious economic threat to the position of finance capital especially (as well as what they refer to as the ‘ruling classes’ more generally). Subsequently they argue that, in response to this

---

249. Foster and Magdoff, 77. As Brenner observes, prior to the neoliberal turn “finance and manufacturing found common ground” in many countries, thus the shift in the intra-capital balance of power should not necessarily be viewed as finance asserting control over the state in opposition to the interests of productive capital. See Brenner 2002, 36.
apparent existential threat, “finance took over the state and institutions of the Keynesian compromise”, thereby effectively establishing “a second financial hegemony.”

In direct contrast to the experience in the advanced capitalist world, a major driver of neoliberal restructuring in the developing world has been the coercive imposition of neoliberal state apparatuses by external forces. This dynamic is particularly evident in the neoliberalisation processes experienced in Latin America (although, now, increasingly reversed and challenged), East Asia, Africa, and Central and Eastern Europe. Externally imposed neoliberalisation has generally been achieved in two main ways.

First, neoliberal institutional and policy arrangements have often been foisted directly onto other nations by the US via military means. This method was employed, most prominently, in the first historical case of imposed neoliberalisation in Chile in 1973. On 11 September, 1973, Augusto Pinochet led a military coup, overthrowing the democratically-elected, but left-leaning, government of Salvador Allende. Pinochet was backed by a body of domestic business elites, but also received significant direct support from major US corporations, the CIA, and US Secretary of State Henry Kissinger. Following the coup, violent repression of popular leftist social and political organisations was immediately undertaken and a group of economists trained at the University of Chicago (thus quite literally members of Milton Friedman’s previously mentioned ‘Chicago School’) were brought in to ‘revive’ the Chilean economy. Working in partnership with IMF, this group of economists (then referred to as ‘monetarists’) undertook a major project of economic

252 Dumenil and Levy 2011, 17.
253 Harvey 2003b, 133; Foster and Magdoff, 75. There has undoubtedly been a very prominent direct imperial element underlying the global spread of neoliberalism. See, for example, Harvey 2003, The New Imperialism (Oxford: Oxford University Press). However, as indicated by the prominent domestic element involved in Chile’s historic shift to neoliberalism, it is not just a case of external imposition. See Harvey 2005, 9.
254 Ibid, 7.
255 Ibid, 7-8.
restructuring closely adhering to pure neoliberal policy prescriptions. Most prominently, the labour market was deregulated, import protections were lifted, nationalisations were reversed, public assets were privatised, the primary sector of the economy was opened up to untrammeled private and foreign exploitation (with the notable exception of the crucially important copper industry), welfare provision was privatised, and controls on FDI, trade and the repatriation of profits were greatly reduced.

Many similar processes of neoliberalisation were experienced in developing nations during the 1970s and 1980s. As part of its so-called ‘dirty war’ foreign policy strategy, for example, the US state backed the emergence of a number of brutal right-wing military regimes in Central America (and also in Argentina) and prompted them to implement neoliberal reforms. Furthermore, it is important to note that militarily imposed neoliberalisation was an ongoing phenomenon during the 2000s. This point is most cogently illustrated by the US’s imposition by force of a neoliberal state apparatus on Iraq in the months following its ‘pre-emptive’ invasion in 2003. As Harvey outlines, despite it overtly contravening the principles of both the Geneva and The Hague conventions, beginning on 19 September 2003, the head of the US-led Coalition Provisional Authority, Paul Bremer, initiated a comprehensive program of neoliberal reforms in Iraq. This applied to all sectors of the Iraqi economy (except for oil) and included, most prominently: complete privatisation of all public enterprises (“getting inefficient state enterprises into private hands is essential for Iraq’s economic recovery”, claimed Bremer);

---

256 McNally 2011, 34. Monetarism is discussed in more detail in Chapter Three.
257 Harvey 2005, 8.
258 This issue is covered in J. Perkins 2008, The Secret History of American Empire: The Truth About Economic Hitmen, Jackals, and How to Change the World (London: Penguin). Official documents relating specifically to the ‘dirty war’ era of historical US foreign policy were only just being declassified as this thesis was being submitted. Consequently, our understanding of this aspect of US foreign policy and global neoliberalisation should soon become more fully developed.
260 Harvey 2005, 6-7.
providing foreign ownership rights to Iraqi businesses; allowing unhindered repatriation of profits; opening Iraqi banks to foreign control; providing for the national treatment of foreign firms; the dismantling of external trade tariffs; the strict regulation of the labour market (legally restricting unionisation and strike activity); and the introduction of a highly regressive ‘flat-tax’ system.262

The second main way in which neoliberalism has been externally imposed on the developing world has been through the exploitation of financial crises.263 This was, for example, a key instrument in bringing about a wave of neoliberal domestic transformations in Latin America in the 1980s.264 As was discussed in the previous section, the 1973 oil crisis generated a glut of petrodollars for OPEC members and, at US insistence, most of these excess funds were recycled through Wall Street investment banks. The dispersal of these funds by Wall Street was heavily concentrated amongst a small group of credit-hungry Latin American and East Asian economies. Indeed, Theberge notes that, via this process Latin America effectively quadrupled “its external debt from $75 billion in 1975 to more than $314 billion in 1983.”265 The loans made to these countries, however, were denominated in the now de-commodified USD of the DWSR. This left the recipient countries increasingly vulnerable in the context of the rising US interest rates associated with the previously mentioned ‘Volcker Shock’. Financial markets chasing expanding interest rate differentials between the US and other countries drove up the

262 Harvey 2006, 6; Klein 2006, 345.
263 It is worthwhile noting, however, that exploitation of financial crises to coercively impose neoliberalism is by no means an exclusive experience of the developing world. This is illustrated by the respective experiences of Greece in the wake of the GFC and of Puerto Rico in 2016.
264 The exploitation of a major financial crisis was also the key means of bringing about another major wave of neoliberal reform in East and South-East Asia (and elsewhere) following the 1997-98 East Asian Crisis. Further, a range of authors have observed that “the axis binding together Wall Street, the US Treasury, and the international financial institutions” (what I have termed the DWSR), actually “promotes what has become one of the chronic features of the neo-liberal era – the ‘emerging market’ financial crash.” See Callinicos 2003, 30-31. Also, Gowan, 23-25; Harvey 2003, 150, 156. Thus, Gowan (and others) argue that the US state has consistently exploited key features of the DWSR “as a formidable instrument of economic statecraft to drive forward...neo-liberal domestic transformations”, particularly in the developing world. See Gowan, 23, 25; Harvey 2003, 129.
value of the USD and, simultaneously, the debt and interest burdens of those countries who had borrowed significant funds. Consequently, beginning with Mexico in August 1982, a host of overburdened Latin American countries were pushed into default on their loans. This left the governments concerned in the unenviable position of having to turn to the IMF for debt relief.\textsuperscript{266}

The IMF was subsequently deployed to organise the rescheduling of the debt. As Pastor observes, throughout the remainder of “the decade, Fund missions shuttled from country to country” across Latin America negotiating debt relief.\textsuperscript{267} However, debt relief was only provided in exchange for the subject governments agreeing to undertake a radical programme of so-called ‘structural adjustment’; the adoption and implementation of the comprehensive programme of neoliberal policy reforms of the Washington Consensus.\textsuperscript{268}

Thus, throughout most of the advanced capitalist world the historic shift to neoliberalism was largely a voluntary process. Neoliberal governments were generally installed into power via democratic processes. In contrast, the experience of neoliberalisation for much of the Global South was strongly characterised by elements of external coercion. As Dumenil and Levy summarise:

\begin{quote}
the international neoliberal order – known as neoliberal globalisation – was imposed throughout the world, from the main
\end{quote}

\begin{footnotes}
\item[266] Gowan, 33-34.
\item[267] M. Pastor 1989, “Latin America, the Debt Crisis, and the International Monetary Fund”, \textit{Latin American Perspectives}, Vol. 16, no 1 (Winter), 79.
\item[268] Ibid. As Harvey points out, in comparison to the situation under the BWS, the role of the key transnational institutional bodies for guiding economic management – the IMF and the World Bank (WB) – has evolved under the DWSR. They have effectively become principal “centres for the propagation and enforcement of ‘free market fundamentalism’ and neoliberal orthodoxy” (Harvey 2005, 29). See also Foster and Magdoff 75; J. Stiglitz 2002, \textit{Globalization and its Discontents} (New York: Norton). It is primarily for this reason that a number of authors (including Callinicos, Harvey, Wade, and Veneroso) incorporate the IMF more prominently within their respective accounts of what I refer to as DWSR. In my view, however, the difference between Gowan’s DWSR and a variant of Wade’s ‘Wall Street–Treasury – IMF Complex’ is largely one of semantics, not substance. Compare with my own, for example, the account provided in R. Wade 2003, “The Invisible Hand of American Empire”, \textit{Ethics and International Affairs}, Vol. 17, no.2, 77. Also note that, for Callinicos, this particular description “fits...the contemporary American hegemony like a glove.” See Callinicos 2009, 189.
\end{footnotes}
capitalist countries of the centre to the less developed countries of
the periphery, often at the cost of severe crises as in Asia and
Latin America during the 1990s and after 2000. As in any stage of
imperialism, the major instruments of these international power
relations, beyond straightforward economic violence, are
corruption, subversion, and war. The main political tool is always
the establishment of a local imperial-friendly government. The
collaboration of the elites of the dominated country is crucial, as
well as, in contemporary capitalism, the action of international
institutions such as the North Atlantic Treaty Organisation
(NATO), the International Monetary Fund (IMF), the World Bank
(WB), and the World Trade Organisation (WTO). 269

Neoliberal Economic Recovery and the DWSR

A common refrain among radical political economists is that the great
structural crisis of capitalism of the 1970s that, as we have seen, resulted from
decreasing corporate profitability and over-accumulation has yet to be
resolved. 270 While their views and subsequent arguments often vary
significantly, centrally, as Callinicos (who includes himself in this group)
oberves, “all these theorists affirm the following: global capitalism has yet to
exit from the era of economic crisis into which it entered in the late 1960s.” 271
Foster and Magdoff, for example, state that “the ‘golden age’ of prosperity”
following World War II “turned…into a ‘leaden age’”, and that “this slowdown
of stagnation has now persisted for four decades, and has only gotten worse
over time.” 272 Similarly, Brenner argues that “the sharp fall in manufacturing
profit rates” in the late 1960s ultimately heralded nothing less than an “epochal
shift from long expansion to long stagnation for the world economy.” 273

269 Dumenil and Levy 2011, 9.
270 This perspective has been advanced
271 Callinicos 2009, 17. Callinicos advanced an argument along these lines in Bonfire of Illusions.
272 J.B. Foster and F. Magdoff 2009, The Great Financial Crisis: Causes and Consequences (New York:
Global neoliberalisation, however, was not simply some sort of “utopian project to realise a theoretical design for the reorganisation of international capitalism.” Rather, it fundamentally constituted “a political project to re-establish the conditions for capital accumulation.” As McNally argues, “in truth, [it] was a pure and simple program for restoring corporate profits – nothing more, nothing less”, and it was ultimately successful. Following the widespread fall in profit rates which, as we have already seen, set in sometime during the late 1960s, profit rates continued to fall throughout much of the 1970s. Then, from 1982 to 1997, “the average rate of profit rose persistently” throughout the advanced capitalist core. The onset of the East Asian financial crisis appears to have coincided with the rate of profit once again entering into a downward trajectory. As McNally observes, this downward trajectory “seems to have reversed for a time after 2001.”

The recovery of profit rates under neoliberalism underpinned a period of relatively strong economic expansion. Three distinct phases of economic growth can be distinguished during the era of global neoliberalism, with each of these phases separated by a brief (but often sharp) economic downturn. The first, beginning in 1982, ended in 1990. This was followed by a second, slightly longer growth phase – popularly dubbed ‘the roaring nineties’ in the US - that lasted from 1991 until 2000. The final phase of growth ran from after the bursting of the so-called dot.com bubble in 2001 until the onset of the GFC in

---

274 Harvey 2005b, 19.
275 Ibid; Panitch and Gindin 2003, 51.
276 McNally 2011, 25-26; Dumenil and Levy 2011, 1, 55.
277 Ibid, 49. The data drawn on here relates only to the US, Japan, and Germany. We can reasonably expect that the recovery of the profit rate in New Zealand was delayed due to its comparatively late turn to neoliberalism.
279 McNally 2011, 41.
The global economy did not, of course, generally witness a return of the historically elevated growth rates that had characterised much of the long post-war boom. But it is nevertheless evident that “the system underwent a sustained wave of expansion” during the period from 1982 to 2007. Furthermore, as can be seen from Table 2.3 (above), this expansion compares well against other major phases in the history of global capitalism.

The global spread of neoliberalism also provided the means for the effective curtailment of inflation. Indeed, it has been suggested that “the reduction and control of inflation is the only systematic success neoliberalisation can claim.” After being rampant throughout the course of the 1970s, high system-wide inflation has not reappeared since the neoliberal turn. Following on from Figure 2.1 (above), Figure 2.3 shows the rate of inflation across the advanced capitalist world during the period from 1984 to 2011. As can be seen, following the implementation of the Volcker Shock, global inflation was progressively brought under control. Over the course of the 1980s and up until the late-1990s, inflation fell more or less continuously (minor temporary increases notwithstanding). Subsequently, throughout the first decade of the 2000s, a relatively low level of inflation was effectively maintained.

---


281 Although China routinely exceeded it.


283 Albo et al, 51.

284 Harvey 2005, 156.

285 It is worth noting also that inflationary pressures were so persistently reduced following the onset of the GFC that widespread deflation emerged as a very real threat to the global economy.
Figure 2.3) Inflation in the Advanced Capitalist Economies during the Neoliberal Era


By greatly increasing real interest rates, the imposition of price stability privileged lenders. This contributed to the great expansion of processes of financialisation that have been a prominent feature of restored neoliberal capitalism. In broad terms, financialisation can be accurately viewed as referring to “the increasing role of financial motives, financial markets, financial actors and financial institutions” in the operation of contemporary political economies. Financialisation in contemporary capitalism has primarily involved significant growth in both “the comparative size and profit rate of the

---

286 As with Figure 2.1 previously, the OECD is again here used as a proxy for the advanced capitalist world.
287 Epstein, 4.
288 As noted earlier, financialisation is a somewhat ambiguous term. It is employed by a range of authors to describe a host of different processes at work in contemporary capitalist economies and liberal democratic societies. For a useful discussion see N. van der Zwan 2014, “State of the Art: Making Sense of Financialisation”, Socio-Economic Review, Vol. 12, 99-103.
financial sector.” Empirical evidence demonstrates that within the OECD, financial institutions and the share of overall profits accruing to them have grown considerably. Financialisation in contemporary capitalism has also involved significant changes in virtually all other sectors of the economy. Non-financial corporations are increasingly involved in (and often reliant on) financial activities as part of their day-to-day business operations, financial motives have become central to their corporate governance models via “the imposition of managerial criteria such as the creation of value for the shareholder”, and “the financial component of management” has also expanded. Furthermore, financialisation has entailed an increasing role for finance in everyday life. This notably includes the increased involvement of individuals in financial markets as both savers and consumers.

The tendency to privilege the interests of financiers over the creation of an environment immediately conducive to productive investment under neoliberalism also provided for the extensive growth in both the size and depth of IPFMs. As Epstein observes, “in the last thirty years, international financial transactions have grown by leaps and bounds.” International private financial flows constituted by FDI, international bank lending, international bond issues, international equity trading, derivatives and futures trading, and international currency trading have all increased significantly since the inauguration of the neoliberal era. As can be seen from Table 2.6, for example, annual FX market turnover has undergone immense, historically unprecedented growth. Moreover, as Table 2.7 emphasises, in recent years, in terms of the key FX market especially, this IPFM expansion has continued unchecked. As the BIS

---

290 Dumenil and Levy 2011, 35.
291 Epstein, 4
292 Dumenil and Levy 2011, 35. See also Krippner 2005; Crotty 2005.
293 Van der Zwan, 102.
294 Ibid.
295 Epstein, 3.
296 Callinicos 2003, 33; Held et al, 202-209.
reports, “turnover in the foreign exchange market has continued to expand rapidly in recent years.” 297 Between 2010 and 2013 FX turnover across all instruments increased on average by around 35% per annum. This easily eclipsed the 19% average yearly increase between 2007 and 2010. 298 In addition, trade in exchange-traded derivatives continues to increase (although at a decidedly more sedate pace). Average daily turnover in exchange-traded derivatives increased from US$155 billion to US$160 billion between 2010 and 2013. 299

**Table 2.6) Estimated Global Annual FX Market Turnover during the Neoliberal Era (US$trillion)**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Turnover (US$trillion)</td>
<td>17.5</td>
<td>75</td>
<td>190</td>
<td>252</td>
<td>298</td>
<td>458</td>
<td>438</td>
<td>694</td>
<td>1163</td>
<td>1449</td>
<td>1951</td>
</tr>
</tbody>
</table>

Source: BIS 2007, 4; 2013, 3, 9; Held et al, 202-211.

**Table 2.7) Average Daily Global FX and Derivatives Trading, 1998 to 2013 (US$billion, at April 2013 exchange rates)**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>FX Market Turnover</td>
<td>1718</td>
<td>1500</td>
<td>2036</td>
<td>3376</td>
<td>3969</td>
<td>5345</td>
</tr>
<tr>
<td>Exchange-Traded Derivatives</td>
<td>11</td>
<td>12</td>
<td>26</td>
<td>80</td>
<td>155</td>
<td>160</td>
</tr>
</tbody>
</table>

Source: BIS 2013, 9.

The massive growth of IPFMs during the neoliberal era coincided with a significant expansion of their geographic reach. To paraphrase from the *Communist Manifesto*, no longer even partially curtailed by BWS capital and exchange controls, during the neoliberal era private financial capital has spread out over virtually the whole surface of the globe, establishing connections

---

298 BIS 2013, 4.
299 Ibid, 9.
everywhere.\textsuperscript{300} As the BIS has comprehensively documented, the “breadth and depth of links between mature and emerging financial markets”, in particular, have increased considerably during the neoliberal era.\textsuperscript{301} While global financial flows remain heavily concentrated between the major advanced capitalist economies, international financial institutions have also rapidly established themselves as important, if not dominant, actors in the domestic financial systems of most so-called “emerging markets.”\textsuperscript{302}

Thus, in addition to delivering a sustained global economic recovery, the global spread of neoliberalism also provided the key bases necessary for cementing the financial dominance of the US globally including, most notably, the ongoing hegemony of the USD.\textsuperscript{303} Intra-capital power was shifted decisively towards finance across the advanced capitalist world. Simultaneously, cross-border capital flows were progressively freed from constraints. In essence, then, the DWSR developed symbiotically with the so-called ‘Washington Consensus’, and global neoliberalisation ultimately provided the necessary regulatory infrastructure for the effective “diffusion of [US] power through the dollar.”\textsuperscript{304}

In his seminal work \textit{The New Imperialism}, Harvey outlines that the simultaneous deepening and expansion of IPFMs (outlined above) has allowed the deployment of “an unholy alliance between state powers and the predatory aspects of finance capital” as “the cutting edge of a ‘vulture capitalism’ dedicated to the appropriation and devaluation of assets.”\textsuperscript{305} This process is referred to as “accumulation by dispossession.”\textsuperscript{306} In broad terms, accumulation by dispossession has tended to entail IPFMs, backed by the monetary

\begin{footnotesize}
\begin{enumerate}
\item Marx and Engels, 46-7.
\item Ibid.
\item Foster and Magdoff, 75
\item Seabrooke, 68,
\item Harvey 2003a, 78.
\item Ibid. For a detailed account of what is meant by ‘accumulation by dispossession’ see 2003b, 137-182.
\end{enumerate}
\end{footnotesize}
institutions of the US Government and the IMF, exploiting foreign debt to externally impose successive major financial crises “upon one sector or upon a territory or whole territorial complex of capitalist activity.”307 A stock of devalued assets is thereby created, which can then be appropriated by US-dominated international capital. The quintessence of this key dynamic within contemporary global capitalism is captured most cogently by Wade and Veneroso’s discussion of the 1997-98 East Asian financial meltdown:

...there is no doubt that Western and Japanese corporations are the big winners...The combination of massive devaluations, IMF-pushed financial liberalisation, and IMF-facilitated recovery may even precipitate the biggest peacetime transfer of assets from domestic to foreign owners in the past fifty years anywhere in the world, dwarfing the transfers from domestic to US owners in Latin America in the 1980s or in Mexico after 1994.308

At this point it is perhaps worthwhile to briefly consider that, for a large number of authors, the extensive financialisation that has taken place under global neoliberalism - combined with the emergence of ‘accumulation by dispossession’ as a major feature of contemporary capitalism - is indicative of a deeper structural change in the underlying nature of contemporary capitalism.309 Exemplary of this is Krippner who has argued that since the mid-1970s “a pattern of accumulation” has emerged “in which profit making occurs increasingly through financial channels rather than through trade and commercial production.”310 As noted by Van der Zwan, the broader “regime of accumulation” thesis (as she terms it) is most commonly linked to the so-called Regulation School.311 Key Regulationist authors such as Aglietta and Boyer have

307 Ibid, 150.
308 Wade and Veneroso, 3-23.
309 Epstein, 4; Van der Zwan, 100.
310 G. Krippner 2004, “What is Financialisation?” mimeo, Department of Sociology, UCLA.
311 The genesis of the Regulation School (or really schools, as there are multiple approaches within the tradition) is to be found in Aglietta’s (1973) work, A Theory of Capitalist Regulation: The US Experience (London: Verso). While initially based on Marxist ideas, the work of key authors within the Regulation
suggested that a finance-led, ‘post-Fordist’ capitalist growth regime has emerged and matured during the era of global neoliberalism. However, not entirely dissimilar arguments have also been advanced by others, including many Marxists and post-Keynesians. A common theme amongst Marxist analyses of financialisation in particular is that the shift from industrial to finance capitalism ultimately stems from an ongoing decline of the ‘real’ productive economy. Due to the persistence of stagnation in the productive sectors of the economy a sort of parasitic ‘rentier’ economy has emerged that primarily relies on asset bubbles and speculation for the generation of profits. In essence, the economy “as a whole”, to paraphrase Foster and Magdoff, has increasingly taken on “the colouration of speculative finance.”

The overarching thesis of this literature – that financialisation reflects the fact that “something has actually radically changed in contemporary capitalism”

---


313 Van der Zwan, 101.


316 J.B. Foster and F. Magdoff 2009, 67.
– has considerable value.\textsuperscript{317} It has, after all, proved to constitute a useful theoretical basis on which to develop numerous crucial insights into the inner workings of the advanced capitalist economies under global neoliberalism.\textsuperscript{318} However, as Boyer quite usefully reminds us, we must remain mindful of the fact that ultimately “finance is an element in, but not the whole of, this complex emerging regime.”\textsuperscript{319} That is, the revival of capitalism during the neoliberal era has involved much more than simply an expansion of finance, predatory raiding, and asset-price speculation.\textsuperscript{320} To be sure, these have been increasingly prominent economic elements and, as Panitch and Gindin relate, there is no doubt that financialisation processes have effectively “blurred the old lines between financial and non-financial activities” during the neoliberal era. But finance and industry nevertheless retain their distinct characteristics.\textsuperscript{321} Furthermore, while the so-called ‘FIRE economy’ has expanded significantly, industry and commerce has been far from stagnant.\textsuperscript{322} Indeed, in many respects they have veritably thrived under neoliberalism. Global neoliberalisation has, after all, been a catalyst for an acceleration of the globalising tendencies within capitalism that, as we have seen, were already advancing steadily under Keynesianism and the BWS. Cross-border investment underwent a massive expansion. Growing at an annual rate of 12%, the global stock of FDI rose from just 6.5% of GDP in 1980 to 32% of GDP in 2007.\textsuperscript{323} Simultaneously, during the period from 1980 to the onset of the GFC in 2007, global trade underwent a massive expansion. Growing at an annual rate of 8.7%, world trade as a share of GDP increased from 32% to 57%.\textsuperscript{324} Together, these dynamics reflect a massive geographic restructuring of capitalism which has resulted in the emergence of

\textsuperscript{318} Lapavistas 2011, 617.
\textsuperscript{319} Boyer 2000, 111.
\textsuperscript{320} Van der Zwan, 105.
\textsuperscript{321} Panitch and Gindin 2013, 290
\textsuperscript{322} Kelsey 2015.
\textsuperscript{323} Panitch and Gindin 2013, 284.
\textsuperscript{324} Ibid.
what is now widely considered to be a truly “global capitalism.” It is important to observe that this “expansion of trade and investment worldwide would have been impossible in the absence of the parallel development of banking activity and the globalisation of financial mechanisms.”

In essence, reflecting the shift in the intra-capital balance of power that, as we have seen, appears to have occurred sometime during the 1970s, it is only logical that many key aspects of the neoliberal policy agenda distinctly favour the interests of private financial capital. The seemingly unbending focus of neoliberal macroeconomic management on achieving and subsequently maintaining a low stable level of inflation, for example, is clearly to the advantage of financiers. But states have not just implemented policies that only favoured finance during the neoliberal era. They have also implemented policies favourable to private enterprise more broadly. Such things as labour and capital market liberalisation, deregulation, and privatisation, served to systematically increase the underlying rate of exploitation, create new markets, and open up entirely new geographic spaces to capital penetration. In-effect, states took responsibility for implementing a policy agenda that successfully mobilised a series of major counter-tendencies to the falling rate of profit that, as we have seen, became manifest from the late 1960s onwards. On this basis, the rate of profit was temporarily restored, and “a volatile but nonetheless real process of sustained capitalist expansion” followed.

This is not, of course, to deny the “massive expansion of finance in global accumulation”, or its overall importance to the restoration of corporate

---

325 Panitch and Gindin 2013.
326 Dumenil and Levy 2011, 118.
327 This is primarily because inflation inherently erodes stored value, which is essentially the form that finance capital takes.
328 As McNally (2011, 38) points out, it is important to note that neoliberal “policies have frequently produced more robust rates of capital accumulation in select regions outside the core, while contributing to slower rates of growth in the dominant economies.” The most obvious example of this is the case of Japan during the 1990s.
329 McNally 2011, 36.
profitability and economic growth. After all, the economic growth wave of 2001 to 2007 was based in considerable measure on the inflation of a series of speculative real estate bubbles in the US and elsewhere following a loosening of monetary policy by the US Federal Reserve. Nor, indeed, is it to entirely repudiate the possibility that a fundamental change in the regime of accumulation may have occurred. Rather it is to highlight a necessary empirical corrective to the apparent pervasive overstatement of the extent to which finance has come to dominate contemporary political economies. The typical counter-position of stagnating or declining production and thriving finance within many political economy explanations of neoliberal financialisation thoroughly misrepresents the actual historical nature of neoliberal capitalism.

---

330 Panitch and Gindin 2013, 284. In-fact, Panitch and Gindin (2010, 50) observe that “the further growth of financial markets increasingly characterised by competition, innovation and flexibility was central to the resolution of the crisis of the 1970s.”

331 Alan Greenspan’s loosening of monetary policy in the early 2000s is a particularly cogent example of the US state taking on the role of ‘capitalist-in-chief’ in order to mobilise an effective countervailing tendency as corporate profitability once again began to slump. As we shall see later in the thesis, due to the institutional arrangements of the DWSR, the effects of this credit expansion were felt in many economies around the world.

332 McNally 2011, 88.

333 Albo et al, 33.
Conclusion

This chapter has argued that the process popularly referred to as ‘globalisation’ is fundamentally rooted in the expansive dynamics of the capitalist mode of production. Centrally, the dynamic of competitive accumulation that to a significant extent defines the capitalist system, produces an inherent tendency within capitalism for the rate of profit to fall over time. This inherent predisposition, in-turn, periodically generates systemic crises that profoundly shape the dynamics of globalisation. The crises inherent to the system primarily serve to promote a major ongoing process of geographic reorganisation that is ultimately oriented towards, at least temporarily, restoring the system-wide average rate of profit.

In addition, it has also been argued that over the last several decades the prominent financial aspect of globalisation has taken place under the auspices of the DWSR. The DWSR has functioned to firmly entrench the US into a position of dominance in the realm of international financial affairs. Based around two main mutually reinforcing pillars – a US dollar standard and the centrality of US-dominated IPFMs in international monetary relations – the DWSR has served to shift the basis of the US’s global hegemony into the very structure of the international financial system. For the majority of the world, DWSR integration has effectively meant the virtual surrender of the formulation of domestic macroeconomic policy to the vagaries of IPFMs and US policy decisions.

Given the considerable advantages that accrue to the US through the DWSR arrangements, it is clear that they were established at least partly as a means of sustaining the political and economic power of the US in the international arena. However, they were not formulated entirely unilaterally, or in historical isolation. Rather the DWSR initially emerged in response to significant economic developments that, while beginning earlier, became increasingly pronounced in the early 1970s. At this time economic growth
slowed considerably in the US and elsewhere as the rate of profit across the advanced capitalist world fell precipitously and a generalised crisis of over-accumulation set in. Simultaneously, the increasingly internationalised and financialised nature of international economic activity (including the emergence of the unregulated Eurodollar market) placed what ultimately constituted unbearable pressure on the existing BWS arrangements. In order to counter these pressures, the US asserted its hegemony by abandoning the official link between the USD and gold, and subsequently overseeing the cancellation of the BWS capital and exchange controls. These moves temporarily alleviated some of the mounting economic and financial pressures being exerted on the US, but did not provide a viable long-term solution to the problems gripping both the US as hegemon and the rest of the advanced capitalist economies. Ultimately, the solution was provided by the geographically-disparate process of global neoliberalisation. The global neoliberalisation project formed the cornerstone of a US-sponsored, finance-led business counter-offensive aimed at the reinvigoration of global capitalism (which was largely successful). Simultaneously, the global spread of neoliberalism also provided the key political-economic changes required for the ongoing viability of the DWSR as a system governing international monetary and financial relations.
Introduction

In the previous chapter, it was argued that what is popularly referred to as ‘globalisation’ is, in-fact, a product of the operation of a tendency towards expansion inherent within the capitalist mode of production. It was also argued that the prominent financial aspect of contemporary globalisation – of which, the influence on New Zealand’s political system is the focus of this thesis - has taken place under a US-dominated global financial structure referred to here as the Dollar-Wall Street Regime (DWSR). Under the DWSR, extensively liberalised and highly deregulated international private financial markets (IPFMs) dominate international monetary relations, with domestic-level macroeconomic policy formulation largely subsumed to the vagaries of these IPFMs and the financial decision-making undertaken by the institutions of the US state. The DWSR initially emerged in response to accelerating economic processes of internationalisation and financialisation that critically undermined the efficacy of the existing BWS, and the near contemporaneous onset of a major global economic downturn. Subsequently, it became fully developed and expanded in geographic scope through the geographically uneven, yet nevertheless comprehensive, global shift to neoliberalism.
This analysis has significant implications for our understanding of how major global financial forces influence developments within New Zealand’s domestic political economy. Primarily, this is because from 1984 onwards, New Zealand followed the international trend towards neoliberalisation. Indeed, New Zealand’s historic shift to neoliberalism has been widely upheld as constituting a model of such speed and purity as to warrant international emulation.\(^{334}\) So what, then, gave rise to neoliberalisation in New Zealand? It is this issue that will be the primary focus of this chapter.

The discussion will begin with a brief overview of the political circumstances that prevailed during the key period of neoliberal reform between 1984 and 1990. It will then move on to provide a more detailed account of the program of financial deregulation and ‘monetarist’ macroeconomic management that was both at the very forefront of New Zealand’s neoliberal reforms and also effectively resulted in New Zealand’s full integration into the DWSR. Following this, each of the groupings of actors that played a key role in the initial promotion and subsequent shift to neoliberalism will be discussed. These are: the cabinet under the Fourth Labour Government; the government’s most important institutional advisors, the Treasury and the Reserve Bank of New Zealand (RBNZ); and business. Finally, existing accounts of the broader set of changes within New Zealand’s political economy that underpinned the progress of the overt political project will be outlined.

In anticipation, it will be argued that like much of the rest of the advanced capitalist world, New Zealand’s neoliberalisation was also the outcome of a distinctly domestic political project. It will also be argued that, fundamentally, the process of neoliberalisation in New Zealand was simultaneously moulded by a broader set of underlying political-economic developments including: the end of the post-war economic boom and the onset

of ‘stagflation’; a shift in the societal balance of power in favour of business; and a major shift in the prevailing international intellectual orthodoxy in the realm of economics from Keynesianism to neoliberalism during the 1970s.
3.1) The Fourth Labour Government: A Political Overview

The key point in New Zealand’s historic shift to neoliberalism was the election of the Fourth Labour Government to power on 14 July 1984. The Labour Party received 42.4% of the total votes cast at the election and secured a powerful parliamentary majority of 56 seats. The incumbent National Party, in comparison, received 35.7% of the vote and 37 seats. Social Credit, the only other party to gain representation at the election, secured 2 seats on the back of receiving 7.6% of the vote. As Roper outlines, Labour’s victory was aided significantly by the performance of the newly formed New Zealand Party. Founded by property magnate Sir Robert Jones, the New Zealand Party attracted 12.3% of the total vote (but no seats) at the 1984 election. It was able to achieve this primarily by securing “the support of traditional National voters who were alienated by [incumbent National Prime Minister Robert] Muldoon’s interventionism.” The New Zealand Party thus bolstered Labour’s result by effectively cannibalising a substantial portion of National’s support base.

On coming into office, the new Fourth Labour Government was immediately faced with a serious foreign exchange (FX) crisis. With expectations of an official devaluation following the announcement of a snap election by Prime Minister Robert Muldoon on 14 June, in June and July 1984, private international currency traders had launched a series of major speculative attacks on the New Zealand dollar. On the express orders of Prime Minister (and Minister of Finance) Muldoon, the RBNZ had subsequently spent an estimated $797 million worth of foreign reserves defending the

---

336 Roper 2005b, 176.
337 The country simultaneously faced a constitutional crisis; Muldoon, technically still in power until the completion of the final official count of the election results (some 12 days after), refused to implement the incoming government’s directive to devalue the currency by 20% and, as Roper (2005b, 176) observes, “thereby effectively [gift] hundreds of millions of dollars to speculators in the private sector (many of whom had donated generously to the Labour Party).”
national currency (equivalent to 2.3% of GDP at the time). Consequently, as Dalziel and Lattimore detail, by the time of the 1984 election, the RBNZ’s official “reserves of overseas currencies, and its lines of credit with overseas lenders, were almost exhausted.”

Consistently reiterating the apparent seriousness of the situation, the newly appointed Minister of Finance, Roger Douglas, used this ‘inherited’ macroeconomic crisis to justify the rapid implementation of a broad ranging programme of neoliberal ‘structural adjustment’ during the Fourth Labour Government’s first term. This neoliberal policy agenda included: the adoption of a freely-floating foreign exchange regime and extensive deregulation of the local finance sector; the adoption of a ‘monetarist’ approach to macroeconomic management; extensive microeconomic reform; the abolition of state agricultural subsidies; regressive taxation reform reflecting the so-called ‘supply-side’ school of economic thought; and the adoption of a strategy of fiscal ‘austerity’, including reduced social spending, and the privatisation and corporatisation of state-owned assets.

Such a radical shift in policy direction had not been signalled by Labour prior to the 1984 election. As Roper elaborates:

most of those who voted Labour in 1984 expected the overall thrust of Labour’s policy-making to be left of the [Third National] Muldoon Government on a broad range of issues, including not

---

342 Roper 2005b, 176.
just sporting contacts with South Africa, nuclear ship visits, French nuclear testing in the South Pacific, and homosexual law reform, but also economic, social and industrial relations policy.\textsuperscript{343}

Thus, it is indeed dubious that the Fourth Labour Government possessed a legitimate democratic mandate for the hard line programme of neoliberal structural adjustment it subsequently enacted.\textsuperscript{344}

Labour was re-elected to power on 15 August 1987. Labour received 48% of the total vote and 57 parliamentary seats. National, in comparison, received 44% of the vote and 40 seats. The Democrats (formerly Social Credit) received just 5.7% of the vote and lost both of the seats they had previously held.\textsuperscript{345} Labour’s strong showing at the 1987 general election was underpinned by “a temporary [large scale] defection to it of traditional National voters.”\textsuperscript{346} The programme of radical neoliberal structural adjustment carried out by Labour during its first term resulted in the inflation of a large, but ultimately short-lived, financial bubble.\textsuperscript{347} Having benefited disproportionately, many wealthy urban voters subsequently shifted their support from National to Labour in 1987.\textsuperscript{348}

Mirroring developments on Wall Street and other major international financial markets, two months after the election, on 20 October 1987, the New Zealand sharemarket crashed. As Dalziel delineates:

At the end of March 1985, the Barclays Share Price Index for the value of the New Zealand sharemarket had been 1463. Twelve months later, the index had increased by more than 50 per cent to 2293 and by a further 42.5 per cent by the end of March 1987. The index peaked at 3969 on 18 September 1987 and was still at 3430

\textsuperscript{343} Ibid.
\textsuperscript{344} Ibid.
\textsuperscript{346} Kelsey 1997, 36; Roper 2005b, 178.
\textsuperscript{347} See Jesson 1999, 103-136.
\textsuperscript{348} Boston and Jackson, 70.
one month later on 19 October. The next day, however, the index fell by 14.7 per cent to 2925. It continued to slide for the rest of the year, settling at 1942 on 31 December, less than half its peak value three and a half months earlier.\textsuperscript{349}

Roger Douglas attempted to exploit the ensuing economic turmoil to extend his neoliberal reform agenda.\textsuperscript{350} “I believe the events of the last three weeks mean that we need to accelerate the process of reform”, he stated.\textsuperscript{351} On 17 December 1987, a new package of neoliberal reforms was announced. The core of the package comprised major changes to the country’s tax and social support systems.\textsuperscript{352} The rate of company tax was to be reduced considerably, a uniform flat income tax rate was to be introduced, and GST was to be increased to 12.5\%.\textsuperscript{353} Simultaneously, as Kelsey outlines, previously “comprehensive welfare provision” would be replaced by “a new Guaranteed Minimum Family Income (GMFI).”\textsuperscript{354} An extensive programme of privatisation was another prominent feature of the reform package. State assets were to be sold with the intention of raising $14 billion specifically for the purpose of retiring gross public debt by a full third by 1992.\textsuperscript{355} Other important elements of the new neoliberal reform package included: reductions in import protections; reform of local government operations; and liberalisation of the telecommunications industry.\textsuperscript{356}

Douglas’ aggressive moves to extend the neoliberal reform agenda fomented the emergence of “a crisis within the government.”\textsuperscript{357} Tensions had

\begin{footnotes}
\item[349] Dalziel and Lattimore 2001, 66.
\item[354] ibid.
\item[355] Sheppard, 49.
\item[356] ibid.
\item[357] Roper 2005b, 179.
\end{footnotes}
been mounting for some time prior, but now full-blown intra-party conflict erupted.\textsuperscript{358} Whilst generally supportive of the programme of free-market reforms implemented in the economic sphere (such as market and trade liberalisation), Lange and a number of other cabinet ministers were adamant that similar reforms would not be extended into the sphere of social policy. For Lange, however, the fundamental aim of Douglas’ December policy package was to do just that:

\begin{quote}
The level of the flat tax was clearly designed to be the great push against the State...By then it had become completely transparent to me that what we had done by way of taxation was part of an agenda which said that there is only one way to make the Government get out of government and that is to tax as little as possible because then we’ll be able to say we don’t have any money to engage in social services.\textsuperscript{359}
\end{quote}

Consequently, on 28 January 1988, Lange unilaterally cancelled significant portions of Douglas’ December policy package including, most notably, those relating the introduction of a flat tax and GMFI.\textsuperscript{360} Lange’s action precipitated the factional division of both the Cabinet and the wider Parliamentary caucus between the adherents of Rogernomics and those loyal to Lange. As Roper observes, “the ensuing political drama dragged on throughout the remainder of the Government’s second term in office”, even as “the Government continued zealously to implement neoliberal policies.”\textsuperscript{361} In November 1988, Lange sacked a close ally of Douglas, Richard Prebble, as Minister of State Owned Enterprises, and also Bevan Burgess, a key figure on Douglas’ staff. This induced Douglas’ effective resignation from Cabinet on 14 December 1988.\textsuperscript{362}

\textsuperscript{359} Lange quoted in Russell 1995, 164.
\textsuperscript{360} Kelsey 1997, 36; Russell 1995, 165-69.
\textsuperscript{361} Roper 2005b, 179.
\textsuperscript{362} Russell 1995, 197-198.
Although “Lange easily survived a leadership challenge by Roger Douglas in caucus a week later”, Douglas and Prebble nevertheless continued to attack Lange’s leadership throughout 1989 with the support of a newly-formed neoliberal “Backbone Club.” Ultimately, this campaign was successful; on 7 August 1989, Lange resigned as leader of the Labour Party and as Prime Minister. Lange’s deputy Geoffrey Palmer would temporarily succeed to the leadership before being replaced by Mike Moore in the lead up to Labour’s defeat at the 1990 election. Douglas and Prebble, meanwhile, were both returned to Cabinet.

---

363 Roper 2005b, 179-80; Russell 1995, 201.
364 As Russell observes (1995, 202), “The [immediate] catalyst for Lange’s resignation occurred on 3 August, 1989...when Roger Douglas was re-elected to Cabinet.”
365 Roper 2005b, 180. While these developments were taking place within the Government itself, outside of Cabinet sitting Sydenham MP and erstwhile party president Jim Anderton led a sizeable portion of the remaining Labour Party membership to splinter off and form the New Labour Party in April 1989. Later, in December 1991, New Labour would combine with Mana Moheke, the Democrats, the Liberals, and the fledgling New Zealand Green Party to form the Alliance. See Roper 2005b, 199.
3.2) Financial Market Liberalisation and Monetarist Macroeconomic Reform

The neoliberal policy agenda implemented in New Zealand during the period from 1984 to 1990 entailed a substantial programme of reforms affecting almost all major areas of public policy. As noted in the previous section, these reforms have already been covered by an extensive body of literature. The discussion here will focus on the Fourth Labour Government’s programme of financial liberalisation and its parallel adoption of a monetarist approach to macroeconomic management.

Financial Market Liberalisation

As documented by Harper and Karacaoglu, New Zealand’s pre-reform financial system was characterised by a high degree of direct government control. Interest rates, deposits, balance sheet structures, the direction and size of lending, external capital movements, market entry in financial services and banking, and segmentation barriers were all highly regulated. The overarching function of the pre-reform financial regulatory regime was to enable the government to exercise a considerable degree of monetary control. Prior to 1984, monetary policy was effectively dictated by government. Thus, tight “control over the growth of monetary aggregates” was a necessary prerequisite for the successful operation of monetary policy. Other key goals of the extant regulatory regime included: encouraging economic growth; promoting “equity in the financial intermediation process”; ensuring

---

366 D. Harper and H. Karacaoglu 1987, “Financial Policy Reform in New Zealand”, in A. Bollard and R. Buckle (eds.), Economic Liberalisation in New Zealand (Wellington: Allen and Unwin/Port Nicholson Press), 207. They were also not particularly transparent. Much of the data relating to these key aspects of the financial system was not uniformly available (nor entirely clear when it was) during the Muldoon years.

367 Ibid, 208.

368 Ibid.
government access to low-cost private funding; and the maintenance of macro-level systemic stability.\textsuperscript{369}

From 1984 onwards, however, a “market-driven” approach to the management of New Zealand’s domestic financial system was adopted. As Kelsey observes, “Treasury’s solution was to replace the direct control of the state with the purportedly unbiased contractual mechanisms of insurance, common law and the market place.”\textsuperscript{370} Overall, “the scope and speed of financial policy reform” programme implemented by the Fourth Labour Government “far exceeded those of the other components of the economic reform package.”\textsuperscript{371} The process of financial liberalisation began with a 20% devaluation of the dollar and the removal of interest rate controls.\textsuperscript{372} Thereafter, comprehensive financial reforms were rolled out at a blistering pace. Indeed, as Harper and Karacaoglu observe, “the scope and speed of financial policy reform in New Zealand [was] unequalled in the OECD.”\textsuperscript{373} By 1986: all price regulations in the financial sector and controls over the balance sheet structures of financial institutions (including those pertaining to borrowing and holding assets offshore) were removed; foreign exchange and capital controls were abolished; the dollar was floating freely; barriers to market entry or exit (including, most notably, controls over foreign involvement in domestic financial institutions) had been minimised to facilitate “contestability”; “prudent” supervision and liquidity management policies seeking to minimise system-wide effects of individual operator failure had been established; and “open market operations” had been adopted as the preferred instruments of monetary control for the RBNZ.\textsuperscript{374} Table 3.1 below provides a brief summary of

\begin{center}
\begin{tabular}{|c|}
\hline
\textsuperscript{369} Ibid; Kelsey 1997, 87. \\
\textsuperscript{370} Kelsey 1997, 87. See also Treasury 1987, Government Management (Wellington: Treasury), 258-259. \\
\textsuperscript{371} Harper and Karacaoglu, 210. \\
\textsuperscript{372} Goldfinch 2000, 87. \\
\textsuperscript{373} Harper and Karacaoglu, 206. \\
\textsuperscript{374} Ibid, 209; Kelsey 1997, 88. \\
\hline
\end{tabular}
\end{center}
the key features of the liberalisation of New Zealand’s financial system carried out by the Fourth Labour Government between 1984 and 1990.

**Table 3.1) Financial Liberalisation in New Zealand**

<table>
<thead>
<tr>
<th>Year</th>
<th>Changes</th>
</tr>
</thead>
</table>
| 1984 | • Run on the dollar leads to foreign exchange market closure.  
• Dollar devalued by 20%.  
• Interest rate controls removed.  
• Private offshore borrowing deregulated.  
• Credit growth guidelines abolished.  
• Exchange rate controls scrapped. | 1987 | • Rules governing operation of building societies liberalised and they are allowed to register as companies. |
| 1985 | • Reserve Asset Ratios and other ratio requirements abolished.  
• Dollar floated.  
• Controls on foreign ownership of domestic financial institutions scrapped. | 1988 | • Rules governing operation of Trustee Banks liberalised and requirement to register as companies introduced.  
• Postbank sold. |
| 1986 | • RBNZ’s powers of financial market oversight are extended and RBNZ given power to register banks. | 1990 | • Reserve Bank Act 1989 revises and extends RBNZ’s approach to prudential supervision of the financial system. |


Fundamentally, it was the implementation of this programme of extensive financial market liberalisation and financial sector deregulation that constituted the integration of New Zealand into the DWSR. From this point on international private financial capital could freely penetrate and circulate in the New Zealand economy. Indeed, As Kelsey has pointed out, the comprehensive relaxation of capital and FX controls, in combination with the rapid deregulation of the financial system, essentially set in motion “market

---

forces which are free to generate monetary expansion” or contraction at will.\textsuperscript{376}

As a direct consequence of this control over international financial flows, the most important aspects of public policy formulation in New Zealand (monetary, FX, and fiscal policy) have been rendered susceptible to unprecedented levels of influence by the vagaries of IPFMs.

**Monetarist Macroeconomic Reform**

The adoption of monetarist policy prescriptions “which maintain firm control of increases in the monetary and credit aggregates, in a manner that does not accommodate higher inflation” was “a critical part of [the Fourth Labour] Government’s economic strategy.”\textsuperscript{377} Moreover, as will be shown in Chapter Five, it has continued to form the foundation of public macroeconomic policy in New Zealand since its inception in 1984. As set out in Treasury’s 1984 post-election briefing paper, *Economic Management*, the official motivation for the Fourth Labour Government’s adoption of monetarism revolved around a concerted effort to reduce persistently rampant inflation. “Inflation is a problem...The key to reducing inflation over the medium term, and of ultimately achieving price-level stability, is a [monetary policy] aimed at restraining the growth of money and credit aggregates.”\textsuperscript{378}

The work of then Deputy Governor of the RBNZ Rod Deane indicates that the monetarist monetary policy strategy adopted by the Fourth Labour Government centred on “a brand of monetarism characterised by the simple quantity theory of (flexible) price determination”.\textsuperscript{379}

The principle objective of monetary policy... is to achieve suitably moderate and steady rates of growth of the major monetary

\textsuperscript{376} Kelsey 1997, 154.
aggregates. Underlying this aim, of course, is the wish...to reduce the rate of inflation and to maximise the rate of increase in real national income.\(^{380}\)

In essence, it was conceived that in operating the monetarist macroeconomic management strategy the RBNZ would control “primary liquidity”, measured as “the broad aggregate (M3).”\(^{381}\) Whitwell outlines that, in order to avoid excess liquidity, “the key control technique was to be a public debt sales programme designed to ‘fully fund’ the net public sector injections from the Treasury and the Reserve Bank into primary liquidity.”\(^{382}\) “This funding rule” was to “simulate the monetarist control rule, whereby close control over the monetary base” would ultimately enable “control over the rate of growth of the money supply and, therefore, [also] ...over the inflation rate.”\(^{383}\) Based on the work of Whitwell, Figure 3.1 (below) comprises a stylised conception of “the official representation of the major theoretical links between the stated operating target – primary liquidity – and the ultimate policy objective – the inflation rate.”\(^{384}\)

As Whitwell has conclusively demonstrated, however, “in-spite of a single-minded adherence to the operating rules specified by its policy framework, from the outset the Bank experienced problems with the transmission lines that were supposed to carry its monetary signals to the inflation rate.”\(^{385}\) In particular, “major technical issues” existed with both “the role of money and credit growth in the disinflation process”, as well as the “monetary signals that were supposedly being transmitted to wage and price setters via the trade-off between unemployment and inflation embodied in the

\(^{381}\) Whitwell, 104.
\(^{382}\) Ibid.
\(^{383}\) Ibid.
\(^{384}\) Ibid, 105.
\(^{385}\) Ibid.
'naive' Phillips curve.” These major problems with the classical quantity theory and Phillips curve monetary policy transmission channels effectively left only the FX channel in operation. As Whitwell observes, “almost by default, the exchange rate became the ‘direct’ channel for transmitting monetary policy signals to the inflation rate.” Furthermore, the FX transmission channel itself did not operate as intended. The “monetary impulses” projected by the RBNZ acted in such a way as to “impact primarily on output and employment instead of on prices.” Whitwell points out that, as a consequence, the RBNZ was ultimately forced “to recast monetary policy into a thinly disguised incomes policy with a selective focus: the profitability of the traded goods sector.” Figure 3.2 constitutes a stylised conception of the monetary policy transmission mechanism (MPTM) that more closely represents this empirical reality.

---

386 Ibid, 108.
387 Ibid, 117.
388 Ibid.
390 Whitwell, 102.
391 Ibid, 105.
Figure 3.1) The New Zealand Monetary Policy Transmission Mechanism: The Theory of Monetary Disinflation


Figure 3.2) The New Zealand Monetary Policy Transmission Mechanism: The Evidence

Figure 3.2 shows that the MPTM ultimately relied on a capacity to completely undermine the profitability of the tradables sector and consequently force exporters and import-substituters out of the market. By inducing an appreciation in the FX rate via increasing domestic interest rates, the traded goods sector (that is, exporters and import-substituters) is effectively subjected to a marked “loss of international competitiveness.” Indeed, it serves to ensure the traded goods sector experiences an “unsustainable fall in profits” due to both “a decline in revenues” and a significant appreciation in “debt-servicing costs.” As Wooding outlines, this serves to offset upward pressure on domestic price levels because the resulting system-wide decrease in employment and output acts to reduce national incomes and “will therefore [also] moderate the rate of increase in prices.” Thus, rather than constituting the anti-inflation strategy upheld by the proponents of the neoliberal reforms, the monetarist approach to monetary policy adopted by the Fourth Labour Government effectively constituted what can be considered an “anti-employment” strategy. As Whitwell summarises the point, in essence, when implementing a “tightening” of monetary policy what the Fourth Labour Government was actually doing was creating “a financial environment that was openly hostile” to the tradables sector.

This monetarist approach to New Zealand’s macroeconomic management was entrenched via the passing into legislation of the Reserve Bank of New Zealand Act (RBA) 1989. The RBA ratified price stability as the sole policy objective of RBNZ operations, and simultaneously enshrined the operational independence of the RBNZ. Dalziel details that

392 Ibid, 115.
393 Ibid.
394 Ibid.
396 Whitwell, 117.
397 Ibid, 115.
the statutory objective of monetary policy is now given in Section 8 of the Act, consisting of a single sentence: “the primary function of the Bank is to formulate and implement monetary policy directed to the economic objective of achieving and maintaining stability in the general level of prices.”

3.3) **Explaining the Shift to Neoliberalism in New Zealand**

With some similarity to the prominent cases of the US and the UK (discussed in the previous chapter), New Zealand’s historic shift to neoliberalism also necessarily took shape as an explicitly political project. Fundamentally, it comprised “a systematic [policy] programme carried out with precision and discipline” by a small discrete network of strategically located political actors, closely integrated through both formal and informal linkages, and in possession of significant institutional support. As Don Brash described the situation in his 1996 Hayek Memorial Lecture, “the economic debate brought together a small but strategically influential team of civil servants, think tankers, policy-makers and politicians around Roger Douglas. This group of quite remarkable people understood clearly what needed to be done and was committed to seeing it through.” As this section progresses, this key driving group – Brash’s “small but strategically influential team” - will be collectively referred to as the ‘Wellington policy community’ (WPC).

**Cabinet**

A core faction within the WPC was formed by a small group of cabinet ministers within the Fourth Labour Government; those who Easton refers to as the “troika.” Although constitutionally the Prime Minister is the most powerful individual political actor in New Zealand, in practice the Minister of Finance, in most policy matters, has more practical power. This largely derives

---


404 Easton 1997a, 73-84.
from a combination of the central political importance of economic and finance issues in the sphere of public policy and the size, competence and, as will be examined in-depth in the following sub-section, the unique institutional power of the ministry serving the Minister of Finance - the Treasury.\textsuperscript{405} The key initial period of neoliberal reform from 1984 to \textit{circa} 1988 was characterised by a weak Prime Minister, David Lange, in relation to an exceptionally strong finance “team.”\textsuperscript{406} Indeed, Easton observes that in a development without recent precedent, three “extremely capable politicians” were appointed to the finance portfolio; Roger Douglas as the Minister of Finance, with Richard Prebble and David Caygill as Associate Ministers.\textsuperscript{407} With respective cabinet rankings of fourth, fifth, and seventh, together these ministers constituted a powerful grouping within the state apparatus.\textsuperscript{408} It is this powerful grouping of cabinet ministers which Easton refers to as the \textit{troika}.

The \textit{troika} effectively possessed the power of policy implementation under the Fourth Labour Government from 1984 to 1988. As Easton outlines, at each stage of the governmental decision-making process, this powerful grouping of pro-neoliberal figures could exercise a significant degree of control enabling a historically unprecedented capacity for pushing through free-market reform.\textsuperscript{409} The \textit{troika} would begin by developing economic policy in collaboration with their Treasury advisors. The Prime Minister and his deputy, Geoffrey Palmer, would then be persuaded of its necessity. Once this was achieved (which, as Easton observes, it almost invariably was due to the interpersonal relationships involved), this group would proceed to present its hardline neoliberal proposals to cabinet.\textsuperscript{410}

\textsuperscript{405} Ibid, 73. See also S. Goldfinch 2000, \textit{Remaking New Zealand and Australian Economic Policy: Ideas, Institutions and Policy Communities} (Wellington: Victoria University Press), 85.
\textsuperscript{406} Easton 1997, 73.
\textsuperscript{407} Ibid, 74.
\textsuperscript{408} Ibid.
\textsuperscript{409} Ibid, 75.
\textsuperscript{410} Ibid, 74.
Within Cabinet, the *troika* and its allies were the dominant force. Douglas and his Associate Ministers combined with Lange and Palmer occupied five of the top seven positions. Close ally Mike Moore, the Minister of Overseas Trade, was also highly ranked.\(^{411}\) The dominance of the *troika* within Cabinet was facilitated, to some extent, by an apparent lack of a thorough understanding of the full implications of many of the *troika’s* policy proposals. Of much more importance, however, was a major reorganisation of the prevailing Cabinet Committee structure that was carried out almost immediately after the Fourth Labour Government took power. All of the existing Cabinet Committees were scrapped (including, most prominently, the powerful Cabinet Economic Committee) and were replaced by a single central Cabinet Policy Committee overseeing five sectoral Committees.\(^{412}\) This new structure effectively served to concentrate power within Cabinet. As Roberts observed at the time, under this regime “the Cabinet Policy Committee exercises considerable control over policy directions, sets the context of debate on major proposals and defines overall resource limits for the major areas of the Government’s programme.”\(^{413}\)

Unsurprisingly, the *troika* and its allies were at the centre of this new concentration of power. The Cabinet Policy Committee was chaired by Lange. Palmer, Douglas, Prebble, Caygill, and Moore were all members.\(^{414}\)

From Cabinet, a policy decision would then move to caucus. Here, Easton notes, the *troika’s* historically unprecedented decision-making power

\(^{411}\) Ibid, 74-5.


\(^{413}\) Ibid.

\(^{414}\) Roberts, 96. At least one of the three Finance Ministers was also a member of each of the sectoral Committees.
was most evident.\(^{415}\) In 1984 the cabinet (which generally operated under a principle of collective responsibility) along with the six under-secretaries formed a 26-strong bloc of MPs within the 56-strong Labour caucus. To its ranks could be immediately added several independently pro-neoliberal backbenchers, as well as party loyalists and party functionaries (such as the two Whips) that could be depended on to follow the leadership's neoliberal policy direction. As Boston observes, during the period from 1984 to 1988, “this gave the [troika] virtual dominance” within the caucus and, thus, the *troika* could effectively impose their neoliberal policy agenda on a house of over 90 MPs and the entire country.\(^{416}\)

**The State’s Institutional Advisors**

Key bureaucrats within Treasury and the RBNZ formed a further important group within the neoliberalisation-driving WPC network.\(^{417}\) Indeed, it has been argued that the adoption and implementation of neoliberal public policy prescriptions under the Fourth Labour Government from 1984 onwards “essentially involved little more than the uncritical acceptance of Treasury’s neoclassical explanation of the economic crisis, and the rapid and comprehensive implementation of Treasury’s policy prescriptions.”\(^{418}\) This hypothesis is entirely unsurprising considering that, as Boston and Cooper have pointed out, “Treasury is the most powerful government department in New Zealand” and “its influence extends over the whole state apparatus and touches almost every important area of public policy.”\(^{419}\)

---

\(^{415}\) Ibid, 75.

\(^{416}\) Boston 1990, 64. See also Easton 1997a, 74-75; Kelsey 1997, 35, 42.


\(^{418}\) Roper 2005b, 169.

The power and influence of Treasury derives from several key sources. First, Treasury possesses the capacity to set the overarching philosophical/theoretical framework within which all core public policy decisions must be made. In this manner, to a significant degree Treasury effectively establishes the boundaries of policy discussion. Second, Treasury serves as the public financial control agent. Through this Treasury has input into almost all public policy formulation, advice and implementation. Indeed, as Roper has emphasised, Treasury has considerable influence over the government budgetary process that funds and implements policy decisions, enabling it to not only establish the macroeconomic context (as indicated above), but also the subsequent fiscal strategy to be adopted, and to comment on all other governmental department’s policies and funding allocations. Treasury’s third major source of institutional the power can be effectively summarised as bureaucratic strength. Treasury employs a large staff, including an unrivalled number of highly trained economists and policy analysts, based on a relative level of funding that is far greater than any other policy oriented department or ministry. It should be noted that Treasury’s position and bureaucratic strength is also maintained and enhanced by the traditionally high cabinet rank of its minister, through its links to the main opposition party, and also, very importantly, through linked career paths with the private commercial sector. Of course it must be remembered that Treasury is constitutionally only a policy advisory body, however, given these sources of power, it nevertheless possesses an unrivalled capacity to promote this advice.

The genesis of a major paradigmatic shift in Treasury thinking (from social democratic Keynesianism to neoliberalism) is evident before 1980. It has been suggested that the shift towards neoliberalism may have begun as early as

---

420 Ibid; Boston and Cooper, 133.
421 Roper 2005b, 158.
422 Ibid.
423 Ibid, 159.
the 1960s, but, as documented by McKinnon, it is during the period from 1978 onwards that the neoliberal shift within Treasury became fully manifest. During this period “the intellectual climate [within Treasury] totally changed.” Central to this shift were the activities of a newly formed division within Treasury, officially titled ‘Internal Economics II’. This division was led for much of the period leading up to 1984 by figures that subsequently featured prominently in the WPC which drove the Fourth Labour Government’s radical program of neoliberal reforms. The influence of this key division was particularly evident from the 1981 post-election briefing Economic Strategy onwards, which, while emphasising a commitment to neoliberal policy prescriptions, also simultaneously explicitly challenged the prevailing Keynesian macroeconomic policy orthodoxy. Due to the dominant influence of this division within Treasury, from this early period onwards there was simply no scope for a coherent alternative to the staunchly neoliberal line espoused by Internal Economics II.

From 1984 onwards the fundamental shift in Treasury thinking became much more publicly pronounced. Roper has observed, for example, that the key briefing papers Economic Management (1984), Government Management (1987), and Briefing to the Incoming Government (1990) all “extensively borrow from neoliberal schools of thought” in terms of both “theory and policy prescriptions, particularly the Chicago and Austrian schools, New Classical economics, Supply-side arguments..., and Public Choice and New Public Management analyses.” These key policy papers outlined and promoted the key features of the neoliberal policy regime that was subsequently

424 McKinnon, 226-273, 276, 284.
425 Ibid, 286.
426 Ibid; Goldfinch 2000, 42-43.
427 McKinnon, 286. These included Graham Scott (secretary to the Treasury in 1984) and Roger Kerr (Assistant Secretary to the Treasury in 1984, and soon after to become the Chief Executive of the New Zealand Business Roundtable).
429 McKinnon, 291-2.
430 Roper 2005b, 160-68.
implemented. Before 1984, Treasury’s neoliberal agenda had essentially been blocked by the then Prime Minister and Minister of Finance, Robert Muldoon. McKinnon notes, for example, that, in terms of its official policy advisory function, from around 1981 Treasury was essentially “under quarantine.”  

This all changed following the election of the Fourth Labour Government; there is “no doubt that Treasury provided the underlying analytical framework for the Labour Party’s policy-making throughout its two terms in office.”

With regards to the key areas of neoliberal policy being focused on in this chapter (financial deregulation and the adoption of monetarism), Treasury officials played a particularly central role in its formulation and implementation. As Goldfinch points out, for example, the broader programme of financial liberalisation, including the devaluation and float of the dollar (key elements of the above outlined monetarist macroeconomic strategy), was initiated and developed by officials from Treasury and the RBNZ, with cabinet largely following their advice. Oliver outlines that, within a more general shift towards neoliberalism from late 1983, the Labour Caucus rapidly adopted financial deregulation and monetarist macroeconomic management prescriptions and that “this shift can be shown to have coincided with a period of close collaboration between Douglas” and Doug Andrews, a Treasury adviser seconded to the opposition from the afore mentioned Internal Economics II division.

The RBNZ’s respective pattern of influence over New Zealand’s neoliberal shift broadly follows that of Treasury, although with some minor differences. Like Treasury, the RBNZ began espousing financial deregulation and monetarism from the late 1970s onwards. Through its research agenda and various resulting publications, such as The Stabilisation Role of Fiscal Policy, it

---

431 McKinnon, 305.
432 Roper 2005b, 169.
433 Goldfinch 2000, 87.
434 Oliver 1989, 11-12.
435 See, for example, McKinnon, 306; Goldfinch 2000, 90-91.
recommended the comprehensive liberalisation of the FX regime, amending the reserve asset ratios for financial institutions, and a number of other regulatory changes to interest rates and monetary policy settings.\footnote{Goldfinch 2000, 88.}

Again like Treasury, during the two terms of the Fourth Labour Government, the RBNZ was also closely involved with the adoption and implementation of the neoliberal financial liberalisation agenda. RBNZ Deputy Governor, Roderick Deane is noted to have played a particularly prominent role within the WPC. While its relative institutional power meant that the RBNZ’s influence was not as wide-ranging as that of Treasury, it was nevertheless centrally involved in the development of policy for its specialist areas (financial, FX, and monetary policy). Indeed, the RBNZ played a crucial role in formulating and implementing both the programs of financial deregulation and the monetarist macroeconomic strategy (including the RBA).

**Business**

As Roper has emphasised, although Treasury and the RBNZ together have substantial institutional power and influence at their disposal, if the policy agenda pushed by these agencies “was seriously at odds with powerful class-based interest groups in civil society, and the dominant faction within cabinet was sympathetic to the concerns of these groups” it is unlikely that the neoliberalisation of New Zealand would have been undertaken in the rapid and comprehensive manner that it was.\footnote{Roper 2005b, 170.} As we have already seen, due to the various sources of power at their disposal, generally “big” business is the most powerful set of interests within contemporary liberal democratic societies like New Zealand.\footnote{See the discussion of neopluralism in Chapter One.} Thus, unsurprisingly, a final key faction of the neoliberalism-driving WPC is to be found within the ranks of private enterprise.
From 1975 to 1984 a major ideological-political shift to neoliberalism took place within business in New Zealand. This shift essentially involved all of the major sectoral business associations, the Employer’s Federation (NZEF), as well the general policy-oriented business associations.\(^439\) The one partial exception was the Manufacturer’s Federation (NZMF), traditionally the strongest defender of Keynesian protectionism. However, between 1974 and 1984, much of the manufacturing sector stagnated while a body of large export-oriented trans-national industrial corporations grew rapidly. Therefore, even within the ranks of the NZMF, a pro-neoliberal constituency began to emerge.\(^440\) The comprehensiveness of business’s neoliberal turn was outwardly demonstrated by the ‘Assembly of Business’ held in August 1983. As Roper outlines, this “brought together representatives from all the major business associations” who endorsed a final communiqué centrally seeking “less state intervention in the economy”, fiscal austerity (reduced taxation, expenditure and government operating deficits), deregulation of industrial relations, and trade liberalisation.\(^441\)

Following its thorough shift to neoliberalism, New Zealand business has been documented as having exerted considerable influence over public policy formulation.\(^442\) Playing a leading role in this, especially up until the end of the first term of the Fourth National Government, was the New Zealand Business Roundtable (NZBR). Indeed, Roper has observed that “the remarkably close correspondence between the policy prescriptions of the Business Roundtable and the policies of the Fourth Labour Government and the… (Fourth) National Government constitutes one of the more conspicuous features of New Zealand politics after 1984.”\(^443\) The NZBR effectively formed the apex of corporate power

\(^{440}\) Ibid 2005b, 107.
\(^{442}\) Ibid, 2006.
at this time, with its membership being comprised of the most significant business interests in New Zealand. This key representative of business interests is noted to have produced numerous policy submissions, funded visits, public seminars, and publications by right-wing academics, to have established the neoliberal think tank the Centre for Independent Studies, and NZBR businesses also gave substantial monetary donations to support the neoliberal factions of both the Labour and National parties. However, it needs to be noted that, to a significant degree, the activities of the NZBR were essentially a systematised expression of the policy preferences of the broader New Zealand business community. Big business figures thus formed a further conspicuous bloc within the neoliberalisation-driving WPC, having documented links, both formal and informal with Treasury, the RBNZ, and the pro-neoliberal faction within the Labour caucus.

**Systemic Pressures**

The practical implementation of radical neoliberal structural adjustment during the period from 1984 to 1990 thus involved a systematic political program carried out by a group of strategically placed individuals drawn mainly from the upper echelons of the Fourth Labour Government, Treasury, the RBNZ, and business. However, New Zealand’s comprehensive neoliberalisation also needs to be understood, fundamentally, as having been formulated in response to “mounting systemic pressures” within the domestic political economy. To date the work of Roper offers the most sophisticated and theoretically rigorous account of the underlying systemic pressures that prompted New Zealand’s historic shift to neoliberalism. Centrally, Roper upholds that the political activities of business (but implicitly also of the various

---

444 Ibid, 17; Easton 1997a, 115.
446 Easton 1997a, 115, 117.
447 Zuerge 1999, 98.
other factions within the influential WPC-network) should be considered to constitute a “a series of political responses to the prolonged economic crisis, intensified industrial conflict, ...faltering attempts of the Third National Government to manage that crisis using Keynesian policy instruments”, and a major shift in the international intellectual orthodoxy from Keynesianism to neoliberalism.448

In the previous chapter it was shown that from the early 1970s onwards the global economy entered into a period of major downturn. New Zealand was not immune from this. Figure 3.3 (below) graphically illustrates the onset of ‘stagflation’ – stagnant economic growth combined with high inflation – in New Zealand. As can be seen, during the period from 1975 to 1984 the nation began to experience a prolonged period of relative economic weakness.449 Compared to a mean level of 4.47% in real terms during the period from 1950 to 1974, economic growth averaged just 1.53% during the period spanning from 1975 to 1984.450 Simultaneously, inflation increased dramatically. Inflation averaged 5.46% between 1950 and 1974. Between 1975 and 1984, however, inflation rose to an average of 13.46% (peaking at 18.4% in 1980).451

449 Ibid, 5.
451 Ibid.
Due to the onset of stagflation, Roper observes that “the economic pressures on the state increased greatly from the mid-1970s onwards.” More specifically, “as profitability and growth declined and unemployment rose, the state was faced with rising social expenditure on the one side... and increasing difficulty in maintaining taxation revenue on the other.” The ultimate result of this was a mounting fiscal crisis of the state.

Simultaneously, the societal balance of power underwent a major shift. Business, erstwhile dominated by organised labour, now came to occupy the preeminent position. The onset of stagflation brought about mass unemployment in New Zealand for the first time during the post-war era.

---

*Figure 3.3) The Onset of Stagflation in New Zealand*


---

452 It should be noted that the significant decrease in inflation shown to have occurred in 1984 was only temporary. It was the result of a 20-month price freeze implemented by Muldoon in 1983. Inflation in New Zealand was not successfully brought under control until circa 1991. See Dalziel and Lattimore 2001, 134.
453 Ibid, xx, 27.
454 Ibid, 27.
455 Ibid, xx, 27.
456 Ibid.
457 Roper 2005b, xx.
Figure 3.4 illustrates this phenomenon. Rising unemployment on a scale unprecedented in recent contemporary history had a profoundly negative impact on the previously robust union movement. The unions’ organisational strength and bargaining power were both critically undermined. Business quickly took advantage of labour’s incipient weakness. From the mid-1970s onwards, a “counter-mobilisation of capital” took place. “Employers became increasingly industrially militant” thereby decisively wresting societal power back in favour of business.

As a consequence, Roper argues, “successive governments from 1975 onwards” were subject to both greatly increased economic and political pressure to take the side of business in the formulation and implementation of public policy. On the one hand, the worsening economic conditions were increasing the structural pressure on governments to provide for the needs of business.

---

458 Ibid.
460 Ibid.
461 Ibid.
the other hand, having returned to the ascendance within society, business interests were rapidly becoming increasingly “politically active” and were primarily directing “this activism towards lobbying successive governments to adopt” pro-business policies.\footnote{Ibid. See 103-110 for more detail.}

Roper outlines that “these [above discussed] economic, social and political developments gave rise to, and in turn were influenced by,” a major paradigmatic shift in economics.\footnote{Ibid.} As the foremost advisor to cabinet, Treasury acted as the principle conduit through which this systemic international pressure was transmitted to the WPC (although other avenues of transmission certainly existed).\footnote{Other avenues of transmission included business associations, the media, and universities (especially the University of Canterbury Economics Department). See McKinnon, 284, 306.} During the period from 1984 to 1990, the crucial papers produced by Treasury “which provided the overall blueprint for the neoliberal policy regime, extensively borrowed from neoliberal schools of thought, often verbatim and without due consideration of the limitations of their theoretical arguments and empirical findings.”\footnote{Roper, 2005b. 161.}

Ultimately, the RBNZ also functioned as a major transmission line for the neoliberal shift in the international economic orthodoxy. This is unsurprising considering that, like Treasury, the RBNZ is one of the preeminent employers of professional economists in New Zealand. In relation to the RBNZ’s role as a principle neoliberal orthodoxy conduit, Dalziel’s analysis of the monetarist legislative lynch-pin, the RBA is particularly illuminating.\footnote{Dalziel, 1993.} Dalziel documents, for example, that the key Section 8, in particular, was in-fact largely based on “Friedmanite” monetarism or “Chicago School” economics, and “New Classical” economics. “Echoes of these monetarist and new classical theories in section 8 of the Reserve Bank Act (with its elimination of output and
employment objectives and its sole focus on price stability) are loud and clear.”

Roper argues that, essentially, “the shift from Keynesianism to neoliberalism within the economics profession and the growing disenchantment with Keynesian demand-management within the so-called business community mutually reinforced each other.” Big business was quickly becoming aware that Keynesianism was “failing to reverse the decline of the economy”, while “neoliberal economists in the Treasury” and the RBNZ “provided a coherent explanation of stagflation and a set of policy prescriptions” that would ensure the restoration of economic prosperity. Consequently, from the late 1970s onwards, business and Treasury began to present “neoliberalism” to the state as constituting the only viable “broad intellectual and ideological paradigm” for the formulation of almost all aspects of public policy in New Zealand.

Overall, Roper’s account is very useful. It identifies and subsequently examines a number of important underlying factors exerting pressure on the decision making of the political actors of the WPC in the years leading up to the neoliberal turn in New Zealand. However, a further underlying factor should perhaps be added to those discussed by Roper. This factor comprises the ongoing transformation of the underlying structure of the economy.

Mirroring developments elsewhere in the advanced capitalist world (discussed in the previous chapter), during the decade leading up to the neoliberal turn in New Zealand, the domestic economy became considerably more internationalised. Crucial here is the comprehensive empirical work contained within the PhD thesis of Cronin, *The Politics of New Zealand Business*...

---

467 Ibid, 85-86.
468 Roper, 2005b, xxii.
469 Ibid.
470 Ibid, xx.
Internationalisation 1972-1996. The close scrutiny “of the internationalisation activities of significant New Zealand companies” contained within this work reveals that well before the liberalisation of capital controls and international investment regulations, during “the 1970s and early 1980s”, “there was a rapid increase” in both “the extent and intensity” of business internationalisation in New Zealand.

Drawing mainly on historical company reports, Cronin identifies four main measures of outward business internationalisation activity. These are: the export share of sales; the offshore share of sales; the number of overseas subsidiaries; and the number of overseas subsidiaries engaged in production. At a general level, each of these key measures show that outward business internationalisation increased significantly in New Zealand during the decade prior to the implementation of neoliberal reforms. As Cronin outlines, “exports, as a share of total sales,” expanded significantly “in four bursts, from 1972 to 1975, from 1981 to 1983, 1984 to 1988, and 1991 to 1992.” The offshore share of sales “rose more steadily through the 1970s, more rapidly in the 1980s to an initial peak in 1988.” Outward internationalisation in terms of both measures relating to offshore subsidiaries, meanwhile, expanded throughout the 1970s and 1980s, reaching a peak in 1988.

Again mirroring international developments, this trend towards significantly increased business internationalisation during the period from 1972 to 1984 was accompanied by a strong trend towards financialisation within the New Zealand economy. Centrally, as the New Zealand financial sector

---

473 Cronin, 318. In this instance, offshore share of sales refers to offshore the sale of goods produced offshore by New Zealand-owned subsidiaries. Respectively, export share of sales refers to the offshore sale of goods produced in New Zealand.
474 Ibid.
475 Ibid.
476 Ibid.
became increasingly dominated by a smaller number of large, foreign-oriented businesses (an issue discussed in more detail in Appendix A), the position of financial capital within the domestic capitalist hierarchy shifted. Whereas before 1972 financial capital had occupied a position supporting other areas of economic endeavor, during the period from 1972 to 1984 the banks, finance houses, and emerging investment companies came to occupy a much more central position within New Zealand’s economy. As Jesson observes, the focal points of economic activity (and, thus, also the primary sites of profit generation) began to move away “from the productive sectors of the economy” and became progressively more orientated around finance.477

The overarching trend towards the increasing importance of finance within the New Zealand economy prior to 1984 is perhaps best illustrated by documented changes in the share of surplus value (profit) appropriated by the finance sector during the period. The New Zealand economy experienced a “large rise in the share of surplus value appropriated by the finance sector” from 1972 to 1990, with “the finance share of surplus value” rising “four-fold from 6 percent to 27 percent, in three steps: 1972 to 1975, 1977 to 1983, and 1984 to 1990.” 478 This prominent trend towards financialisation is presented graphically in Figure 3.5 below.

478 Cronin, 183.
But, following Krippner, “the growing weight of finance in the economy” during the period from 1972 to 1984 was also registered “in the behavior of non-financial firms.”

Mirroring their offshore counterparts, major industrial firms began to increasingly turn to finance as a means of supplementing their traditional operations. Long established firms such as Fisher and Paykel established new finance arms. Simultaneously, major non-financial firms began to acquire interests in the finance sector. Most notable in this regard was then emerging conglomerate Fletcher Challenge which took control of a majority stake in major finance house Marac. It also appears that it was within this time period that the concept of ‘shareholder value’ first became established as a guiding principle of business operations in New Zealand.

As Kelsey notes, for figures such as Ron Trotter of Fletcher Challenge (and also inaugural chair of the NZBR), “the new priority [for their businesses] was to maximise returns to shareholders through high dividends and rising share prices.”

---

480 Kelsey 2015, 61-62.
481 Ibid, 61.
There is little doubt that the entry of the UK into the European Economic Community (EEC) in 1973 was a significant factor driving the increased internationalisation of New Zealand business. As Cronin explains, “the British accession to the EEC closed the door on New Zealand’s major export market, and prompted a major reorientation of the country’s international economic relations.” However, the prevailing economic climate (both in the domestic sphere and globally) must have also had some bearing on these underlying structural changes. Facing weak growth prospects, New Zealand business would have greatly increased incentives to look both offshore and to financial activities as viable options to boost profitability.

Easton has observed that a generational shift occurred within the nation’s business elite in the years leading up to the reforms. But the shift observed by Easton can be seen to have been more than just generational; it also appears to have reflected the changes in the underlying structure of the economy documented above. These changes helped drive a decisive shift in the intra-capital balance of power occurring sometime during the period from 1975 to 1984. Business people linked to the financial sector and increasingly re-orienting their operations towards finance and the international arena now ascended to the apex of corporate power in New Zealand. It was the core of this new dominant faction within corporate New Zealand that would later coalesce to form the NZBR in 1986.

This transformation of the balance of power within the business community would have inevitably influenced the specific character of the political-economic pressures being exerted on the state in New Zealand state prior to the neoliberal turn in 1984. As argued in Chapter One, the advanced capitalist state is fundamentally reliant on the taxation of the process of private

---

482 Ibid 317.
483 Easton 1997, Commercialisation of New Zealand.
capitalist enterprise to maintain viability. Because of this, especially during an extended period of economic downturn (such as that being experienced in the period leading up to the reforms), there is significant implicit or ‘structural’ pressure on the state to implement policies to reinvigorate the process of capital accumulation. With increasingly powerful elements within domestically-operating capital become progressively more internationally-oriented and financialised, there would have been rising pressures on the state to take responsibility for creating an economic framework specifically conducive to business in these areas. At the vanguard of this dynamic would have been increasing pressure for comprehensive financial deregulation, the relaxation of capital and exchange controls, and the reduction of inflation. The substantive degree of such pressure being exerted on the state is perhaps indicated by the subsequent primacy accorded to such policies within the broader programme of neoliberal reform.
Conclusion

This chapter has outlined how, from 1984 through to 1990, New Zealand underwent a comprehensive process of radical neoliberal reform. A key feature of this initial stage of New Zealand’s neoliberalisation was rapid and comprehensive deregulation of the country’s financial sector combined with extensive financial market liberalisation, and the parallel adoption of neoliberal monetarist macroeconomic policy prescriptions. Fundamentally, these policy initiatives served to integrate New Zealand into the DWSR and, therefore, also to expose the country to the vagaries of IPFMs. Existing accounts of New Zealand’s historic shift to neoliberalism place significant emphasis on the role played by a small but extremely influential body of individuals located within cabinet, the key institutional advisors to cabinet (Treasury and the RBNZ), and the business community, in first promoting and then subsequently driving through radical reform. The actions of this group, however, were influenced to a significant degree by a much broader set of underlying developments within New Zealand’s political economy. These included, most prominently: the onset of ‘stagflation’ during the mid-1970s; employers taking the place of organised labour as the dominant force within New Zealand society and simultaneously becoming much more industrially militant and politically active; a major shift in the international economic orthodoxy from Keynesianism to neoliberalism; and the increasingly financialised and internationally-oriented nature of business activity within the New Zealand economy.

Mr Speaker, the Prime Minister has outlined the scale and nature of the problems confronting this new Government. At the heart of these problems is the crushing burden of government spending. The continuing increase in the size of the State has resulted in growing debt, punitive tax levels and intolerable pressure on interest rates. These burdens have sapped the initiative and the energy of New Zealand’s wealth creators. We cannot prosper as a nation if we put spending ahead of earnings.

- Ruth Richardson, 1990.¹

Introduction

The last chapter documented how, during the period from 1984 to 1990, New Zealand underwent a process of radical neoliberalisation. It outlined how this process was primarily impelled by a relatively small, yet highly influential group of MPs within the Fourth Labour Government, Treasury and Reserve Bank (RBNZ) officials, and business leaders. It also outlined how the activities of this group were heavily influenced by a range of broader international developments. These developments included: the worldwide onset of stagflation; a sharp upswing in employer militancy; and the shift in the prevailing international economic orthodoxy from Keynesianism to neoliberalism.

During the period from 1990 to 1999, New Zealand’s historic shift to neoliberalism continued. As Roper observes, the Fourth National Government

that succeeded the Fourth Labour Government “enthusiastically picked up where Labour had left off.”

2 Roper 2005b, 195.

3 Ibid.
4.1) **The Fourth National Government: A Political Overview**

The Fourth National Government was elected to office on 27 October 1990. The National Party received 47.8 percent of the total votes cast in the election and secured a healthy majority of 67 of the 99 parliamentary seats available. In comparison, the incumbent Labour Party gained only 35.1% of the vote and 29 seats. As Roper observes, “in electoral terms” this constituted “a crushing defeat for Labour and a resounding victory for National.” However, National’s victory was not secured via attracting a significant amount of new support. Rather, as documented by Vowles and Aimer, National’s victory was largely based on a massive rejection of the Fourth Labour Government’s prior policy direction on the part of the electorate.

National won the election campaigning on a platform of creating a “decent society.” Party leader Jim Bolger stated in his party’s 1990 election manifesto that:

> National’s vision is clear. We are going to build the Decent Society where people enjoy the opportunity of worthwhile work…the chance to enjoy the rewards of hard work and initiative…access to good education, quality healthcare, and a clean environment.

It was intimated that this policy platform would generally entail adhering to Labour’s neoliberal approach to public policy, albeit with a somewhat less extreme policy mix. In the pre-election policy document *National’s Economic Vision*, incoming Finance Minister Ruth Richardson stated that the Fourth National Government’s “principle first term economic targets” would be:

---

5 Roper 2005b, 195.
7 Ibid, 9-10. See also Roper 2005b, 111.
9 Ibid, 3.
10 Roper 2005b, 196.
economic growth of at least 3% per annum; the halving of unemployment levels; an inflation rate of 0-2%; interest rates below 10%; a balanced budget; and reduced government spending and taxation as a percentage of GDP.\textsuperscript{11}

However, beyond these very general policy targets, National did not clearly outline the specific details of its intended policy agenda. As Vowles and Aimer observe in their detailed empirical study of the 1990 election, “it was unclear...which of their...objectives would be stressed” and what the overall “balance of National’s policies would therefore be.”\textsuperscript{12} Furthermore, “apart from a vague reference to the need to ‘redesign’ welfare with a view to achieving a more affluent and self-sufficient society”, “prior to October 1990, there was little or no indication of where National would make cuts it promised in government expenditure.”\textsuperscript{13} As a result, it was somewhat unexpected when “National moved very rapidly to finish implementing Labour’s neoliberal program of structural adjustment” in the areas of industrial relations, social welfare, and fiscal policy.\textsuperscript{14}

Despite its apparently crushing victory at the 1990 General Election, on the back of its poorly signaled hard line neoliberal policy agenda, the Fourth National Government’s popularity quickly fell away. As Vowles \textit{et al} outline, by late 1991 “National’s popularity in opinion polls reached an all-time low for any government. From a high of 50 per cent support just after the 1990 election, National dropped to a mere 22 per cent.”\textsuperscript{15} Mass protests and widespread industrial action also erupted. Hundreds of thousands of New Zealanders took part in (amongst other things) a ‘Week of Action’ involving “strikes, stopwork meetings, rallies, and marches” in response to the introduction of the

\textsuperscript{13} Ibid.
\textsuperscript{14} Roper 2005b, 196.
\textsuperscript{15} Vowles \textit{et al} 1995, 7-8.
Completing the Shift to Neoliberalism

Employment Contracts Bill (ECB). Simultaneously, a massive wave of Maori protests began, and thousands of tertiary students took part in “large protest marches and mass occupations against rising fees, inadequate living allowances and rapidly rising student debt.”

This historically unprecedented unpopularity lead to the development of major schisms within the Fourth National Government. In August 1991, National MPs Gilbert Myles and Hamish MacIntyre abandoned the party and formed the Liberal Party. Soon after, in October, populist conservative politician Winston Peters was ejected from cabinet. Peters (and also former Prime Minister Robert Muldoon) had been consistently outspoken about the Fourth National Government’s neoliberal policy direction. Ongoing public criticism of the Government’s neoliberal policy agenda from Peters ultimately resulted in him being fully excluded from the National caucus in October 1992. Outside of the National Party, Peters forced a by-election in his North Island electorate of Tauranga. Peters won this contest comfortably. Running as an independent candidate, he gained 90.7% of the vote. Shortly after this decisive by-election victory, in mid-1993, Peters established the New Zealand First Party.

The substantial popular dissatisfaction with the performance of the Fourth National Government also helped foment the rapid emergence of the social democratic Alliance. Bringing together former Labour Party president Jim Anderton’s New Labour Party, with erstwhile electoral minnows the Green

---

16 E. Dannin 1997, Working Free (Auckland: Auckland University Press), 146. The ECB was, at its core, a fundamentally anti-union piece of legislation designed to drastically reduce real wages and employment conditions, whilst concurrently crushing union membership and power. Its central provisions were: to make union membership voluntary; to legally entrench free-riding on union-gained pay and work conditions; and to severely restrict workers ability to strike. The ECB was later passed into law as the Employment Contracts Act (ECA) on 15 May, 1991. For a detailed overview and critical discussion of the ECA see Roper 2005b, 209-212.
17 Roper 2005b, 112.
18 See, for example, New Zealand Herald 1991, “PM Angered by Speech from Peters”, 14 June.
19 The extent of this victory is partly explained by the fact that neither of the two major political parties fielded candidates in opposition to Peters.
Completing the Shift to Neoliberalism 183

Party, the Democrats, Mana Motuhake and the previously mentioned Liberal Party, the Alliance Party formed on 1 December 1991.21 As Roper outlines, soon after the Alliance was “surging ahead of both Labour and National in the polls.” 22 In a poll conducted by the weekly business publication National Business Review (NBR) in early December 1991, “37 per cent supported the Alliance compared to Labour’s 35 per cent and National’s 27 per cent.”23

Thanks in a large part to the vagaries of the First Past the Post (FPP) electoral system, the Fourth National Government was nevertheless re-elected on 6 November 1993. National received just 35.1% of the vote, but still managed to secure 50 parliamentary seats. Labour, in comparison, secured 45 seats with 34.7% of the vote and the newly formed Alliance and New Zealand First parties each acquired 2 seats on the basis of receiving 18.2% and 8.4% of the vote respectively.24 As Vowles et al outline, the outcome of the election was not initially clear, “with the party composition of the next government to remain unknown until the final count of special votes in several key contests.” 25 National only secured power after the provincial South Island Waitaki electorate was confirmed as having been taken by National after the counting of special votes and Labour MP Peter Tapsell was made speaker of the house, thereby effectively propping up the Government by yielding National a two seat parliamentary majority.26

The 1993 General Election was conducted in conjunction with a binding referendum on electoral reform. More specifically, the referendum was on whether to retain the existing FPP system or instead to adopt German-style Mixed Member Proportional (MMP) representation. The referendum was a product of mounting disillusionment with the credibility of the country’s

21 Roper 2005b 199. The Liberal Party was a slightly later addition to the ranks of the Alliance.
22 Ibid.
23 Ibid.
26 Vowles and Aimer 1994, 1. See also Roper 2005b, 201.
electoral system. As Roper outlines, “a large majority of New Zealanders were...not happy that first Labour then National had taken power, having made promises to the electorate that were subsequently broken.” 27 As a result, the Fourth National Government had held a referendum on the possible reform of New Zealand’s electoral system on 19 September 1992. The result of this initial indicative referendum was “an overwhelming rejection of the status quo.” 28 Based on an overall turnout of 53.5% of registered electors, 84.7% voted in favour of scrapping the existing FPP electoral system, and 70.5% voted specifically in favour of adopting an MMP system. 29 Such a powerful result effectively obligated the Fourth National Government to subsequently hold a corresponding binding referendum simultaneous with the 1993 election. 30 Some 54% of the 85.2% of eligible voters who took part in the 1993 election endorsed New Zealand adopting MMP while 46% supported the retention of the existing system. 31

As would be expected, the combined outcomes of the 1993 election and coinciding referendum “seriously weakened” the Fourth National Government. 32 The Government faced considerable public opposition and could not conceivably claim a credible democratic mandate for further neoliberal reform. Thus, Jim Bolger dumped Ruth Richardson as Finance Minister, replacing her with close ally Bill Birch. Widely disparaged as the architect of National’s harsh first term welfare reforms (popularly dubbed ‘Ruthanasia’, discussed below), Richardson had become a major political liability for the chided Fourth National Government. 33 Bolger also sought to shift his government’s “rhetoric away from the overt and strident neoliberalism of the

---

27 Roper 2005b, 200.
29 Ibid.
30 Vowles and Aimer 1994, 1.
31 Ibid.
33 Ibid, 201.
early 1990s”, attempting to reframe his government as pragmatic and moderate in comparison.\footnote{Ibid.}

However, as Roper observes, the Fourth National Government did have “one major factor operating in its favour during its second term – a strong economic recovery.”\footnote{Ibid, 202.} As can be seen from Figure 4.1 below, after averaging just 0.8% per annum during the Fourth National Government’s first three years in power, real economic growth reached 6.8% in the year to March 1994, 4.8% in the year to March 1995, and 4.1% in the year to March 1996. This cyclical economic recovery significantly “reduced the fiscal pressures on the state.”\footnote{Roper 2005b, 202.} The upswing in economic activity served to substantially boost the government’s incoming revenues. Having declined markedly during the Fourth National Government’s first term, core government revenues increased from $27.6 billion in the year to March 1993 to $29.0 billion in the year to March 1994, $32.5 billion in the year to March 1995, and $33.8 billion in the year to March 1996.\footnote{Treasury 2014, \textit{Fiscal Time Series} (Wellington: Treasury). It should be noted however, that the initial increase in revenues coincided with the official shift from cash accounting to Generally Accepted Accounting Practice (GAAP) in 1994. This process may account for some of the change in revenue levels.} At the same time, the upswing in economic activity acted to greatly reduce the government’s required outlays for welfare payments. The number of registered unemployed in New Zealand fell from approximately 207,300 to 154,100 during the Fourth National Government’s second term.\footnote{Dalziel and Lattimore 2001, \textit{The New Zealand Macroeconomy: A Briefing on the Reforms and their Legacy} (Melbourne: Oxford University Press), 134-135.} Indeed, the combined impact on the government’s finances was so significant that in 1994 the Fourth National Government was able to post an operating surplus (of $755 million); the first time a New Zealand government had been able to do so since 1978.\footnote{Ibid, 110, 139.}
At New Zealand’s first MMP election, held on 12 October 1996, the Fourth National Government once again retained power. At the election, the opposition Labour Party received 28.2% of the party vote and 37 seats, the Alliance 10.1% and 13 seats, the hardline neoliberal Association of Consumers and Taxpayers (ACT) 6.1% and 7 seats, and United 0.9% and 1 seat. The Fourth National Government, meanwhile, secured just 33.8% of the party vote and 44 seats within the newly expanded 120 seat MMP parliament. Nevertheless, National was able to retain power by enlisting the support of erstwhile critic Winston Peters and his New Zealand First Party. Through opportunistic exploitation of issues such as political corruption, the undue influence of big business within politics, and Asian immigration, New Zealand First had been able to capture a healthy 13.4% of the party vote and 17 seats at

---

40 GDP data based on years ending in March.
41 The United New Zealand Party was formed in mid-1995 from a combination of former National and Labour MPs. In 2000 it merged with the conservative, Christian-dominated Future New Zealand party to form United Future under the leadership of Peter Dunne.
the 1996 election and, inadvertently, also the balance of electoral power.\textsuperscript{43} Despite previously indicating that “the only way to remove National was to vote New Zealand First” (and also a vast majority of party supporters being in opposition to the move), Peters entered his party into a coalition agreement with National on 10 December after a notoriously extended period of negotiations.\textsuperscript{44}

The nation’s much heralded economic upswing came to a swift conclusion soon after the re-election of the Fourth National Government in 1996. As can be seen from Figure 4.1, after reaching over 4\% of GDP in 1996, New Zealand’s economic growth rate fell to 2.4\% in 1997, and then just 0.6\% of GDP in 1998.\textsuperscript{45} Although regional droughts and tightening monetary conditions were certainly important contributing factors, the primary cause of this sharp downward correction in the nation’s short-term economic fortunes was the onset of the 1997-98 East Asian financial crisis.\textsuperscript{46} The immediate trigger of the crisis was the bursting of a speculative property bubble in Thailand. The bursting of the Thai property bubble acted to severely undermine confidence in IPFMs. This sparked a mounting wave of financial turmoil that rapidly spread across the region, initially impacting on the Philippines, Malaysia, and Indonesia, before expanding to Hong Kong, South Korea, and Japan.\textsuperscript{47} The resulting period of severe regional macroeconomic instability significantly


\textsuperscript{45} RBNZ 2014.

\textsuperscript{46} Treasury 1998, “Budget Overview”, 13. Until the GFC in 2008, the 1997-98 East Asian crisis had the dubious distinction of being the worst episode of financial instability of the neoliberal era, a period characterised by its remarkable propensity for crisis.

\textsuperscript{47} The impact of the 1997-98 East Asian crisis was not as geographically restricted as the title suggests. By early 1998, many other so-called ‘emerging economies’ throughout the world had been hit by its effects, most notably Russia.
curtailed New Zealand’s export earnings and, ultimately, overall economic activity.  

Despite specifically stating that “the purpose of the coalition” was “to provide sound and stable Government for New Zealand” in its coalition agreement, the newly formed government proved to be almost inherently unstable. Support for both National and New Zealand First collapsed during 1997. This prompted Ashburton MP Jenny Shipley to successfully challenge Jim Bolger for leadership of the National Party in November. Shipley’s leadership – characterised by a sharp turn back to the right – served to inflame already strained intra-coalition relationships. This culminated with Shipley sacking Winston Peters as Deputy PM and Treasurer in August 1998 and, ultimately, the New Zealand first caucus fragmenting. As a result, for the remainder of its final term (approximately a year), the Fourth National Government operated as a minority government propped up by ACT, United, and a handful of (primarily New Zealand First) defectors.

---

4.2 Fiscal Austerity

On coming into office, the Fourth National Government immediately moved to complete Labour’s “unfinished business.” As Roper outlines, “the Fourth National Government adopted and rapidly implemented the ‘employers’ charter’ for industrial relations, advocated by the Business Roundtable (NZBR) and the Employers’ Federation (NZEF).” This ultimately saw a system of “centralised wage determination” replaced by “decentralised single-employer enterprise bargaining” via the ECA 1991. Simultaneously, the Fourth National Government announced a fundamental “redesign [of] the welfare state.” In order to “reduce the amount and improve the quality of government spending”, the Fourth National Government “recast the levels and forms of social assistance offered by the state” through “a major reorganisation of the institutional structures in housing, health, social welfare and education.” It is outside the ambit of this thesis to discuss in detail all of the major changes the Fourth National Government introduced in the area of industrial relations. However, as will be demonstrated in Section Three, the changes announced by the Fourth National Government in the realm of social policy are integral to our understanding of the role played by the DWSR in New Zealand’s historical shift to neoliberalism and its subsequent retention and entrenchment through to 2011.

Redesigning the Welfare State

The first tranche of reforms constituent of the Fourth National Government’s ‘redesign’ of the welfare state were introduced as part of the Economic and Social Initiative (ESI) announced on 19 December 1990, just two

51 Roper 2005b, 195.
52 Ibid.
53 Roper 2005b, 208-209.
54 J. Bolger in ESI, 11, quoted in Roper 2005b, 197.
55 R. Richardson in ESI, 54, quoted in Roper 2005b, 197.
months after the election. Within the ESI, the Fourth National Government outlined major cuts to the nominal value of core benefit entitlements. The single adult rate for the unemployment benefit was reduced by $14 per week, the widows and domestic purposes benefits were both cut by between 9% and 16%, and the age at which the youth rate for benefits abated was raised from 20 to 25.\textsuperscript{56} As Kelsey observes, this last move effectively constituted a cut “of 24.7%, from $143 to $108 a week”, for those unfortunate enough to be caught within this age bracket.\textsuperscript{57} The Fourth National Government’s Minister of Social Welfare, Jenny Shipley, justified this particularly harsh aspect of the welfare reforms on the somewhat dubious grounds that “generally younger single people are competing for jobs which attract lower wages and they generally have more ability to change their circumstances.”\textsuperscript{58} The only major benefit class not to suffer substantial cuts in nominal terms at this time was that for invalids.\textsuperscript{59} Simultaneously, eligibility criteria for state-funded assistance were tightened significantly. In particular, the stand-down period for those deemed to be ‘voluntarily’ out of work increased from 6 weeks to 6 months and the previously universal family benefit was abolished.\textsuperscript{60} The latter was to be accompanied by a highly targeted “compensatory rise in Family Support for low income families.”\textsuperscript{61} As Dalziel observed, together, these cuts to “core benefit rate[s] and tighter welfare eligibility rules” were expected to slash “$1.275 billion from the social welfare budget in a full fiscal year.”\textsuperscript{62} This was the

\textsuperscript{56} Kelsey 1993, 83.
\textsuperscript{57} Ibid.
\textsuperscript{58} J. Shipley quoted in \textit{New Zealand Herald} 1990, 20 December.
\textsuperscript{59} However, the level of the invalids benefit was frozen in nominal terms by cancelling indexing for inflation. As a result, it was effectively reduced by 4.5% in real terms due to inflation. See J. Boston and P. Dalziel (eds.) 1992, \textit{The Decent Society?} Auckland: Oxford University Press, 11.
\textsuperscript{60} Kelsey 1993, 83.
\textsuperscript{61} Ibid.
\textsuperscript{62} P. Dalziel 1992, “National’s Macroeconomic Policy” in J. Boston and P. Dalziel (eds.), \textit{The Decent Society?} (Auckland: Oxford University Press), 19. This was on top of a further $245 million that was expected to be saved during what remained of the 1990/91 fiscal year. See K. Fowlie 1999, “Automatic Fiscal Stabilisers”, \textit{Treasury Working Paper 99/7} (Wellington: Treasury), 6. Total social security spending (including superannuation) prior to the cuts was around $10.5 billion per annum. See Dalziel and Lattimore 2001, 140.
equivalent of 1.8% of GDP in 1990/91. Alongside these reforms to benefit provision, the Fourth National Government also announced major policy changes relating to national superannuation in the ESI. Inflation indexing of state pension entitlements was cancelled for the following year (constituting an effective 4.5% cut in real terms), and the promised abolition of the superannuation tax surcharge that had been introduced by the previous Labour Government in 1985 was to be deferred indefinitely. In addition, major ministerial expenditure reviews were announced for “welfare, housing, health, education, ACC, and defence”, to be overlooked by the Expenditure Control Committee - popularly referred to as the ‘Razor Gang’.

Budget 1991 formed the second stage of the Fourth National Government’s redesign of the welfare state. Dubbed the ‘Mother of all Budgets’ by Ruth Richardson, it set out a wide-ranging programme of long-term policy initiatives designed to fundamentally restructure the provision of public health, education, and housing along neoliberal lines. A new system of user part-charges for public health services was announced. The public health system as a whole was to be redesigned according to neoliberal principles, with hospitals to become profit-driven Crown Health Enterprises (CHEs). Funding for early childhood education was to be cut significantly. Universal access to a student allowance while studying was abolished, government funding for tertiary education was slashed, a student loan scheme was introduced, and fee setting was shifted to individual universities under the so-called ‘Study Right’ scheme. Commencing on 1 July, 1993, state housing tenants were to be subject

---

63 Fowlie 1999, 7.
64 Kelsey 1993, 83.
67 The Study Right scheme involved introducing a limited ‘user pays’ element into tertiary education funding. The state would cover 80% (later 75%) of the cost of enrolment, with the remainder covered by the student.
to market-based rents. A new ‘accommodation supplement’ would offset some of the associated increase in the cost of renting, but only for those on the lowest incomes. In addition, Budget 1991 continued the severe benefit cuts that the Fourth National Government had begun in the December ESI. The minimum age of eligibility for the sickness, invalids and domestic purposes benefits were all raised from 16 to 18 years and the stand-down provision for ‘high earners’ seeking to move onto the unemployment benefit was extended from six to ten weeks.

Budget 1991 also announced further significant changes in the area of superannuation policy. Indeed, it is apparent that it was intended for these to comprise an “integral part” of National’s broader policy agenda of ‘redesigning’ the welfare state. The indexing for inflation of pension rates was delayed for a further two years, until 1 April 1993. This constituted an additional cut of over 5.3% in real terms. The age of eligibility for National Superannuation was to be raised from 60 to 65 progressively over an extended period of 10 years. As had been promised during the 1990 election campaign (and reiterated in the post-election Speech from the Throne), the existing surcharge on the GRI was scrapped. But while the incumbent ‘claw-back’ policy was abolished as promised, it was ‘coincidentally’ replaced with an even

---

70 Ibid 1993, 84.
71 Ibid 1993. High income earners were officially defined in this instance as those previously earning $22,500 or more per annum.
74 Kelsey 1993, 84.
more harsh new income abatement scheme. St. John delineates the main features of this new abatement scheme:

The gross pension was to be abated at the rate of 90 cents in the dollar for any income above $4,160 per annum, with the exemption level exactly the same for a married couple as for an individual. For married couples under 70, the entire National Superannuation payment would be clawed back once joint income from other sources reached $23,740. For a single person under 70 living alone, the cut-out point was $17,279. Those over 70 were to have only one half of the pension subject to the income test.

Thus, the existing GRI was in-fact “radically modified.” Rather than constituting “a relatively generous universal payment to all regardless of need” (which, St. John notes, would obviously have been “seriously out of kilter with the philosophy expressed in the December [ESI] statement.”), from 1992 onwards National Superannuation would instead “become a tightly income tested welfare benefit.” Ultimately aimed at slashing up to $650 million a year from the Government’s expenditure on National Superannuation, together these moves constituted major cuts to pension entitlements, especially for retirees on lower incomes.

However, the political sustainability of the Government’s budget night superannuation proposals quickly became doubtful. National’s proposed reforms were “profoundly unwelcome” and generated widespread popular resistance. With many of their members facing substantial cuts to their incomes, many retired groups – representing the so-called ‘grey’ vote - were especially ardent in their opposition to the Government’s plans. Internal dissent was also rife. Several National back bench MPs broke party ranks and

77 Kelsey 1993, 84.
78 St. John 1992, 126.
79 Ibid.
80 Ibid, 126, 137. See also Boston 1992, 11.
81 St. John 1992, 126, 141. See also Dalziel 1992, 19.
82 Boston 1992, 11.
83 Vowles et al 1995, 7-8.
84 St. John 1992, 141.
refused to support the Government in passing the proposed legislation.\footnote{M. Russell 1995, *Revolution* (Auckland: Hodder Moa Beckett), 226.} A number of the same backbenchers “openly promoted meetings to help the retired avoid the consequences of the income test.”\footnote{St. John 1992, 141.} The Government’s superannuation proposals were also a key factor motivating the defection of National MP’s Gilbert Myles and Hamish MacIntyre (see Section One).\footnote{Ibid.} Indeed, Myles specifically justified his decision to leave the party on the grounds that National were “looking at trimming the fat where there is no fat to trim.”\footnote{G. Myles 1990, quoted in *New Zealand Herald*, 20 December.} As a result, and despite a party conference speech from Ruth Richardson that “insisted there would be no budging on the budget”, on 3 October 1991, the Fourth National Government publicly announced that it was backing down from the hard line it had taken on superannuation in *Budget 1991*.\footnote{Roper 2005b, 214; M. Russell 1995, 226.} Just over a month later, on 7 November 1991, the Government unveiled a revised set of superannuation policy proposals. Under this adjusted policy package, the existing surcharge - long criticised by National for being “immoral” - was retained.\footnote{St. John 1992, 127.} However, as St. John delineates, it would be even more rigorous than before:

The rate of surcharge was raised from 20 per cent to 25 per cent, and the exemption was lowered to $6,240 per annum for a married couple and to $4,160 per annum for an individual. The universal portion for those over 70 was quietly dropped, along with any suggestion of a joint income test.\footnote{Ibid.}
In addition, the budget night proposals to increase the age of entitlement in a series of steps from 60 to 65 over ten years and to halt inflation adjustment for the pension until 1 April, 1993 both remained in place.\footnote{J. Boston \textit{et al} 1999, “Rebuilding an Effective Welfare State”, in Boston \textit{et al} (eds.), \textit{Redesigning the Welfare State in New Zealand: Problems, Policies, and Prospects} (Auckland: Oxford University Press), 306.}
Table 4.1) Main Features of the Fourth National Government’s Redesign of the Welfare State, 1990 to 1993

<table>
<thead>
<tr>
<th>Social Welfare</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Core benefit entitlement rates, including the unemployment, sickness and domestic purposes benefits, were cut significantly from 1 April 1991.</td>
</tr>
<tr>
<td>• Age of applicability of youth benefit rates for unemployment, domestic purposes, sickness, and invalids benefits raised.</td>
</tr>
<tr>
<td>• Stand-down periods prior to eligibility for the unemployment benefit strengthened substantially.</td>
</tr>
<tr>
<td>• Eligibility criteria for most welfare entitlements tightened significantly.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Superannuation</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Pension rate frozen for three years, until 1 April 1993.</td>
</tr>
<tr>
<td>• Age of eligibility for national superannuation raised from 60 to 65.</td>
</tr>
<tr>
<td>• Promised abolition of the Superannuation tax surcharge deferred indefinitely. 93</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Health</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Universal health subsidies scrapped. Replaced with an extensive system of user part-charges and a highly targeted ‘Community Services Card’. 94</td>
</tr>
<tr>
<td>• Corporatisation of the public health system.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Housing</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Market-based rents for state housing introduced from 1 July 1993, with highly targeted amelioration only available for the very poor via an ‘Accommodation Supplement’.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Education</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Universal student allowance scrapped, replaced with highly targeted assistance.</td>
</tr>
<tr>
<td>• Funding for tertiary education slashed, fee setting simultaneously shifted to universities.</td>
</tr>
<tr>
<td>• Student Loans scheme introduced.</td>
</tr>
<tr>
<td>• Early Childhood Education funding slashed.</td>
</tr>
</tbody>
</table>


Table 4.1 (above) summarises the main features of the Fourth National Government’s fundamental redesign of the New Zealand welfare state that it implemented during its first term. Despite the Government’s late back down on

93 The superannuation surcharge was finally repealed as part of the 1996 National-New Zealand First Coalition Agreement, see below.

94 User part-charges were later abolished due to the high cost and inefficiency of the system. The Community Services Card remains in existence.
some of the harshest aspects of superannuation policy reform proposals and also on some unworkable aspects of its healthcare reforms, as they were intended to do these above outlined measures substantially reduced overall government “expenditure in real terms on a permanent basis.” 95 As a consequence, “the structural deficit [was] virtually eliminated in the 1992/93 fiscal year.” 96 The Fourth National Government achieved “a small but genuine financial surplus” in 1994. 97 This was the first operating surplus recorded in New Zealand in nearly 30 years. Sizeable surpluses were recorded by the Fourth National Government in each year thereafter.

**The Fiscal Responsibility Act**

In July 1994, the Fourth National Government implemented the Fiscal Responsibility Act (FRA). The FRA effectively sought to ‘lock in’ the Fourth National Government’s neoliberal fiscal austerity strategy. 98 It set into legislation five core “principles of responsible fiscal management.” Set out in Section 4, subsection 2 of the Act, these were:

- Reducing crown debt to ‘prudent’ levels.
- Operating budget surpluses on average over the medium term.
- Maintaining a positive crown net worth so as to provide a buffer versus adverse economic or financial shocks.
- ‘Prudent’ management of the Crown’s financial risks.
- Pursuing a policy agenda which provided stable and predictable levels of future taxation. 99

In addition, the FRA also set out an extensive “cycle of financial reporting.” 100 This cycle included a Budget Policy Statement (BPS) before 31

---

95 Rudd 1992, 40.
96 Fowlie 1999, 6.
97 Dalziel and Lattimore 2001, 68.
99 As Dalziel and Lattimore observe, the FRA did not actually define “exactly what a prudent level of total Crown debt is”, however the standard that became generally accepted was “gross public debt below 30 percent of GDP and net public debt below 20 percent of GDP.” See Dalziel and Lattimore 2001, 70.
March each year, an Economic and Fiscal Update and Fiscal Strategy Report (FSR) accompanying the official budget speech in June or July, and, finally, an additional Economic and Fiscal Update in December each year and also prior to any general election. The purpose of this was to effectively make it unlawful for a future government to conceal any deterioration in its financial position, especially before an election. In theory any future government could reverse the FRA. However, as Kelsey observes, with the FRA firmly “embedded in law” this was unlikely to occur; whatever was set down in legislation was likely to be the standard to which future New Zealand governments would adhere.

Dealing to Debt

In accordance with pre-budget publicity, the Fourth National Government announced the delivery of a so-called ‘social dividend’ as a prominent feature of new finance minister Bill Birch’s first budget in 1994. Comprising a small number of new spending initiatives, Birch portrayed this ‘social dividend’ as being indicative of the rewards that could now be expected going forward as payoff “for the years of pain” experienced by many New Zealanders as a result of the decade-long neoliberal ‘structural adjustment’ process. “Mr Speaker, tonight I have been able to report that New Zealand’s ‘quiet revolution’ is now beginning to pay real dividends for New Zealand and New Zealanders.” However, as prominent journalist Colin James pointed out at the time, this ‘social dividend’ constituted “surely one of the most cynical of the public relations ruses dreamt up for Bolger over the past four years.” Overall, the ‘social dividend’ totaled just $375 million. To put this into

\[100\] ibid.
\[101\] ibid.
\[102\] ibid, 70-71.
\[103\] Kelsey 1997, 238-239.
\[105\] Kelsey 1997, 231.
perspective, the recorded operating surplus for the same 1994/95 financial year was $2.7 billion. Health received the bulk of the new funding. Some $241 million of additional spending on health was announced for the 1994/95 financial year. But, as James again points out, “most of the extra funding for health came in the shape of balance sheet restructuring for the struggling CHEs.” The Government was to write-off nearly $300 million of accumulated debt from CHE balance sheets, whilst simultaneously providing new equity of $100 million to CHEs and a conditional loan of up to $140 million. Moreover, both the equity injection and additional lending were only to be advanced against strict criteria. Education received a share of the ‘social dividend’ worth $151 million spread over three years. Over 10% - $17 million – “of this new expenditure, however, [was only] made possible through savings [made] elsewhere in education.” Thereby, the Fourth National Government effectively masked what was in-fact a much smaller funding increase. The Family Support programme for low-income households was accorded a funding increase of $67 million a year. The Government expected this increased assistance to reach some 170,000 families. However, as Kelsey observes, “for a single mother with two children whose domestic purposes benefit had been cut in 1991 by $26 a week, it meant an extra $3 a week.”

Simultaneous to the announcement of this ‘social dividend’, the Fourth National Government outlined its broader short-term fiscal strategy. This encompassed the Government’s fiscal policy agenda for the period spanning the next three years. The over-arching objective of this strategy was “dealing to debt.” Indeed, as Bolger notes in his 1997 autobiography A View from the Top,

---

111 Kelsey 1997, 231.
112 Treasury 1994, Budget 1994 (Wellington: Treasury). This overarching ‘low debt’ objective had been previously indicated in both the policy document The Next Three Years released two weeks prior to the
“Bill Birch made debt reduction the centerpiece of his budget presentation.”\textsuperscript{113} As set out in the Government’s 1994 \textit{Fiscal Strategy Report}, net public debt was to be reduced from 42.1\% of GDP to the more “prudent” level of below 30\% of GDP by June 1997.\textsuperscript{114} In more concrete terms, this entailed net public debt falling by $7.43\ billion over three years, from $35.56\ billion to $28.13\ billion.\textsuperscript{115} Within the overarching debt reduction strategy, “a key priority” would be to retire and, if possible, eliminate foreign currency-denominated debt.\textsuperscript{116}

The main driver of this ‘low debt’ fiscal strategy was to be the accumulation of large surpluses “for at least the next three years.”\textsuperscript{117} The Government expected to record “a surplus on the adjusted financial balance” of $730\ million in 1994/95. “Even larger surpluses...[were] projected for the [following] two years: $2.49\ billion in 1995/96, and $4.53\ billion in 1996/97.”\textsuperscript{118} These “cash-flow surpluses” were to be primarily generated from \textit{within} existing government operations; there was to be no increases made to statutory tax rates.\textsuperscript{119} A ‘tight rein’ would continue to be maintained over government expenditure. There was to be little new spending during the following three years. What new spending there was would be largely concentrated in the Government’s ‘priority areas’ of health and education.\textsuperscript{120} Defence spending would be cut.\textsuperscript{121} “Chief executives in the public service”, meanwhile, would be required to work largely from within existing baselines, and also to cooperate “with Ministers to reprioritise their spending”, increase public sector “efficiency”, and “achieve savings.”\textsuperscript{122}

\begin{thebibliography}{99}
\bibitem{113} J. Bolger 1998, \textit{A View From the Top} (Auckland: Viking), 197.
\bibitem{116} ibid, “Speech”, 25.
\bibitem{118} ibid, 7.
\bibitem{119} ibid FSR, 31, 41.
\bibitem{120} ibid 41.
\end{thebibliography}
An ongoing programme of privatisations would play an important secondary role in the Government’s debt reduction strategy, as would the progressive reduction of public debt itself. Prior to the budget, the Fourth National Government had outlined a renewed programme of state asset sales. This included “the divestment of Landcorp, Workscorp, and…Government Property Services Limited”, as well as the sale of Government Computer Services (GCS) Limited, the state-owned computer company.\(^\text{123}\) As stated in the 1994 *Fiscal Strategy Report*, “the Government [was] not prepared to meet its debt objective from the proceeds of [such] asset sales.”\(^\text{124}\) However, “any surpluses from investing activities” would nevertheless “be used to make additional reductions in public debt.”\(^\text{125}\) Meanwhile, as noted in the 1994 budget document *Public Debt Goal*, as at 30 June 1993 the Government’s debt servicing bill amounted to some $3.6 billion per annum. This was equivalent to around 13% of total government spending that year.\(^\text{126}\) By opting to vigorously ‘deal to debt’ in the immediate term, the Government would effectively be acting to reduce this major component of overall expenditure. Not insubstantial tax-payer funds previously tied up servicing debt would be progressively freed up over the following three years, thereby allowing them to be applied to further repayment of the public debt principle.

In the following year, the Fourth National Government announced that it would be adopting what it considered to be a “balanced approach” to the formulation of fiscal policy.\(^\text{127}\) As part of this, Finance Minister Birch announced a new programme of social spending. Overall, this new spending would “average around $600 million in each of the next three years” and would be largely concentrated “in the important social areas of education, health, and

---
\(^{124}\) Ibid, FSR, 31.  
\(^{125}\) Ibid.  
welfare.” Acceded the distinction of being the “the top expenditure priority in this [1995] Budget”, education received the largest portion of the new funding - $654 million over three years. This included, most prominently: a $217 million increase for general operating expenses; $184 million for capital investment in the primary and secondary sectors; a $66 million increase in operating funding for tertiary institutions; and $57 million for Early Childhood Education (ECE). Health, respectively, was allocated additional funding of around $667 million, also spread over three years. As had previously been announced in late 1994, $152 million of this would be available for immediate use in the coming 1995/96 year, alongside a further $190 million (that is, additional to the $667 million) specifically for the purposes of “maintaining and upgrading hospitals.” Welfare funding, meanwhile, was increased by around $50 million a year, for the following three years. The main initiatives to derive from this funding increase were a slight easing of eligibility rules for Special Needs Grants and Special Benefits and extra funding for state housing.

But, despite appearances, this “balanced approach” did not diverge significantly from the “surplus-driven, low debt” fiscal strategy set out by the Fourth National Government the year before. Once again, debt reduction would be the primary focus in Budget 1995. Net government debt was to be reduced by a further $2.3 billion over the course of the 1995/96 fiscal year, bringing overall net government debt down to $30.8 billion or 33.6% of GDP. In order to achieve this, the Government continued to maintain “firm overall expense control” in 1995, and this was “projected to be sustained over the next

---

128 Ibid, 5.
129 Ibid, 8.
132 Ibid.
133 Ibid, 11.
As outlined in Treasury’s 1995 *Fiscal Strategy Report*, “in dollar terms”, overall government “spending [only rose] by around $900 million in 1995/96.” This constituted just a 3.0% nominal increase compared to the previous year. CPI inflation in the same year was 2.2%, meaning that the overall increase was minuscule in real terms. The increased spending was also largely concentrated in the Government’s so-called ‘priority areas’. “Over 90% of the net increase in spending [was] accounted for by increases in education, health and welfare spending.” Most government departments and agencies received no additional funding. Instead, they were required to fund any new policy initiatives from within existing baselines by “shifting resources from lower priority areas”, whilst simultaneously seeking to achieve further “efficiencies.” The 1995 budget’s flagship programme of new priority social spending, meanwhile, was to a significant extent (though not entirely) fiscally neutral. As outlined above, the spending package entailed a $1.8 billion spending increase over three years. However, $1.2 billion of this was to be directly offset by a commensurate fall in public debt servicing costs, and another $60 million of the $149 million specifically earmarked for new welfare funding was to be derived from “firmer benefit administration.”

**Moderation**

As previously discussed in Section One, beginning in late 1992, New Zealand experienced a strong cyclical economic recovery which had the effect of significantly boosting public revenues ahead of expectations whilst simultaneously reducing social welfare outlays. This, combined with the Fourth

---

137 Ibid, FSR, 27.
138 Ibid.
141 Ibid, 29.
142 Treasury 1995, FSR, 30, 32. Kelsey outlines that “firmer benefit administration” here primarily referred to the scrapping of eligibility of 16 and 17 year olds for student and job search allowances, various training benefits, and also the sickness benefit from 1 January 1996. This effectively served to cut off around 8000 young people from welfare payments. See Kelsey 1997, 232.
National Government’s continued maintenance of a relatively tight fiscal stance (despite having dumped Ruth Richardson as Minister of Finance), meant that “substantial progress towards reducing net public debt” was made during the 1994/95 fiscal year.\(^\text{143}\) Net public debt was reduced by around $2.5 billion in the year to 30 June 1995, bringing total net debt down to $33 billion or 37.9% of GDP (that is, 1.7% of GDP ahead of the schedule laid out in *Budget 1994*).\(^\text{144}\) Of even more importance, however, projections also revealed the future path of public debt reduction quickly moving far ahead of what had been previously anticipated.\(^\text{145}\) Based on budget night figures net public debt was set to almost halve during the following three years. The 1995 budget *Executive Summary* states that, with no alterations to current fiscal settings, “net public debt is projected to fall from 33.6% of GDP at 30 June 1996 to [just] 18.7% of GDP by 30 June 1998.”\(^\text{146}\) Figure 4.2 compares this projected future track of public debt reduction with that originally set out in *Budget 1994*. Powering this forecast surge in debt reduction was a substantial increase in the expected size of future surpluses. The operating surplus was expected to blowout to the equivalent of over 8% of GDP in the very near future if the Fourth National Government’s tax and spending plans went unchanged.\(^\text{147}\) As can be seen from Figure 4.3, *Budget 1995* forecast the operating surplus to increase from around $3.3 billion in 1995, to $5.4 billion in 1996, and to a staggering $7.8 billion in 1997.\(^\text{148}\)

\(^{143}\) Treasury 1995, FSR, 24.

\(^{144}\) Ibid; 1994, FSR, 34.


\(^{147}\) Fowlie 1999, 7; Treasury 1995, FSR, 26.

\(^{148}\) Bolger 1998, 199-200; Treasury 1995 “Executive Summary”, 4; Speech, 16.
Figure 4.2) Comparison of Actual, Forecast, and Projected Paths of Net Debt Reduction contained in the 1994 and 1995 Budgets (% of GDP)


Figure 4.3) Comparison of Actual, Forecast, and Projected Operating Balances contained in the 1994 and 1995 Budgets ($billion)

Subsequently, although it had previously signaled that it would continue to maintain a relatively tight fiscal stance in the medium term, in 1996 the Fourth National Government noticeably “loosened the purse-strings.” The “centre piece” of the third Birch Budget, delivered at 2pm on Thursday, 23 May 1996, was a “Tax Reduction and Social Policy Programme” (TRSPP). As Birch himself outlined, the “key components” of the TRSPP were a two year programme of personal tax cuts (policy which had been clearly signaled by the National Government since 1994), increased Family Support, and the introduction of a new “Independent Family Tax Credit [(IFTC)] for working low- and middle-income families.” In two stages, timed one year apart and commencing on 1 July 1996, the middle marginal income tax rate would be dropped from 24% to 19.5%, and the upper threshold to which the same rate applied would be progressively raised from $30,875 p.a. to $38,000 p.a. The top, company, and lower tax brackets would remain unchanged at 33%, 33%, and 15% respectively. Constituting the first alteration of the country’s income tax scale since 1 October 1988, overall the personal tax cut package “was designed to return over $3 billion, over the next two years, to working New Zealanders.” Family Support entitlements, meanwhile, would increase by $2.50 per week, per child coinciding with each stage of the proposed tax cuts, and working families earning $20,000 or less a year would receive an IFTC worth $7.50 per child, per week, rising to $15 in 1997. The Fourth National Government estimated that up to 150,000 households would be eligible to receive the new IFTC. Together, this latter pairing of initiatives was expected to

---

151 Ibid.
155 Ibid.
to cost an additional $500 million.\textsuperscript{156} Other important components of the 1996 TRSPP were an increase of the threshold for the superannuation surcharge by $20 per week for single retirees and $30 per week for couples, and a parallel increase of the guaranteed minimum family income from $278 per week to $290 per week. As with the rest of the TRSPP, both of these initiatives were also to be implemented in two tranches, the last on 1 July 1997.\textsuperscript{157} Table 4.2 below sets out all of the major components of the Tax Reduction and Social Policy Programme contained in \textit{Budget 1996}.

\textsuperscript{156} Ibid.

\textsuperscript{157} Ibid.
In support of the TRSPP, the Fourth National Government also pursued what it described as “an aggressive spending programme in priority areas” in Budget 1996.\footnote{Treasury 1996 “Ministerial Statement”, 6.} Corresponding with its previous second term budgets, the lead elements of this ‘aggressive’ new spending programme consisted of significant new spending increases in the areas of health and education. The Fourth National Government outlined $733 million of new expenditure on health to be delivered over three years in Budget 1996. Base operating funding was increased by $349 million over three years, acute services received a permanent, ongoing
funding increase of an extra $45 million per year, and elective services received $40 million over two years as well as with a one-off provision of an additional $130 million specifically for the purpose of clearing a growing – and politically damaging – backlog of elective surgeries in the public health system.159 Simultaneously, the Fourth National Government announced $419 million of new spending spread over three years for education. The base operations grant - “funds allocated to schools to spend at their own discretion” - was increased by $75 million over three years, Special Education received “a major gain” of $55 million over three years, and an additional $206 million over three years was provided for a variety of “new education initiatives” spread across early childhood, primary, secondary, and tertiary education.160 Other lesser, but still relatively substantive, elements of the Fourth National Government’s ‘aggressive’ new spending programme included a three-year, $110 million ‘Green Package’, and $119 million over three years for the purpose of “Strengthening our communities.”161 Cumulatively, this “aggressive spending programme” pursued by the Fourth National Government in Budget 1996, combined with the other new spending and revenue initiatives, was expected to amount to a further $1.7 billion of new spending spread over three years.162

It is worth noting that there was little in the TRSPP for beneficiaries.163 Indeed, they were effectively excluded from almost all of it.164 As Herbert observes, because “benefits are paid on an after tax basis” in New Zealand, beneficiaries were completely left out of the new tax cut programme and, as they were not in paid full-time work, they were also ineligible for the IFTC.165 Conversely, as Boston et al point out, “middle- and upper-income households

159 Ibid, 7.
162 Ibid.
163 Rudd 1996 in Miller, 264.
gained significantly” from the TRSPP.\footnote{Boston et al 1999. Vi.} The bulk of the value of the tax cut package accrued to those earning middle incomes and higher.\footnote{P. Dalziel 1999, “Macroeconomic Constraints” in ibid, 71-73.}

Further “fiscal easing” was announced as a key plank of the Coalition Agreement eventually signed by the new National-New Zealand First Government.\footnote{Fowlie 1999, 7.} Centrally, this comprised a “comprehensive social policy programme” worth an aggregate of $5 billion spread over three years.\footnote{Treasury 1998, “Budget Overview” (Wellington: Treasury), 1.} That is, “up to $1.2 billion in 1997/98; up to $1.7 billion in 1998/99; and up to $2.1 billion in 1999/2000.”\footnote{Bolger and Peters, 62.} This constituted the largest increase in discretionary public expenditure announced in a single year since Muldoon’s 1983 ‘Think Big’ programme. Funding for the extra social spending was provided, in part, by delaying the second round of 1996 tax cuts by a year (excluding “the increases to the Independent Family Tax Credit and Family Support”), and also by accepting lower surpluses of around 2.5% of GDP (instead of the potentially 8% of GDP forecast in \textit{Budget 1995}) over the three years to 1999/2000.\footnote{Ibid, 63.}

The first tranche of the Coalition Government’s three year, $5 billion social policy package was delivered as part of their debut budget presented on 26 June, 1997.\footnote{Treasury 1997, “Treasurer’s Statement and Overview” (Wellington: Treasury), 3.} The core component of the new social spending was to be a substantial increase in the funding available to the Coalition’s “principle priority areas” of health and education.\footnote{Ibid, 4.} New spending worth $355 million over three years was announced for the education portfolio by the Fourth National Government in \textit{Budget 1997}. New spending worth $900 million over three years (three tranches of $300 million a year) was announced for health.\footnote{Ibid.} “On top of this” the Fourth National Government signaled that it also intended to allocate the health portfolio “a further $180 million per year in the 1998
Completing the Shift to Neoliberalism

Budget, increasing to $450 million [per year] in the 1999 Budget. Other important components of the Coalition’s new social expenditure programme delivered as part of Budget 1997 were the abolition of the politically-charged superannuation surcharge from 1 April 1998 and increases to the Accommodation Supplement and Special Benefit at a cost of $554 million and $151 million (over three years) respectively. Alongside these announced increases in operational funding, Budget 1997 also allocated $350 million for new capital expenditure. This was primarily for hospitals ($148 million) and schools ($120 million), but there was also “a significant allocation for the justice sector” ($85 million). In addition, a further $1 billion was earmarked as a “policy contingency” in order to enable the funding of further social spending initiatives in the future. In total, Budget 1997 allocated $900 million in the 1997/98 financial year and $3.3 billion over three years to newly announced social policy initiatives.

As expected, Budget 1998 continued the delivery of the Coalition Government’s three-year, $5 billion social policy programme. Building on the measures implemented during the Coalition’s first year, the core of this second installment consisted of additional funding increases for public health and education provision, as well as law and order enforcement. The Coalition Government announced $1.03 billion of new spending over three years on health, and $340 million of new spending over three years on education in Budget 1998. Law and order, meanwhile, received additional funding worth a total of $257 million over three years. This included, most prominently, the provision of the resources required for the recruitment of 214 additional police

---

178 Ibid.
179 Ibid, 3.
181 Ibid, BPS (Wellington: Treasury), 5.
officers (114 in 1998/99 and 100 in 1999/2000). Budget 1998 also “increased the overall level of resources available for implementing [the Coalition Government’s] employment strategy.” This entailed increased funding for a number of different initiatives worth a total of “$142 million in 1998/99 and $125 million in 1999/2000.”.

The 1997-98 East Asian Crisis and the Return to Austerity

The specific combination of fiscal policy initiatives implemented during the period spanning from mid-1996 to mid-1998 entailed a noticeable ‘loosening’ of the Fourth National Government’s previously persistently tight fiscal stance. Having been held more or less steady (in nominal terms) at a depressed level for several years after Ruth Richardson’s successful imposition of fiscal austerity, Government expenditure increased markedly as the Budget 1996 tax and spending initiatives took effect. As can be seen from Figure 4.4 below, from a level of $31,743 million in 1996, total government spending increased by over $1200 million to $32,953 million in 1997. This trend gained further momentum with the implementation of the Coalition’s social spending package in 1997 and 1998. Total government expenditure increased a further $1206 million to $34,211 million in 1998 and another $1600 million to $35,825 million in 1999. So, to clarify, between the end of the Fourth National Government’s first term and mid-1996, total government spending increased just $314 million in nominal terms. Then between mid-1996 and mid-1999, annual government expenditure increased by almost $4100 million (and this does not include the cost of tax cuts).

---

184 Fowlie, 7.
185 Dalziel and Lattimore 2001, 140. Note that the figures quoted above do not include the fiscal cost of the 1996 tax cut programme.
However, this fiscal ‘loosening’ only constituted a moderation of the Fourth National Government’s overarching neoliberal fiscal strategy. \(^{186}\) Although undoubtedly lower than those forecast in \textit{Budget 1995} (documented above), both the initial Fourth National Government and succeeding New Zealand First-National Coalition Government continued to record not inconsiderable operating surpluses during the period from 1996 to 1998. \(^{187}\) Following the $3.3 billion surplus recorded for the 1995/96 fiscal year, the Government accumulated surpluses totaling $1.9 billion in 1996/97, $2.5 billion in 1997/98, and $1.8 billion in 1998/99. \(^{188}\) Further, “reflecting the ongoing application of cash surpluses to debt repayment”, net crown debt also continued to decline quickly over the full period of the ‘fiscal easing’. \(^{189}\) Figure 4.5 compares the forecast path of debt reduction contained in \textit{Budget 1995} to the

---

\(^{186}\) B. Easton 1999, \textit{The Whimpering of the State} (Auckland: Auckland University Press), 44.


\(^{188}\) Dalziel and Lattimore 2001, 139.

actual recorded path of public debt reduction. As can be seen, while “the
decline in crown debt is [generally] slower and the debt profile higher” than
projected in the 1995 budget, the actual debt reduction track nevertheless did
not deviate substantially from the Fourth National Government’s previous
policy direction (that laid out in the Budget 1994 FSR and documented
previously). From a level equivalent to 31.3% of GDP in 1995/96, net public debt
fell to 26.7% of GDP in 1996/97, through 24.6% of GDP in 1997/98, and reached
21.9% of GDP by the end of the 1998/99 fiscal year. Thus, despite some
contemporary claims to the contrary, the expansion of government expenditure
during the period from mid-1996 to mid-1998 did not represent a policy
direction “radically at odds” with the previous direction of National party
policy.\textsuperscript{190} Rather, as Dalziel observed at the time, during the period from mid-
1996 to mid-1998, the Government had in-fact persisted with its previous fiscal
strategy but had “softened it at the edges.” “It [was] essentially in the same
direction but with more money available on the fringes.”\textsuperscript{191}

\textsuperscript{190} See, for example, C. Trotter 1997, “Who’s Winning? The Nats’ Neoliberals or Win’s Conservatives?”,

\textsuperscript{191} P. Dalziel 1997, quoted in “Economy set spending limit, says lecturer”, \textit{The Press}, 27 June. On this
point, see also Easton 1999, 46; C. James 1997, “Coalition Partners Find Little to Cheer About in Budget”,
In addition, this moderation proved to be only temporary. In the 1996 Coalition Agreement document, the new Government’s flagship social spending package featured prominently. Ostensibly “aimed at addressing the economic and social issues facing New Zealand” (specifically defined as: “economic soundness, fairness, equity, inclusion and consultation”), the three-year, $5 billion social programme was set out over 49 pages in the very first schedule of the 68-page agreement. But there was also a second schedule in the Coalition Agreement. This comparatively short 2-page schedule stated that, while overall spending was expected to increase during the forthcoming parliamentary term, the Coalition would nevertheless continue to “maintain a prudent approach to fiscal policy.” Any further expenditure would be balanced by further tax reductions and public debt repayment, and, most importantly, would be entirely “subject to the [continued] availability of adequate surpluses.” As Easton

---

193 Bolger and Peters, 62.
194 Ibid. Emphasis added.
points out, “despite the ordering it appears that the second schedule was [always] intended to dominate the first.”

The broader process of ‘fiscal easing’ was also predicated on an assumption of continued robust economic growth. As Easton observes, despite the fact that the economy was already showing signs of slowing down before the 1996 general election, “the established forecasters remained broadly optimistic” about New Zealand’s medium to long-term economic prospects. In the 1996 December Economic and Fiscal Update, for example, the Treasury projected “GDP growth of 3.4% on the average over the three years to March 2000.” Similar, though somewhat less rosy, forecasts were presented by Treasury in Budget 1997. Essentially, continued strong economic growth was expected to progressively reduce the fiscal pressures faced by the state. Employment would increase and unemployment would commensurately decrease thereby reducing social welfare outlays. Simultaneously, tax revenues would increase (even with the Fourth National Government’s promised tax cuts). Ultimately, these factors would grant the state greatly enhanced flexibility in relation to fiscal policy formulation.

It is apparent that both the Treasury and the Fourth National Government had bought into their own hype regarding the fundamental success of the decade-long neoliberal reform process. Budget 1997 states, for example, that “over the medium term, the Treasury’s analysis suggests that the economy should be able to sustain growth rates of around 3% to 3.5% per annum. In part this reflects the ongoing benefits of a more open and

---

195 Easton 1999, 47.
197 Easton 1999, 46.
198 Bolger and Peters, 62.
199 See, for example, Treasury 1997, “Speech”, 10, 15-16.
200 Despite the previously documented fundamental redesign and downsizing of the welfare state undertaken from 1990 to 1993, social welfare expenditure continued to comprise nearly 40% of total government expenditure in 1997/98. See Dalziel and Lattimore 2001, 140.
competitive environment created by the extensive reforms of the last decade.”

According to the official narrative, as “a paragon of free-market economics and fiscal and monetary prudence”, it was now “springtime in the New Zealand economy.” As a direct consequence of the so-called ‘New Zealand Experiment’, the country had moved onto a fundamentally higher plane of economic endeavor:

Today’s [economic] performance is very different to the short-lived recoveries we have experienced over the past 20 years. It is not the result of extra Government spending, or a big pickup in overseas prices or demand for a few of our agricultural products. In a major break from the past, the economy is not expected to go into the “boom-bust” pattern we have so often seen.

New Zealand had instead entered into a “virtuous circle” of perpetually strong economic growth and prosperity. But the expected continuation of strong economic growth failed to materialise. As discussed in detail in the previous section, beginning in late 1997, New Zealand experienced a relatively sharp economic downturn due in part to regional droughts, tightening monetary policy, and, most significantly, the impact of the Asian financial crisis and associated financial market volatility.

Consequently, at the same time as it delivered the second installment of its three-year, $5 billion social spending package, the Coalition Government moved to tighten up its fiscal stance. The as yet unallocated portion of the $5 billion allowance for new spending was cut by $300 million, from $1.7 billion to $1.4 billion. This involved an immediate $150 million reduction in the current

---

206 Easton 1999, 42, 46-47.
1998/99 fiscal year, followed by a further $150 million reduction in 1999/2000. This trimming back of planned social spending was accompanied by a revision of the Fourth National Government’s debt reduction targets. With the existing “goal of net debt of 20% of GDP…forecast to be met by 2000/01”, the Coalition established a new target of net debt being reduced to below 15% of GDP within five years.208

Further fiscal retrenchment was announced in late 1998. It formed the core feature of the ‘Policies for Progress’ package introduced by new Prime Minister Jenny Shipley on 29 September. Described by opposition leader Helen Clark as “a cowardly, vicious, and underhanded move”, the cornerstone initiative of this policy package was a reduction in the minimum rate of national superannuation provision. Beginning on 1 April 1999, the extant level of 65% of the average wage was to be cut to 60%. This was “to be phased in by not increasing the pension until the new floor was reached.” While only expected to provide the Government with minimal immediate fiscal benefits (estimated at just $22 million during the remainder of the 1998/99 financial year), implementing this cut to future pension rates was ultimately “expected to save the Government NZ$2.6 billion over ten years.” The other major fiscal initiative announced as part of the ‘Policies for Progress’ package was the Government’s intention to sell the country’s second largest power producer, Contact Energy. With a book value of some $860 million at the time (according to Treasurer Bill Birch), this move was expected to generate a revenue boost of more than $1 billion. In addition to this one-off cash-injection, the sale of Contact was also “expected to cut the Government’s debt servicing costs by about $35 million a year.” In total, the initiatives announced as part of the ‘Policies for Progress’ package were expected to cut government spending by a total of $400 million over the following three years.

To the apparent chagrin of the New Zealand Business Roundtable (NZBR) who sought “an alternative medium-term strategy of vigorous expenditure and tax cuts”, Budget 1999 did not continue to cut government spending. Nevertheless, it did effectively curtail it. As indicated in Figure 4.4 above, total government expenditure increased just $346 million in 1999/2000. This was just a 0.96% nominal increase compared to the previous fiscal year which, in a year when CPI inflation stood at 1.5%, actually constituted a slight reduction in real terms. Overall, the 1999 budget policy package had included initiatives worth some $1.6 billion spread over the following three years. The leading element of the package, however, was a new programme of “tax reductions worth more than $200 million a year to the tax paying public.” The abolition of the public broadcasting fee accounted for around half of the value of the programme ($97 million a year), with the abolition of stamp duties ($77 million a year), and the introduction of a new parental tax credit making up the rest ($29 million) a year. This left just $1 billion available for actual new spending over three years. Of this, Health was the only Vote to receive a substantive portion; $644 million over three years was earmarked for new spending in this area. Education, the second largest spending component in the 1999 Budget package, in comparison received just $179 million over three years. Delivered in the form of 1.6% increase in general operational funding, in essence, Budget 1999 only provided for the indexation of education funding for inflation for the following three years. All other policy areas combined received additional funding of just $279 million over three years in Budget 1999.
4.3) Explaining Fiscal Austerity

Implementation

Corresponding with the situation that had prevailed under the previous Fourth Labour Government, Treasury again played a major role in the development and implementation of the neoliberal policy agenda pursued in New Zealand during the period from 1990 to 1994. As Kelsey observes, Treasury’s “influence [had] waned somewhat during the later 1980s.”217 The marginalisation of Roger Douglas within the Labour cabinet due to mounting intra-party tensions over the policy direction of the Fourth Labour Government resulted in a parallel side-lining of Treasury. However, “under Richardson’s patronage in the early 1990s” Treasury’s previously high level of “influence [was] revived.”218 Once more, the Treasury became a central player in public policy making. To have an accurate indication of what the Fourth National Government actually intended to do, one would be far better served reading Treasury’s briefing papers than official party programmes.219

As noted in Section 4.1, by early 1990 significant deterioration was becoming apparent in the New Zealand economy “despite the magnitude of the policy reforms undertaken” by the Fourth Labour Government over the previous six years.220 Many critics placed blame for the country’s continuing poor economic performance on the “over-vigorous monetary disinflation” that had been steadfastly pursued by the Fourth Labour Government (with the vocal backing of Treasury).221 Overly tight domestic monetary conditions - ostensibly aimed at stamping out inflation – were considered to have produced a drastic “contraction in aggregate demand” which, in turn, had resulted in

217 Kelsey 1997, 50.
218 Ibid.
221 Dalziel 1991, 262; McKinnon, 340.
significantly curtailed domestic economic activity and employment. Treasury acknowledged that the economy had not performed well in recent years:

The results of New Zealand’s economic reforms in terms of growth and employment have been disappointing. Some pain was inevitable during economic restructuring. But the costs of adjustment have been higher than they needed to be, and the benefits have been delayed.

However, Treasury rejected the notion that tight monetary policy was the main cause of the country’s economic underperformance. Instead, primary blame was placed on a lack of overall coherence in the formulation of government macroeconomic policy. In particular, overly loose fiscal policy was cited as undermining the efficacy of Labour’s disinflation strategy.

As discussed in the previous chapter, during the period from 1984 to 1990 the Fourth Labour Government had made a “determined” effort to pursue a neoliberal fiscal austerity agenda. State subsidies of agriculture and industry were cut, Government departments were corporatised and other state assets privatised, the regressive GST consumption tax was introduced (and subsequently raised), and various tax exemptions were scrapped. As Dalziel outlines, these measures “did much to bring the [Fourth Labour] Government’s accounts back towards balance.” However, in terms of achieving its goal of ‘fiscal restraint’ the Fourth Labour Government ultimately came up short; significant and ongoing budgetary deficits were passed on to the incoming Fourth National Government at the 1990 election.

---

224 Ibid.
225 Ibid. 2. Treasury also noted factors outside of government control such as having contributed to New Zealand’s economic deterioration. In particular, “adverse events and trends in the world economy, especially in the markets for some of our major exports.” See Treasury 1990, 2.
226 Dalziel 1992, 22.
227 Ibid.
228 Fowlie 1999, 3.
Treasury argued that these ongoing fiscal deficits had generated upward pressures on domestic interest rates, with the resulting high interest rates suppressing new investment and simultaneously increasing the exchange rate.\(^\text{229}\) The unnecessarily inflated New Zealand currency had, in-turn, placed considerable extra competitive pressures on exporters by undermining their price competitiveness, resulting in both a “reduction in output” and “a major loss of jobs.”\(^\text{230}\)

In order to eliminate the apparent inconsistency in the country’s macroeconomic policy framework, and thus ameliorate New Zealand’s sclerotic economic performance, Treasury advised the incoming National government to pursue what it was now terming “fiscal consolidation.”\(^\text{231}\) Centrally, this would entail an array of major spending cuts. “Reductions in government expenditure should be the primary means of reducing the deficit”, argued Treasury.\(^\text{232}\) Social welfare, education, and health – the core elements of the New Zealand welfare state – were to be the focus of these cuts.\(^\text{233}\) Treasury advised haste in implementing its proposed fiscal austerity agenda. “The fiscal problem is very large and it should be dealt with as quickly as is practicable. The timing of actions should be as fast as is consistent with careful decision-making and sound implementation.”\(^\text{234}\) Raising additional taxes, meanwhile, was rejected outright as a viable method of deficit reduction.\(^\text{235}\)

National’s incoming Minister of Finance, Ruth Richardson, was highly amenable to the Treasury message.\(^\text{236}\) Richardson was a committed, long-standing Libertarian and member of the neoliberal Mont Pelerin Society. She accepted Treasury’s neoclassical explanation of New Zealand’s on-going

\(^{229}\) Treasury 1990, 4, 7, 40-41.
\(^{230}\) Ibid, 44.
\(^{231}\) McKinnon, 346; Treasury 1990, 28. See also Goldfinch 2000, 115.
\(^{232}\) Treasury 1990, 28.
\(^{233}\) Goldfinch 2000, 115; Treasury 1990, 2; Kelsey 1997, 228.
\(^{234}\) Treasury 1990, 3.
\(^{235}\) Kelsey 1997, 228.
\(^{236}\) McKinnon, 349.
economic difficulties at face value and subsequently implemented the bulk of Treasury’s policy prescriptions. However, as Richardson herself observes, “there was no question of Treasury capturing the [policy] agenda.” A free-market faction (led by Richardson) had taken effective control of the National Party in the years leading up to 1990. After their defeat at the 1984 election, the National Party had endured a prolonged period of factional infighting and electoral ineffectiveness. This came to an end in late 1987. Following an unsuccessful challenge for the deputy leadership, Ruth Richardson, was elevated to the position of party finance spokesperson by new National Party leader Jim Bolger. Richardson quickly moved to build a powerful team of like-minded, pro-neoliberal MPs around her. As journalist Denis Welch observed, by mid-1988, “Richardson’s team” had become “the engine-room of party policy direction and growth.”

Richardson’s free-market faction had already determined the broad direction a new National Government would take well in advance of the 1990 election. “We came to office ready to hit the ground running”, states Richardson, “we had our agenda.” Government spending was “to be substantially reduced” and the fiscal deficit was to be eliminated. A radical restructuring and downsizing of the welfare state was determined to be the primary means by which this would be achieved. Funding for the welfare state was easily the largest component of government expenditure at the outset.
of the Fourth National Government’s first term. Furthermore, social spending is characterised by a prominent ‘cyclical demand’ aspect which, as Kelsey observes, makes it “difficult to control without changing levels of benefits and eligibility.” Therefore, in order to rebalance the nation’s public finances, Richardson determined that it was necessary for the Fourth National Government to seek to make considerable savings in this area.

As Kelsey observes, the free-marketeer’s policy agenda was primarily driven by “deeply ideological, rather than fiscal, considerations.” Fundamentally, the goal of National’s neoliberal caucus faction was to substantially reduce the size of the state in New Zealand. “We are determined to shift the balance of resources from the state towards the private enterprise sector”, stated Jim Bolger in one pre-election speech. National’s neoliberal caucus faction firmly believed that it was the size of the state that was the ultimate cause of New Zealand’s ongoing economic problems. “The state was stifling us as New Zealanders and was knocking the stuffing out of the economy”, recalls Richardson. At around 40% of GDP, public sector spending was “a crushing burden” that was having a profound negative impact on New Zealand’s economic growth by undermining “the initiative and the energy of New Zealand’s wealth creators.”

Therefore, in contrast to the situation that prevailed from 1984 to 1990, the continuation of the neoliberal revolution in New Zealand from 1990 to 1994 did not entail a “case of the bureaucratic and ideological capture” of the Fourth

---

246 Rudd documents that social spending had reached over 60% of total government expenditure in the 1989/90 financial year and was projected to increase significantly further. See Rudd 1992, 49-50.
252 Richardson 1990, ESI.
National Government by Treasury. Instead, it was Richardson’s neoliberal cabinet faction that crafted the agenda. Treasury’s role was more of a supporting one, primarily involving the provision of higher-level technical advice relating to effective policy implementation. As Richardson relates, the Treasury’s “advice was more the action stations, not the ideas.” Treasury officials did, however, help Richardson and her faction to persuade some of the less enthusiastic cabinet ministers of the veracity of Richardson’s austerity agenda. Iain Rennie, a Treasury official seconded to the National opposition in 1989, is noted to have been particularly important. According to Richardson he exerted a considerable degree of influence over Jim Bolger, “helping to educate [him], and steadying him at crucial times.”

National’s free-market faction was aided significantly in the advancement of their pre-formulated fiscal austerity agenda by “the specific institutional structure of the state in New Zealand.” As discussed in detail in Chapter Three, due to “the institutional dominance of the executive within New Zealand’s machinery of government” and New Zealand’s unicameral parliament, during the period from 1984 to 1987, just three cabinet ministers – the so-called ‘troika’ of Roger Douglas, David Caygill, and Richard Prebble – were able to rapidly drive through Labour’s radical neoliberal policy agenda. As Kelsey outlines, for much of National’s first term, “Richardson enjoyed considerably more strategic Cabinet support than Douglas initially had. Observers estimate that at least twelve of the 1990 cabinet were free-market ideologues, giving them effective control.” Consequently, like Douglas under

\[253\] Roper 2005, 169.
\[254\] Goldfinch 2000, 115.
\[255\] Russell 1995, 220.
\[256\] Richardson 1995, 56.
\[257\] Roper 2005, xxi.
\[258\] Ibid.
\[259\] Kelsey 1997, 41. Richardson’s position within Cabinet began to go into decline following her introduction of the ‘Mother of all Budgets’.
Labour, Richardson and National’s neoliberals were able to, at least initially, rapidly advance their agenda against little effective opposition.260

The DWSR also played an important supporting role in the further promulgation of neoliberalism in New Zealand during the early 1990s. Indeed, for Richardson, “the financial markets would prove to be” a key “ally.”261 As McKinnon observes, although they were a powerful faction within the National caucus by October 1990, “Richardson[’s neoliberals were] not the National Party.”262 A large number of National MPs, including, most prominently, the new Prime Minister Jim Bolger and his chief supporters Don McKinnon and Bill Birch, remained more traditional National Party members; conservatives “habituated to pragmatic approaches to policy.”263 Consequently, the question of whether the new government would steadfastly pursue a fiscal austerity agenda to the far-reaching extent sought by Richardson and her allies was by no means a fait accompli.264 The financial markets, however, ensured that Richardson was able to garner sufficient support from amongst her colleagues for the immediate implementation of the neoliberal austerity agenda and also that, once successfully initiated, “the momentum of reform continued over into the new year.”265

On arriving in office, the Fourth National Government was immediately faced with an impending fiscal crisis. In its official Briefing to the Incoming Government, Treasury advised that, “with no change from current policy,...the Government [would] confront financial deficits of $3.7 billion, $4.5 billion and $5.2 billion over the next three years.”266 Table 4.3 (below) compares Treasury’s

260 This is not to say there was no internal caucus opposition. As noted in Section One, Muldoon and Peters, in particular, were both outspoken critics of National’s neoliberal policy agenda.
261 Ibid.
262 McKinnon 2003, 346.
263 Ibid; Kelsey 1997, 40. In her autobiography, Richardson also observes that, in many ways, Jim Bolger was the quintessential “rural conservative, skeptical about the merits of Rogernomics.” See Richardson 1995, 39.
264 Kelsey 1997, 40.
265 Richardson 1995, 86. See also McKinnon 2003, 353.
266 Treasury 1990, 2.
post-election fiscal projections with those presented in July as part of *Budget 1990*. As can be seen, Treasury’s new figures represented an extremely sharp deterioration in the New Zealand Government’s apparent financial position within a very short space of time. In *Budget 1990*, the Labour Finance Minister, David Caygill, had announced a small maiden financial surplus for the 1989/90 fiscal year. This was expected to be followed by deficits of 2.8% of GDP in 1990/91 and 1.9% of GDP in 1991/92. Just a few months later, not only had Caygill’s surplus disappeared (replaced by a sizeable deficit), the forecast deficits for the ‘out’ years had also increased dramatically.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>1990 Budget</th>
<th>Treasury Post-Election Briefing</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$billion</td>
<td>% GDP</td>
</tr>
<tr>
<td>1990/91</td>
<td>$0.089</td>
<td>1.9%</td>
</tr>
<tr>
<td>1991/92</td>
<td>-$2.2</td>
<td>2.8%</td>
</tr>
<tr>
<td>1992/93</td>
<td>-$1.6</td>
<td>1.9%</td>
</tr>
<tr>
<td>1993/94</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
</tbody>
</table>


There is some contention over the extent to which a serious fiscal crisis actually existed in the wake of the 1990 election. McKinnon, for example, suggests that it merely served as a pretext for Treasury to advance its own preferred policy agenda. However, as Dalziel delineates (in contrast to a previous position), “the fiscal crisis announced by Treasury was certainly real.” In addition to “uncosted Budget night items” (adding $140 million to the deficit in 1990/91, $334 million in 1991/92, and $747 million in 1992/93) from the previous Labour Government’s last budget, “revised economic assumptions” since budget night meant that in October 1990 the Fourth National Government also found itself facing much higher debt servicing costs.

268 Ibid.
269 McKinnon, 347. See also Roper 2005b, 196.
270 Dalziel 1992, 27.
and social welfare outlays, coupled with declining tax revenues. Combined, these were expected to add $1.2 billion to the deficit for 1991/92 and $1.7 billion for 1992/93. Further, the new National Government “found itself needing to inject $620 million into the Bank of New Zealand, $240 million into Government Property Services and $112 million in the failed Development Finance Corporation.”

New Zealand already had a weak extant public debt position at the time of the 1990 election. As discussed in more detail above, the previous Fourth Labour Government had run persistent large budget deficits throughout its two terms in power. These fiscal shortfalls had been necessarily funded by debt. Figure 4.6 below illustrates the path that New Zealand’s net public debt took under the previous Labour Government. As can be seen, despite some temporary improvement due to Labour’s asset sales between 1987 and 1988, by 1990 the New Zealand government had accrued net liabilities equal to 50.5% of GDP. This level of net public debt was exceptionally high in the contemporary international context.272

---

271 Ibid.
272 Treasury 1990, 69.
The impending fiscal crisis threatened a rapid build-up of additional public debt. Figure 4.6 (above) also shows the projected future path of net government debt contained within Treasury’s Briefing to the Incoming Government. As can be seen, net public debt was expected to fall sharply during the 1990/91 fiscal year, primarily due to the privatisation of Telecom and the subsequent use of the proceeds to pay down public debt. However, thereafter net public debt was forecast to rise substantially. From a level of around 43.1% of GDP in 1991, net public debt was expected to increase by around 5% of GDP annually, to reach some 53.3% of GDP by 1993/1994. In effect, under existing fiscal policy, the benefit of New Zealand’s largest single privatisation would have been nullified within just two years.

---

273 Ibid, 63.
274 Ibid, 4,
275 Ibid, 64, 69.
Richardson states that “Jim Bolger was never more solidly behind me than during the government’s pre-Christmas period.”276 The growing public debt problem was integral to this. Treasury advised Bolger that an increase in debt of the magnitude forecast raised the prospect of significant increases in domestic interest rates and the foreign exchange rate, both of which would have serious negative consequences for the country’s economic performance in the immediate future.277 Furthermore, accruing additional public debt would also generate ongoing “fiscal risk”, thereby increasing “the prospects of adverse reactions in financial markets.”278 As Treasury states:

throughout this period and beyond, there would be an ever increasing risk of a major break in financial market confidence. This could see a very sharp depreciation in the exchange rate take place, further upward pressures on interest rates and the need for urgent corrective action.279

Such threats compelled Bolger’s endorsement of the Richardson agenda; “the Government cannot go on spending money it does not have”, he averred in the 1990 ESI.280

Thus, the second major stage of New Zealand’s historic shift to neoliberalism also constitutes a prime example of what Naomi Klein terms the “Shock Doctrine” in action.281 The 1990 fiscal crisis effectively created a pretext for ostensibly necessary emergency public policy measures and this situation “was...methodically leveraged” by Richardson’s neoliberal cabal in order to rapidly advance the unfinished aspects of their neoliberal policy agenda.282 Indeed, it is particularly noteworthy and interesting that the 1990 fiscal crisis was not only exploited to justify the imposition of draconian fiscal austerity on

276 Richardson 1995, 83.
278 Ibid.
279 Ibid.
280 Bolger 1990 in ESI, 5.
282 Ibid, 156, 164.
the New Zealand electorate, but also extensive labour market deregulation and further privatisations. Richardson, with the help of her allies in Treasury, successfully “obfuscated” the difference between macroeconomic policies actually oriented towards alleviating the immediate threat to New Zealand’s macroeconomic stability and neoliberal microeconomic policies that ultimately “had nothing to do with ending [the] crisis” but, instead, had everything to do with boosting the power and profitability of capital in New Zealand.283

Ultimately, however, the Fourth National Government was, to a significant extent, serving the particular interests of an increasingly financialised and internationally-oriented business elite. Indeed, to borrow from Jesson, “there is not the slightest reason for treating this [((National’s neoliberal policy agenda))] as anything other than the self-serving programme of a self-serving elite.”284 In this regard it is important to recognise that business shifted its support from Labour to National in the two years prior to the 1990 election. After Roger Douglas’s exit from cabinet in December 1988, the Fourth Labour Government’s programme of neoliberal reform was continued by his replacement, David Caygill.285 “Without consulting the Treasury”, recalls Graham Scott, “[Caygill] just announced, “We’re going to have Rogernomics part II”.”286 Labour continued to adhere to the monetarist “anti-inflationary policy that had been pursued fairly consistently since 1984.”287 The privatisation programme announced by Douglas as part of Budget 1988 proceeded as planned, culminating with the sale of Telecom in 1990.288 GST was raised, import protections were reduced further, and the State Sector Act (SSA) was passed.289 Caygill also ensured that both the Public Finance Act 1989 (PFA) and

283 Ibid, 164.
284 Jesson 1999, Only Their Purpose is Mad, 58.
286 McKinnon 2003, 340.
288 Ibid.
289 Richardson 1995, 44, 52. The function of the SSA was effectively to privatise the public sector workforce. See Kelsey 1997, 37.
the Reserve Bank Act 1989 (RBA) were successfully steered through the house and enshrined into legislation.\textsuperscript{290} Thus, in-fact, two of the most important legislative pillars of the overarching neoliberal policy regime (the PFA and RBA) were implemented by Caygill.\textsuperscript{291}

Yet, despite this, the business community was not exceedingly enamoured with the overall policy direction being taken by Labour under the leadership of Palmer. “At present…the government is drifting aimlessly” claimed key NZBR figure Alan Gibbs in 1989.\textsuperscript{292} From the viewpoint of business, the Fourth Labour Government had failed to complete what they considered to be some of the most important aspects of the neoliberal reform agenda that they had been vigorously advocating since 1984.\textsuperscript{293} First, Caygill’s continuation of the neoliberal reform programme had not extended into the realm of social policy. Public health, housing, and education all remained uncommercialised by free-market policies, and existing social welfare and income maintenance programmes had been maintained and, indeed, “enhanced…in some respects.”\textsuperscript{294} Second, the New Zealand labour market remained largely untouched by wholesale deregulation.\textsuperscript{295} Speaking in Hamilton in early 1989, the then vice-chairman of the NZBR and CEO of brewer Lion Nathan, Doug Myers, noted that, for business, “it [was] astounding that so little [had] yet been achieved, or even attempted, by the Government in these areas.”\textsuperscript{296}

Palmer did his utmost to placate business in order to keep them onside. Throughout late 1989 and on into 1990, Palmer actively endeavoured to

\begin{thebibliography}{99}
\bibitem{290} Russell 1995, 211.
\bibitem{291} Scott, quoted in Russell 1995, 201.
\bibitem{293} Roper 2005b, 195.
\bibitem{294} Russell 1995, 213.
\bibitem{295} Roper 2005b, 195; NZBR 1992, Budgetary Stress (Wellington: NZBR), 50.
\end{thebibliography}
reassure the business community that Labour was still fundamentally a “government of momentum and reform.” Despite Palmer’s desperate efforts, however, business shifted its support decisively to National – or, more specifically, to their finance spokesperson Ruth Richardson - in 1988. While her party was distracted with internal conflict between 1984 and 1987, Richardson had been busy “doing the rounds of the major corporates”, largely on her own initiative. As Richardson relates, during this time “I was putting a lot of time into meeting and networking with the business sector. I also met regularly with participants in the financial markets.” Through this activity, by 1987 Richardson had developed for herself personally a very strong and vocal constituency amongst the nation’s business elite.

Through this support, business exerted a considerable degree of influence over the subsequent direction of National Party policy. Most notably, business ensured that Richardson was appointed Minister of Finance. As Richardson recalls, while “I had been fairly confident of securing the job [of Finance Minister] ever since the publication of the vision document,…I had never been 100 per cent confident.” “Despite the success of the Vision document”, for some time afterward, there was continued “speculation over whether Jim would appoint me.” Business quickly put any doubts about the matter to rest. As Kelsey observes, “business interests made it clear [to Bolger]

297 Richardson 1995, 38.
299 Kelsey 1997, 40.
300 Richardson 1995, 51.
301 Ibid, 42, 46.
303 Richardson 1995, 75.
304 Ibid, 68.
that they expected her to be appointed Minister of Finance in return for supporting National, both financially and electorally; and she was.”305

Sustaining the Changes

Although subsequent to the successful implementation of labour market reform and fiscal austerity there was a general consensus within the business community that the Fourth National Government’s “policy framework [was now] fundamentally sound”, following the 1993 election, business nevertheless continued to press for the further extension of the neoliberal policy agenda.306 As Roper has comprehensively documented, throughout the period from 1994 to 1999, “business...vigorously promoted further [neoliberal] reforms that it considered to be in its interests, which it equated with those of the nation as a whole.”307 Most prominently, business advocated:

Further reduction of import protection through the lowering of tariffs; further tax cuts for companies and high income earners, to be funded by a general reduction in social spending; elimination of the Employment Court, with labour disputes to be dealt with in the civil courts; further privatisation of state- and local body-owned enterprises; increasing fees for tertiary students; the introduction of market rents for tenants in state houses, and the privatisation of state housing.308

For the Fourth National Government, however, further substantive neoliberal reform had “become politically untenable” after the 1993 general

---

305 Kelsey 1997, 40. It should also be noted that it was partly due to her extensive support within the corporate world that Richardson was initially offered the position of Finance Spokesperson in 1987. See Richardson 1995, 42.
308 Ibid 2005b, 108. For a more detailed discussion see ibid 2006, 171-74. NZBR 1992, Budgetary Stress (Wellington: NZBR) also provides a good overview of the key features of the business political agenda following their successful advocacy of radical industrial relations reform and the redesign and downsizing of the welfare state.
As discussed in more detail in Section One, National’s poorly signaled continuation of Labour’s radical neoliberal reform agenda had been extremely unpopular. At the 1993 election voters had expressed their dissent; National’s vote share fell precipitously and National only retained power with a bare majority. As Easton observes, having only just scraped back into office, “Bolger had neither the mandate in the House nor the personal inclination to continue” the neoliberal revolution.

Consequently, the second phase of New Zealand’s historic shift to neoliberalism effectively came to an end. Richardson, chief architect of the reforms and also the focal point of business political influence from 1990 to 1993, was not re-appointed to the finance portfolio. Bolger replaced her with close ally Bill Birch, whilst simultaneously shuffling Cabinet in order to promote MPs “of a more pragmatic or moderate stance.” When explaining the changes, Bolger stated “we believe the time has come to recognise the big moves are behind us and a different form of management is needed.”

Yet, although the political climate was no longer conducive to substantive neoliberal reform, the Fourth National Government nevertheless persevered with a distinctively neoliberal approach to macroeconomic management. As outlined in detail in the previous section, throughout the period from 1994 to 1999, the Fourth National Government – in each of its various guises - adhered to a surplus-driven, low-debt fiscal strategy coupled with a monetarist low-inflation monetary strategy. A number of factors contributed to the Fourth National Government not “deviating from the free
market path” in the realm of macroeconomic policy. 314 As Roper has documented, for example, throughout the period from 1994 to 1999, major business interests “vigorously opposed any perceived “rolling back” of the neoliberal policy reforms of 1984-93.” 315 Treasury also directed much of its policy advice from 1994 onwards towards persuading the Fourth National Government to maintain the recently established neoliberal policy framework. 316 A particularly important factor contributing to the Fourth National Government’s steadfast adherence to a neoliberal fiscal strategy, however, was New Zealand’s integration into the DWSR. In a context of open capital controls, a flexible exchange rate, an extensively deregulated domestic financial system, and a highly liberalised foreign investment regime, New Zealand’s extremely high level of offshore debt meant that IPFMs and international credit rating agencies exerted a significant degree of influence over government fiscal policy formulation during the period from 1994 to 1999.

Figure 4.7 (below) illustrates New Zealand’s current account deficits during the decade leading up to 1994. As can be seen, New Zealand recorded large current account deficits throughout the period. 317 From an already weak level of -5.5% of GDP in 1984, the country’s balance of payments position initially deteriorated significantly, with an average deficit of -8.7% of GDP in each of the following two years. The current account deficit subsequently improved (although still remained sizeable) in the following three years, reaching a nadir of 0.8% of GDP during the depths of the severe recession in 1989. 318 Following this, the overall balance of payments position worsened once

314 Kelsey 1999, 77.
315 Roper 2006.
317 Perhaps with the exception of 1989.
318 Since at least the 1980s, there appears to be a strong correlation between economic growth and current account deficits in New Zealand. During periods of relatively strong economic growth, current account deficits tend to widen due to import expansion, while the opposite tends to occur during economic downturns. It is thus unsurprising that New Zealand’s current account deficit narrowed
more; the country recorded average annual current account deficits of -3.14% of GDP during the period from 1990 to 1994. Thus, despite an apparent turnaround in a number of other important measures of economic performance (noted above), the previous decade of radical neoliberal reform had failed to alter the underlying nature of New Zealand’s balance of payments position. Fundamentally, as Kelsey observes, the country continued to regularly earn significantly “less from exports and income from its investments overseas than it paid for imports and income from foreign investment in New Zealand (including interest and profits remittable on loans and investments).”

![Figure 4.7] New Zealand’s Current Account Deficits, 1984 to 1994

Source: Dalziel and Lattimore 2001, 135.

considerably during the late 1980s and early 1990s as the country endured its worst economic downturn since the Great Depression.

Kelsey 1999, 141.
Table 4.4) New Zealand’s Net International Investment Position, March 1994

<table>
<thead>
<tr>
<th>New Zealand’s IIP</th>
<th>$million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total International Assets</td>
<td>32,417</td>
</tr>
<tr>
<td>Total International Liabilities</td>
<td>99,789</td>
</tr>
<tr>
<td>New Zealand’s Net International Asset Position</td>
<td>-67,371</td>
</tr>
<tr>
<td>Nominal GDP</td>
<td>80,824</td>
</tr>
<tr>
<td>Net IIP as % of Nominal GDP</td>
<td>83%</td>
</tr>
<tr>
<td>Total International Liabilities as a % of Nominal GDP</td>
<td>123%</td>
</tr>
</tbody>
</table>


Persistent current account deficits of the magnitude indicated above necessarily entailed a concurrent accumulation of an increasingly large body of offshore debt. The best official measure of the overall significance of New Zealand’s external indebtedness is contained within Statistics New Zealand’s regularly updated *International Investment Position* (IIP) data series. The pertinent aspects of this data series are presented in Table 4.4 (above). As can be seen, by the end of March 1994, the New Zealand economy as a whole had amassed a net external liability of $67.4 billion, equivalent to just over 83% of GDP. This “level of (net) dependence on foreign capital” was particularly high compared to other small developed economies at this time.

New Zealand was “not facing an incipient crisis” at the beginning of the Fourth National Government’s second term. Unlike the situation when National first took office in late 1990, there appeared to be no immediate danger of a major national financial crisis developing. However, New Zealand’s large ongoing current account deficits and corresponding heavy reliance on foreign capital necessarily entailed a concurrent accumulation of an increasingly large body of offshore debt. The best official measure of the overall significance of New Zealand’s external indebtedness is contained within Statistics New Zealand’s regularly updated *International Investment Position* (IIP) data series. The pertinent aspects of this data series are presented in Table 4.4 (above). As can be seen, by the end of March 1994, the New Zealand economy as a whole had amassed a net external liability of $67.4 billion, equivalent to just over 83% of GDP. This “level of (net) dependence on foreign capital” was particularly high compared to other small developed economies at this time.

New Zealand was “not facing an incipient crisis” at the beginning of the Fourth National Government’s second term. Unlike the situation when National first took office in late 1990, there appeared to be no immediate danger of a major national financial crisis developing. However, New Zealand’s large ongoing current account deficits and corresponding heavy reliance on foreign capital necessarily entailed a concurrent accumulation of an increasingly large body of offshore debt. The best official measure of the overall significance of New Zealand’s external indebtedness is contained within Statistics New Zealand’s regularly updated *International Investment Position* (IIP) data series. The pertinent aspects of this data series are presented in Table 4.4 (above). As can be seen, by the end of March 1994, the New Zealand economy as a whole had amassed a net external liability of $67.4 billion, equivalent to just over 83% of GDP. This “level of (net) dependence on foreign capital” was particularly high compared to other small developed economies at this time.

New Zealand was “not facing an incipient crisis” at the beginning of the Fourth National Government’s second term. Unlike the situation when National first took office in late 1990, there appeared to be no immediate danger of a major national financial crisis developing. However, New Zealand’s large ongoing current account deficits and corresponding heavy reliance on foreign capital necessarily entailed a concurrent accumulation of an increasingly large body of offshore debt. The best official measure of the overall significance of New Zealand’s external indebtedness is contained within Statistics New Zealand’s regularly updated *International Investment Position* (IIP) data series. The pertinent aspects of this data series are presented in Table 4.4 (above). As can be seen, by the end of March 1994, the New Zealand economy as a whole had amassed a net external liability of $67.4 billion, equivalent to just over 83% of GDP. This “level of (net) dependence on foreign capital” was particularly high compared to other small developed economies at this time.

New Zealand was “not facing an incipient crisis” at the beginning of the Fourth National Government’s second term. Unlike the situation when National first took office in late 1990, there appeared to be no immediate danger of a major national financial crisis developing. However, New Zealand’s large ongoing current account deficits and corresponding heavy reliance on foreign capital necessarily entailed a concurrent accumulation of an increasingly large body of offshore debt. The best official measure of the overall significance of New Zealand’s external indebtedness is contained within Statistics New Zealand’s regularly updated *International Investment Position* (IIP) data series. The pertinent aspects of this data series are presented in Table 4.4 (above). As can be seen, by the end of March 1994, the New Zealand economy as a whole had amassed a net external liability of $67.4 billion, equivalent to just over 83% of GDP. This “level of (net) dependence on foreign capital” was particularly high compared to other small developed economies at this time.

New Zealand was “not facing an incipient crisis” at the beginning of the Fourth National Government’s second term. Unlike the situation when National first took office in late 1990, there appeared to be no immediate danger of a major national financial crisis developing. However, New Zealand’s large ongoing current account deficits and corresponding heavy reliance on foreign capital necessarily entailed a concurrent accumulation of an increasingly large body of offshore debt. The best official measure of the overall significance of New Zealand’s external indebtedness is contained within Statistics New Zealand’s regularly updated *International Investment Position* (IIP) data series. The pertinent aspects of this data series are presented in Table 4.4 (above). As can be seen, by the end of March 1994, the New Zealand economy as a whole had amassed a net external liability of $67.4 billion, equivalent to just over 83% of GDP. This “level of (net) dependence on foreign capital” was particularly high compared to other small developed economies at this time.
capital nevertheless rendered New Zealand particularly vulnerable to one. As Woolford, Reddell, and Comber observe, while “all countries that borrow internationally face the same potential risks”, an exceptionally high level of net external indebtedness exposed New Zealand to the distinct possibility of a sudden reversal in capital flows. A material deterioration in the nation’s underlying economic fundamentals, a marked increase in risk aversion within IPFMs, or a major disruption in IPFMs resulting in “a widespread retreat from the ready international cross-border flow of capital” (such as what occurred in 2008 during the GFC) could all have resulted in a major outflow of private foreign capital (or, alternatively, a so-called “sudden stop” involving an inability to attract new offshore capital inflows). The likely outcome of such an episode would have been significant downward pressure on the currency, rapidly rising domestic interest rates, and, ultimately, a period of severe macroeconomic instability.

New Zealand’s elevated vulnerability to “future financial shocks” emanating from IPFMs placed significant pressure on the Fourth National Government to implement macroeconomic policies that would help to preserve the country’s ongoing financial stability. Centrally, the Fourth National Government was responding to this latent IPFM-derived pressure when it moved to make rapid reduction of public debt “the major objective of its fiscal strategy” in 1994. As Bill Birch explained in Budget 1994, “Lower debt is a means to an end, not an end in itself.” “Lower debt makes the country less vulnerable to adverse international events like trade shocks, interest or

---

327 Ibid. See also Lane 2011, 6-7.
328 A more detailed account of how a potential domestic financial crisis might develop in New Zealand is provided later in Section 8.3.
329 Lane 2011, 1.
exchange rate movements.” Figure 4.8 shows the overall structure of New Zealand’s total overseas debt at the end of March, 1994. As can be seen, central government borrowing made up a sizeable component of the nation’s substantial external liabilities at the beginning of the Fourth National Government’s second term. Official government overseas debt totalled some $26.3 billion. This constituted 36.2% of New Zealand’s substantial external liabilities, and was the equivalent of around 32.5% of nominal GDP. Therefore, the prioritisation of large operating surpluses for the specific purpose of “dealing to debt” (as Birch termed it) would make a significant contribution towards alleviating New Zealand’s overall external indebtedness, the primary cause of the country’s elevated level of macroeconomic vulnerability.

![Figure 4.8) Total New Zealand Overseas Debt, March 1994 ($billion)](image)


---

The specific targeting of foreign currency denominated debt within the broader drive to reduce debt, meanwhile, was primarily designed to mitigate the risk of adverse movements in exchange rates sparking a financial crisis.\textsuperscript{334} Previously, when tapping international debt markets in order to finance successive budget deficits, New Zealand governments had effectively been obliged to borrow offshore funds denominated solely in foreign currency. Due to the country’s relatively high level of indebtedness, IPFMs would simply not accept the risk of providing funding denominated in the local currency (the New Zealand dollar).\textsuperscript{335} Consequently, at the start of its second term, the Fourth National Government found itself in possession of a considerable body of foreign currency debt. This foreign currency denominated debt exposed the Fourth National Government to considerable exchange rate risk. In the event of a sudden major depreciation in the value of the New Zealand dollar, the local currency value of the Government’s debt would have simultaneously increased, as would the cost of servicing that debt. Due to the Government’s relatively high levels of foreign currency debt, the compounding effects on the overall public debt burden would have been significant. This is highlighted by the fact that a relatively minor 10\% currency depreciation in 1991 (linked to the fiscal crisis discussed earlier) resulted in a $2.4 billion appreciation in “the New Zealand-dollar value of gross public debt.”\textsuperscript{336} Thus, a serious exchange rate shock could have potentially fomented the development of a broader financial crisis. Rapidly mounting government debt levels on a sufficient scale would have undermined investor confidence, resulting in major capital outflows and a severe macroeconomic disruption. Moving the Government to a “zero net foreign currency debt” position over the following three years would effectively

\textsuperscript{335} Woolford et al, 6.
\textsuperscript{336} Treasury 1994, FSR, 51.
eliminate the Crown’s direct exposure to such risks. Exchange rate fluctuations would simply no longer have any bearing on “the burden of [public] debt in domestic currency terms”, and thereby also the Government’s perceived creditworthiness in IPFMs.

Moving decisively to reduce the government’s share of the nation’s accumulated overseas debt and to eliminate official foreign currency debt in particular, quickly served to boost the nation’s underlying creditworthiness in IPFMs. This was confirmed when international credit rating agency Standard and Poor’s upgraded New Zealand’s sovereign credit rating from AA- to AA in December, 1994. Fundamentally, the immediate improvement in the Fourth National Government’s own financial position, combined with being seen to be clearly prioritising the generation of large operating surpluses for the specific purpose of paying off additional public debt, significantly increased “investor confidence in the New Zealand economy.” New Zealand was essentially now a more attractive destination for increasingly mobile international financial flows.

New Zealand’s enhanced creditworthiness in IPFMs undoubtedly lent the Fourth National Government an increased degree of flexibility in relation to the formulation of fiscal policy. For example, the Fourth National Government was able to moderate its overarching fiscal strategy (by accepting “a lower surplus and a slower reduction in debt”) in order to accommodate a brief period of so-called ‘fiscal easing’ between mid-1996 and mid-1998. However, New Zealand’s large ongoing current account deficits did not simply come to an end in 1994. Figure 4.9 (below) illustrates New Zealand’s current account balances during the period from 1991 to 2000. As can be seen, despite the

338 Hargreaves and Watson, 19.
340 Ibid.
341 Despite protestations that the 4NG’s moderation was not politically motivated, it was almost undoubtedly undertaken in order to address mounting counter-veiling electoral pressures to increase social spending.
apparent turnaround in a number of other important measures of economic performance (noted above), New Zealand continued to experience sizeable current account deficits throughout the period from 1994 to 1999. Indeed, the country’s average annual balance of payments positions actually worsened significantly. From 1991 to 1994, New Zealand’s annual current account deficit had remained broadly steady. The annual average current account deficit for the period was just over $2.13 billion. In 1995, however, the current account deficit increased markedly. From a level of around -$1.86 billion in 1994, the annual current account balance deteriorated to reach -$4.11 billion. It subsequently remained at an elevated level throughout the remainder of the Fourth National Government’s time in office. During the period from 1996 to 1999, the average annual current account deficit totaled almost $5.2 billion.

Due to these ongoing large current account deficits, New Zealand’s total overseas debt continued to grow unabated throughout the period from 1994 to 1999. Figure 4.10 shows New Zealand’s net stock of external liabilities during the period from 1991 to 2000. As can be seen, despite the Fourth National Government dramatically reducing its own external indebtedness, “over the decade as a whole…New Zealand’s [overall] dependence on international capital (both debt and equity)...increased substantially.” From the (previously noted) level of -$67,371 in 1994, New Zealand’s net external debt position deteriorated by some $20 billion (in nominal terms) to reach -$87.084 billion in March, 2000.

---

343 Ibid.
344 This is despite the current account deficit trailing off somewhat in the immediate aftermath of the 1997-98 East Asian financial crisis.
345 Ibid.
346 Kelsey 1999, 140.
347 Woolford et al, 6.
Figure 4.9) New Zealand’s Current Account Deficits, 1991 to 2000 ($billion)


Figure 4.10) New Zealand’s Net External Liabilities, 1991 to 2000 ($billion)

Source: Statistics New Zealand.
New Zealand’s “increased external indebtedness” during the 1990s was wholly driven by the private sector. As Woolford, Reddell, and Comber observe, “over the decade as a whole”, the saving and investment decisions of private “households’ [and firms’ were] the largest single factor in [the country’s] increased need for foreign capital.” Government offshore borrowing had previously dominated New Zealand’s external debt. As documented by Bertram, by the late 1980s, the country had accumulated a total foreign debt equivalent to 70% of GDP, “of which the government accounted for half.” “During the 1990s”, however, New Zealand’s “overseas debt [was] privatised.” Initially, increasing private external liabilities took the form of a “surge of inward equity investment.” Foreign multi-national corporations (MNCs) effectively took control of an increasing share of New Zealand-domiciled companies. Subsequently, following the onset of the 1997-1998 East Asian financial crisis, foreign private direct investment inflows were replaced as the main driver of New Zealand’s increasing external indebtedness by greatly expanded offshore borrowing by the nation’s largely foreign-owned banking system. As Bertram delineates, from around 1997 onwards, “the banks…moved to offshore funding on a grand scale.” This was primarily in order “to finance domestic credit expansion within New Zealand, much of which went to fund speculative activity in the housing and property markets.” As will be discussed in more detailed in Chapter Seven, heavy offshore borrowing by the banks continued through until the onset of the

---

348 Woolford et al, 6. See also The Economist 1998.
349 ibid.
351 ibid, 13, 15.
352 ibid, 13.
354 Bertram 2009, 9, 13. See also The Economist 1998; Woolford et al, 6.
355 Bertram 2009, 11.
356 ibid.
Global Financial Crisis (GFC) in 2008, and also for a number of years thereafter.\textsuperscript{357}

As a result, despite a marked improvement in the Crown’s own financial position between 1994 and 1999, New Zealand nevertheless remained “vulnerable to any downturn in [international] investor confidence.”\textsuperscript{358} Adverse developments in IPFMs – such as what occurred during the 1997-98 East Asian financial crisis – continued to pose a very real threat to the country’s ongoing macroeconomic stability. This now seemingly perpetual vulnerability to externally induced financial crises ensured that significant IPFM-derived “nonconstitutional constraints” remained firmly in place.\textsuperscript{359} Throughout the period from 1994 to 1999, the Fourth National Government faced considerable pressure to commit “to running fiscal surpluses and repaying government debt.”\textsuperscript{360} As outlined above, the major driver of New Zealand’s current account deficit during the 1990s was, in-effect, significant private sector dis-saving. As then RBNZ Governor Don Brash described the situation at the time (in typical neoliberal obfuscating fashion), private individuals, households, and corporates were simply exercising “a strong demand for additional funds within New Zealand.”\textsuperscript{361} By running sizeable fiscal surpluses, the Fourth National Government would effectively lean against the private sector’s extensive offshore borrowing activity. Strong government savings would bolster otherwise weak national savings, thereby improving the overall balance on the current account.\textsuperscript{362} Using these same fiscal surpluses to secure further public debt reduction, meanwhile, would help maintain New Zealand’s creditworthiness in IPFMs. It would do this by ensuring that New Zealand was

\textsuperscript{357} At the time of writing the situation remains largely unchanged, although the overall maturity profile of offshore bank funding has lengthened.
well situated to weather any significant future financial shocks which might eventuate. Principally, lower public debt levels would endow the state with a balance sheet “sufficiently robust” to be able to intervene as an emergency source of working capital to banks and major corporates otherwise facing acute funding issues in the event of a ‘sudden stop’. The government would effectively be capable of providing a fiscal “cushion”, absorbing much of the impact of a major external financial shock on its own balance sheet.

364 Ibid.
Conclusion

During the period from 1990 to 1994, the Fourth National Government rapidly moved to complete the previous Labour Government’s programme of neoliberal structural adjustment.365 In the realm of fiscal policy this entailed a fundamental redesign of the welfare state. During its first term in power, in two main stages – the ESI announced in December 1990 and the 1991 ‘Mother of all Budgets’ – the Fourth National Government initiated sweeping changes affecting all of the major facets of the New Zealand welfare state including health, education, superannuation, housing, and social welfare (see Table 4.1). These efforts significantly curtailed overall public expenditure and served to eliminate the fiscal deficit by the end of its first term. In order to help lock in this neoliberal fiscal austerity strategy, in July 1994 the FRA was passed into legislation. The Fourth National Government initially persevered with a relatively austere approach to fiscal policy during its second term in office. Adopting what Kelsey refers to as a ‘surplus-driven, low debt’ fiscal strategy, the National Government consolidated its underlying fiscal position by reducing public debt. The level of progress made in ‘dealing to debt’ in the 1994 and 1995 fiscal years meant that during the period from mid-1996 to mid-1998, the Fourth National Government was able to significantly loosen its fiscal stance. A major programme of tax cuts was implemented and several large new social spending packages were introduced. However, this period of what Fowlie terms ‘fiscal easing’ constituted only a temporary moderation of the Fourth National Government’s overarching fiscal strategy. As the 1997-98 East Asian financial crisis began to have an impact on the economy, the Coalition Government quickly moved to tighten up its fiscal stance once again. Under the leadership of Shipley, this tight fiscal stance was maintained by the minority National Government in 1998/99.

365 Roper 2005b, 195, 196.
In the first instance, the primary driver of the second major phase of neoliberalisation that was implemented in New Zealand from 1990 to 1994 was the Fourth National Government Finance Minister Ruth Richardson and her allies in cabinet. Richardson was an ardent free-market fundamentalist and had successfully maneuvered to ensure that the Fourth National Government would pursue (amongst other things) a radical neoliberal fiscal austerity strategy on coming into office. Richardson and her pro-market cabinet faction were aided significantly in the advancement of their neoliberal fiscal policy agenda in New Zealand by the specific institutional structure of the state, the country’s recent integration into the DWSR, and also a largely compliant and ideologically aligned Treasury. However, the Fourth National Government’s pursuit of fiscal austerity from 1990 to 1994, to a significant extent, also reflected the preferences of big business. Having previously supported the Fourth Labour Government, the nation’s business elite shifted its support to the National Party prior to the 1990 general election, and subsequently exerted a considerable degree of influence over the public policy programme pursued by the Fourth National Government during its first term in office.

Ongoing business political activism and pro-market policy advice from Treasury undoubtedly played important roles in the Fourth National Government’s subsequent close adherence to a neoliberal fiscal strategy during the period from 1994 to 1999. However, another key factor was New Zealand’s integration into the DWSR. Ongoing large current account deficits meant that throughout the period New Zealand was one of the most heavily indebted nations in the developed world. This exceptionally high level of reliance on foreign capital posed a persistent threat to the country’s macroeconomic stability, which effectively served to constrain the Fourth National Government in the realm of fiscal policy formulation. The Fourth National Government faced significant implied pressure from IPFMs to closely adhere to a neoliberal fiscal strategy focused on running budget surpluses and reducing public debt
so as to mitigate the potential threat posed by destabilising external capital flows.

As will be shown throughout the remainder of this thesis, integration into the DWSR continued to place significant constraints on the formulation of fiscal policy in New Zealand subsequent to the defeat of the Fourth National Government at the 1999 election. During the period from 1999 to 2008, the Fifth Labour Government (FLG) faced considerable pressure to closely adhere to a neoliberal fiscal strategy oriented around public debt reduction funded by large operating surpluses. But the DWSR-derived constraints were not just restricted to fiscal policy. Fundamentally, New Zealand’s integration into the DWSR placed pressure on the FLG to retain all of the key features of the neoliberal macroeconomic policy agenda that it had inherited.
The Fifth Labour Government and Macroeconomic Policy: 1999 to 2008

Introduction

As the previous two chapters have shown, New Zealand underwent a process of radical neoliberalisation during the period from 1984 to 1999. Indeed, the speed and scope of the ‘New Zealand experiment’ was such that it has been lauded in some circles as a model of voluntary neoliberal structural adjustment worthy of international emulation.¹ This political project was initially advanced by the Fourth Labour Government. Extensive neoliberal restructuring of the economy was implemented throughout their two terms in power from 1984 to 1990. The succeeding Fourth National Government subsequently continued the rollout of the neoliberal policy agenda. Most notably, National completed Labour’s ‘unfinished business’ in the key areas of industrial relations, social welfare, and fiscal policy.

New Zealand’s historic shift to neoliberalism was impelled, in the first instance, by a relatively small, yet highly influential group of MPs, Treasury and Reserve Bank (RBNZ) officials, and business leaders. Prominent figures within this group included: Labour Government ministers Roger Douglas, David Caygill, and Richard Prebble; National’s first-term Finance Minister Ruth Richardson; Treasury Secretary Graham Scott; RBNZ deputy governor Roderick Deane; and former Treasury official and New Zealand Business Roundtable

¹ Kelsey 1997, 1.
head Roger Kerr. However, the highly important political activities of this key group of actors were heavily influenced by a number of broader international developments. These included, most prominently: the worldwide onset of ‘stagflation’ in the mid-1970s; a sharp upswing in employer militancy and business political activism; the shift in the prevailing international economic orthodoxy from Keynesianism to neoliberalism; and the political ascendancy of the ‘New Right’ internationally (including, most prominently, Thatcher and Reagan).

This chapter shifts our attention to the Fifth Labour Government (FLG), in power in New Zealand from 1999 to 2008. It begins by providing a broad descriptive overview of the prevailing political and economic conditions during this period. The FLG’s so-called ‘Third Way’ approach to public policy making is then briefly outlined. Following this, a detailed examination of the core features of the FLG’s macroeconomic policy nexus – monetary policy, fiscal policy, and foreign exchange (FX) policy – is undertaken. The core findings are summarised by way of conclusion.

The principal argument asserts that while the FLG’s ‘Third Way’ approach to public policy formulation included an undeniable softening of the prevailing policy regime, it nevertheless only constituted a mild social democratic moderation of neoliberalism in New Zealand. An overarching ‘monetarist’ approach to macroeconomic management primarily (if not solely) focused on maintaining low, stable levels of inflation was adopted, and day-to-day power of policy implementation was ceded to an operationally independent RBNZ. The FLG also continued to closely abide by a largely unchanged Fiscal Responsibility Act (FRA), pursuing a mutually reinforcing conservative fiscal strategy focused on generating operating surpluses and the reduction of public debt. The currency, meanwhile, was essentially allowed to float freely according to the vagaries of IPFMs. Fundamentally, the FLG retained and entrenched all of the key features of the neoliberal macroeconomic
policy nexus constructed by the previous Labour and National governments during the period from 1984 to 1999.
5.1) The Fifth Labour Government: A Political Overview

On 27 November, 1999, the centre-left FLG was elected to power in New Zealand. Having received just 30.5% of the party vote, the incumbent Shipley-led minority National Government was soundly defeated by a coalition formed by Labour and the Alliance, with additional support from the Greens on issues of confidence and supply. Labour, under the leadership of Helen Clark, secured 38.7% of the party vote and 49 parliamentary seats, while the social democratic Alliance secured 7.7% of the party vote and 10 seats. Combined with the seven seats secured by the Greens, this easily gave the Labour-led coalition control over the house, with 66 out of the 120 total seats in parliament.

As Roper observes, “widespread popular disillusionment with neoliberalism played a key role in the election of the Labour-Alliance coalition government.” 15 years of radical neoliberal reform had served to progressively alienate a significant portion of the population from the neoliberal policy agenda being propagated in Wellington. Labour and the Alliance successfully exploited this during the election campaign. Both parties vigorously attacked the National Government’s policy record. Particular attention was drawn to issues related to chronic underfunding in the public health system, the increasingly prohibitive cost of tertiary education, cuts to national superannuation, and increased economic hardship and inequality.

The election of an ostensibly left-wing government elicited a profoundly negative response from business. This culminated in a “crisis of business confidence” in mid-2000, latterly dubbed the ‘winter of discontent’. Business

---

5 James 2000, 73; Roper 2005b, 222.
6 Ibid, 224.
political opposition largely derived from deep-seated fears over the extent to which the new Coalition Government intended to substantively roll back the neoliberal policy agenda. As Roper outlines, in specific terms,

business opposition to the incoming Government [was] focused on the increase in the marginal rate of income tax for those earning over $60,000 from 33 per cent to 39 per cent, the repeal of the ECA and introduction of the Employment Relations Act, the renationalisation of the ACC scheme, and the introduction of paid parental leave.\footnote{Ibid, 114.}

Ultimately, business opposition was largely ameliorated once it was made clear that, while the FLG would seek to address some of its harshest aspects, all of the key features of the neoliberal policy regime would nevertheless be retained.\footnote{Ibid. For a prime example of this message see H. Clark 2000, “Speech to the Auckland Chamber of Commerce”, 16 June. Available at \url{http://www.beehive.govt.nz/speech/auckland-chamber-commerce}. Accessed 11 December, 2014.} As Prime Minister Helen Clark quite succinctly explained the situation to one meeting of prominent business people held in late 2000, “the government [did not] intend to throw the baby out with the bathwater.”\footnote{H. Clark 2000, “Speech to the Government-to-Business Forum”, 24 October. Quoted in Kelsey 2002, 51.}
Despite initially facing significant public opposition from the business community, the FLG nevertheless enjoyed a prolonged period of popularity throughout its first term in power. As Church observes, “after building steadily throughout 2001, Labour was consistently scoring 50 per cent in polls” published during April, 2002.\textsuperscript{11} A key factor contributing to this surge in popularity was the onset of a sustained period of strong economic growth in 1999. As can be seen from Figure 5.1 (above), from a level of just 0.6% immediately following the East Asian Financial Crisis in 1998 (see the previous chapter), real economic growth measured as a percent of GDP rose to 2.7% in 1999 and then 6.4% in 2000. After falling dramatically again in 2001 due to the bursting of the so-called ‘Dotcom bubble’, the rate of real economic growth subsequently rebounded strongly. Real economic growth averaged almost 4% of GDP between 2002 and 2007, peaking at 5.4% of GDP in 2004. Overall, the years spanning 1999 to 2007 constituted the strongest period of prolonged

\textsuperscript{10} GDP data based on years ending in March.

economic expansion experienced in New Zealand since the onset of ‘stagflation’ in the mid-1970s (see Chapter Three). This relatively high level of economic growth served to significantly reduce the rate of unemployment in New Zealand. The official rate of unemployment during the tenure of the FLG is set out in Figure 5.2 below. As can be seen, from a level of 7.4% in 1998, the official rate of unemployment declined significantly during the following decade to reach a nadir of 3.8% in 2008.\textsuperscript{12} Fundamentally, strong economic performance, in concert with these historically low levels of unemployment, acted to create a widespread sense of relative economic security, thereby greatly enhancing the standing of the Government amongst the voting public.\textsuperscript{13}

\textbf{Figure 5.2) Official Rate of Unemployment in New Zealand, 1998 to 2008}\textsuperscript{14}

As the parliamentary term progressed, the Alliance found itself becoming increasingly dominated by the resurgent Labour Party.\textsuperscript{15} Comprising

\textsuperscript{12} That is, immediately prior the onset of the Global Financial Crisis (GFC), see Chapter Seven.


\textsuperscript{14} GDP data based on years ending in March.
the junior coalition partner, it found itself largely unable to advance any of its major policies.\textsuperscript{16} As Miller outlines, Prime Minister Helen Clark either postponed or rejected a range of policy proposals, including several by senior Alliance ministers. Among those she vetoed were proposals for an extra week’s annual leave, employer-funded parental leave, and an increase in the minimum youth wage rate.\textsuperscript{17}

Subsequently, significant internal conflict developed within the Alliance. Undoubtedly, a number of factors fed the incipient factional infighting within the party.\textsuperscript{18} However, a particularly salient factor was disagreement over the Government’s support of the US ‘war on terrorism’ following the terrorist attacks of 11 September, 2001.\textsuperscript{19} As Levine and Roberts delineate, ultimately, “the problems within the Alliance [became] so acute” that they induced a fundamental split within the party.\textsuperscript{20} “An ‘official’ Alliance party led by a cabinet minister, Laila Harre (and supported by the extra-parliamentary party)” remained in existence, while a minority faction led by Anderton splintered off to form what would later become the Progressives.\textsuperscript{21}

The FLG was re-elected to office at an early election held on 27 July, 2002.\textsuperscript{22} Although pre-election polling had hinted at the possibility of an outright majority, Labour received only 41.3% of the party vote and gained control over

\begin{footnotes}
\footnote{18} Levine and Roberts 2003, 221. See also Miller 2002, 115.  
\footnote{19} Ibid; Roper 2005b, 225.  
\footnote{20} Levine and Roberts 2003, 222.  
\footnote{21} Ibid.  
\footnote{22} Roper 2005b, 225.}

a total of 52 seats in parliament.\textsuperscript{23} Labour was joined in a formal coalition by the Progressives who, while only attracting 1.7% of the vote, gained two seats thanks to Jim Anderton’s continued domination of the Christchurch electorate of Wigram.\textsuperscript{24} Not unsurprisingly, the now divided Alliance did not return to parliament. Their respective share of the vote collapsed to just 1.3%.\textsuperscript{25} The new minority coalition government formed by Labour and the Progressives were supported on the right via a formal agreement with the “broadly centrist United Future Party.”\textsuperscript{26} Largely on the back of one strong performance by its leader Peter Dunne at a televised campaign debate (and the associated effect of the so-called ‘worm’), United Future had secured 6.7% of the vote and eight parliamentary seats.\textsuperscript{27} The Greens, meanwhile, aligned themselves on the left of the new government.\textsuperscript{28} They had increased their share of the party vote to 7% and thus increased their parliamentary presence to nine seats.\textsuperscript{29} Amongst the opposition parties, the neoliberal ACT party attracted 7.1% of the vote and thereby secured nine seats. New Zealand First, respectively, received 10.4% of the vote and 13 seats. Perhaps most significantly, however, the main opposition party, National, won just 20.9% of the party vote and 27 seats.\textsuperscript{30} As Roper observes, this constituted “the worst performance in the history of the party.”\textsuperscript{31}

National’s dismal result at the 2002 election played a key role in precipitating a change in the party’s leadership soon thereafter. On Tuesday, 28 October 2003, former RBNZ governor and erstwhile finance spokesperson Don

\begin{thebibliography}{99}
\item Ibid.
\item Levine and Roberts 2003, 23, 26.
\item Boston and Church 2003, 333.
\item Levine and Roberts 2003, 26.
\item Ibid.
\item Roper 2005b, 225.
\end{thebibliography}
Brash took over control of the parliamentary caucus from Bill English. In his illuminating work *The Hollow Men*, investigative journalist Nicky Hager reveals that Brash’s leadership campaign was not actually widely supported within the National Party. Instead, “most assistance came from people with no connection to the party.” Those backing Brash primarily constituted a loose grouping of individuals closely linked to the neoliberal ACT Party, including a number of prominent business leaders. Familiar figures such as Roger Douglas, Ruth Richardson, and Roger Kerr are amongst those identified as being centrally involved. As Hager delineates,

> attempts [by this group] to move Don Brash into the leadership had begun only eight months after he became an MP [in April 2003]. Despite denials, it is likely that this had [in fact] been the plan of at least some people since the party president Michelle Boag first approached Brash to be a candidate in April 2002.

It is now apparent that the overarching goal was to re-establish the National Party as a politically viable “vehicle to introduce [further] free market policies.” Indeed, Brash and his close political allies “referred to [this] privately as the ‘Grand Plan’.”

The elevation of Brash to the leadership served to quickly rejuvenate the National Party’s flagging electoral fortunes. After spending most of 2003 languishing in the polls at around 25%, National soared to 45% in February,

---

35 Hager, 41.
36 Ibid, 62.
37 Ibid, 69.
Central to National’s rapid resurgence was the issue of race relations. National successfully exploited deep-seated prejudice and mounting frustration within the broader populace (but especially amongst older Pakeha New Zealanders) relating to perceived preferential treatment of Maori in society in order to regain political ascendancy. This process was initiated on 27 January, 2004 in an address made by Brash to the Orewa Rotary Club. In this speech (entitled “Nationhood”), Brash proposed that New Zealand should have just “one people, living under one set of laws.” To this end, Brash boldly called for the abolition of so-called “special privileges” for Maori (including separate Maori seats in parliament) and an end to an “entrenched Treaty grievance industry.”

In mid-2004, a small but important new force also emerged onto New Zealand’s political landscape. On 7 July, former Labour Party MP Tariana Turia formed the Maori Party. The formation of the Maori Party was precipitated by Labour’s announcement of controversial Seabed and Foreshore legislation. On 19 June, 2003 the New Zealand Court of Appeal ruled that the Maori Land Court had jurisdiction to determine ownership claims made on the seabed and foreshore. In response, the FLG proposed legislation that would essentially ensure perpetual Crown control over the foreshore and seabed. The Government’s proposal created widespread discontent amongst Maori. It also impelled Tariana Turia to resign as a Labour MP. Turia successfully defended

39 de Malmanche, 559.
42 Ibid.
43 de Malmanche, 562. Turia was subsequently joined as party co-leader by prominent academic Pita Sharplees.
44 Ibid.
45 Attorney-General v Ngati Apa [2003] 3 NZLR 643 (CA).
47 de Malmanche, 554.
her Maori electorate seat of Te Tai Hauāuru at the resulting by-election, and subsequently returned to parliament at the head of the newly-formed Maori Party.

Consequently, the outcome of the 2005 general election was far from a *fait accompli*.48 The emergence of the Maori Party constituted a serious threat to Labour’s historical dominance of the Maori electorates.49 This was borne out in the final election result, with the Maori Party claiming four of the seven Maori seats.50 Meanwhile, the rejuvenation of National under Brash’s leadership meant that, on the broader political stage, the “intensely fought” election campaign was a particularly close-run contest.51 Indeed, the National Party leadership claimed that it came extremely close to being able to form an alternative centre-right government in the weeks following the 17 September election.52

However, as Johansson observes, “ultimately, the Labour Party prevailed”, securing “a third successive term for only the second time in its history.”53 Labour won 41.1% of the party vote and a total of 50 parliamentary seats at the 2005 election. This result endowed Labour with “a narrow two-seat advantage over National”, who respectively won 39.1% of the party vote and 48 seats.54 Labour again entered into a formal coalition with the Progressives. Leader Jim Anderton, however, was their only successful candidate. Consequently, support on issues of confidence and supply was solicited from New Zealand First and United Future (who secured seven seats and three seats respectively) in exchange for ministerial roles outside of cabinet.55 Additional

---

49 Levine and Roberts 2007, 30.
51 Ibid.
54 Ibid, 63; Levine and Roberts 2007, 34.
55 Ibid
support on issues of confidence and supply was garnered from the Greens who won 5.3% of the popular vote and six seats.\textsuperscript{56}

Labour’s victory at the 2005 election was at least partly due to superior campaign tactics.\textsuperscript{57} The announcement of interest-free student loans for tertiary education in conjunction with a major new expansion of Working for Families (WFF, discussed further below), for example, proved a broadly effective counter to popular tax cut proposals announced by National. Another salient factor, however, was undoubtedly leadership. As Levine and Roberts observe, “the inexperienced Brash committed various gaffes and blunders during the campaign”, which contrasted markedly with the “experienced Clark, fluent and competent.”\textsuperscript{58} This significant disparity in the quality of leadership on offer was of crucial significance. Fundamentally, it meant that while National under Brash “was able to occupy much of the political space previously taken up by ACT, New Zealand First, and United Future”, it was largely unable to dent Labour’s large base of electorate support and thereby take control of parliament.\textsuperscript{59}

Despite successfully staving off National’s strong challenge at the 2005 election, the political tide had nevertheless turned against the FLG. Support for Labour began to fall away dramatically subsequent to the election, a process that continued throughout its third term in office. Driving Labour’s fading electoral appeal was a widespread perception that it was over-taxing the populace, whilst simultaneously fostering the creation of a so-called ‘nanny state’. The trend was accelerated, however, by John Key’s replacement of Don Brash as leader of the National Party in November, 2006. Key’s elevation to the position of Leader of the Opposition quickly enhanced National’s appeal to the

\textsuperscript{56} Ibid.


\textsuperscript{59} Ibid, 345. Labour’s share of the party vote was only 0.2% lower than in 2002.
political centre, directly at the expense of the FLG. The FLG did make a last-ditch attempt to be returned to power in 2008, highlighting their record of sound economic management and the desirability of strong leadership during times of economic uncertainty following the onset of the GFC (see Chapter Seven). This attempt, however, ultimately failed; as discussed in more detail in Chapter Seven, John Key and the National Party displaced the FLG at the 2008 election.
5.2) The Fifth Labour Government’s Third Way

As Roper observes, “with respect to its broad ideological and policy orientation” under each of its various guises the FLG “presented itself as treading a middle path between the extensive interventionism of the old Social Democratic Left and the extreme free-market orientation of the New Right.”

“Ours is a third way government striving to achieve a better balance between a dynamic market economy and a fair society which offers opportunity and security to all” averred Prime Minister Helen Clark at the end of her first year in office. Globally, the term ‘Third Way’ refers to a broad ideological stream generally associated with the political programmes pursued and advocated in the US in the 1990s by the Clinton Administration, and later in the UK by the Labour Government under Tony Blair. An extensive literature covering the various facets of this so-called Third Way already exists, so here the discussion is restricted to only a brief excursus on its central tenets.

According to Anthony Giddens, widely acknowledged as the most prominent intellectual exponent of the Third Way, three key transformations have fundamentally altered the contemporary socio-political landscape: the advent of fully realised ‘globalisation’; the rise of the ‘knowledge economy’; and the rise of individualism. On the basis of these changes, Giddens upholds that “as a theory of the managed economy, socialism barely exists any longer” and, furthermore, that the “Keynesian welfare compromise...has been largely dissolved.” In addition, however, Giddens and other intellectual exponents of the Third Way have also acknowledged that “the electorate has recoiled” from

---

60 Roper 2005b, 226.
61 Helen Clark, quoted from the New Zealand Herald, September, 2000 by J. Kelsey 2002, At the Cross Roads (Wellington: Bridget Williams Books), 50.
64 Giddens 2001, 3-4.
the market-driven policy prescriptions of neoliberalism. In reaction to these developments, the Third Way is couched by its advocates as a pragmatic renewal of social democracy in response to changing contemporary social and economic conditions. Consequently, it is considered to constitute “a very fundamental paradigm shift in politics.”

It is important to note that while the Third Way fundamentally rejects substantive traditional ideas of socialism, its respective criticism of the prevailing neoliberal policy framework is much more restrained. As many authors have observed this raises serious questions relating to the accuracy of Giddens’ claims that the Third Way represents a fundamentally ‘new’ framework for public policy. Indeed, Kelsey goes so far as to state that the Third Way functions simply in order for ‘centre-left’ governments to be able to “rationalise their role in consolidating neoliberalism” as the dominant global political paradigm.

The broad policy orientation of the Third Way has been developed at length by Giddens, although as Kelsey and others have observed, it generally suffers from a marked lack of specificity when it comes to establishing a substantive policy framework. According to Giddens the Third Way involves the implementation of various ‘structural reforms’ aiming to ‘modernise’ the role of the state in response to the ‘fundamental transformations’ that have occurred within the contemporary socio-political arena. Centrally, the state should look to “preserve a core of collective social justice, while defending individual autonomy of action.” As Roper argues, however, the broad policy programme of the Third Way can be more succinctly and accurately summarised as involving a generalised commitment to most of the key features of neoliberalism. The

69 Ibid, 58; Zuerge, 90.
70 Kelsey 2002, 54-55.
Third Way continues to uphold: a leaner bureaucracy; “a commitment to continuing private ownership of formerly state-owned enterprises”; a smaller, more targeted welfare system; a taxation system characterised by a historically low level of progressiveness; a “lightly regulated” economic arena (including industrial relations and international trade); fiscal austerity; and, most importantly, monetarist macroeconomic management and a highly liberalised and deregulated financial system. The Third Way does acknowledge the requirement for governmental involvement in the economy, but the government’s capacity for involvement is largely restricted to the stimulation of “technological innovation and economic investment.” ‘Social justice’ is also recognised as an important element of Third Way politics and for this reason a Third Way agenda supports the retention of a limited degree of progressive taxation and rejects the neoliberal ‘safety-net’ welfare system.

As documented by Kelsey, the Third Way was adopted by the Labour Party in New Zealand in mid-1998. Labour’s Third Way was to seek a balance between Keynesian Social Democracy’s overemphasised “commitment to the collective”, and neoliberalism’s ‘overstressing’ of atomistic self-interest. In terms of an actual substantive guiding policy framework, however, there was little beyond vague, Giddens-esque policy-lines. The incoming FLG indicated their intention as being “to implement a policy platform which reduces inequality, is environmentally sustainable, and improves the social and economic wellbeing of all New Zealanders.”

In substantive terms, the core of the FLG’s social democratic agenda initially took the form of ‘closing the gaps’. As Minister of Finance Michael Cullen stated in his first budget speech, “for too long, New Zealand governments have ignored the growing gap between rich and poor. This

---

71 Roper 2005b, 229.
72 Giddens 2001, 8, 9, 10.
Government is committed to closing the gaps.” The major features of ‘closing the gaps’ included: an increase in the top marginal rate of income tax from 33% to 39% on all income over $60,000 per annum; the restoration of income-related state-housing rents (set at 25% of income); the restoration of the married couple superannuation provisions to no less than 65% of the average wage; progressive increases in the statutory minimum wage; and the indexing for inflation of social welfare benefits.

From 2004 onwards, the focus of the FLG’s social democracy agenda shifted to the WFF policy package. Involving expenditure of $1.1 billion at maturity, the “centerpiece of Budget 2004” was intended to deliver “a social dividend to low income families.” Measures encapsulated within this broad program included more targeted assistance through “increases to Family Support, a new in work payment, [an] increase in the family tax credit and changes to abatement rates and thresholds.” Budget 2004 claimed that by 1 April 2007, over 300,000 households would be receiving direct assistance, with an average benefit for households earning between $25,000 and $45,000 per annum being in the vicinity of $100 a week. 2006 saw a significant expansion of the package with additional funding of $1.845 billion over four years announced, including tax relief for 350,000 people and improved overall access to the programme.

However, the substantive progressiveness of the FLG’s measures towards reviving social democracy in New Zealand should not be overstated. In the preceding chapters it was argued that the process of neoliberalisation undertaken in New Zealand between 1984 and 1999 was exceptionally swift and comprehensive in comparison to other states of the advanced capitalist

78 Ibid, 9, 12.
79 Ibid, 12.
81 Kelsey 2002, 68.
world. Indeed, New Zealand has been characterised as a paragon of voluntary neoliberal ‘structural adjustment’. The measures undertaken by the FLG in order to ‘close the gaps’ and ‘work for families’ constituted only a limited retreat from this hardline neoliberal policy agenda. Although Working for Families was expanded further after their work was published, St. John and Craig argue, for example, that the money being directed to the Working for Families programme in particular was actually small in both absolute and relative terms.\(^82\)

As will be argued throughout the rest of this chapter, in essence the FLG’s Third Way largely operated to entrench the existing neoliberal policy framework.\(^83\) All of the economic fundamentals of the neoliberal policy framework remained, yet it was precisely these factors that would ultimately determine the sustainability of a meaningful shift towards social democracy.\(^84\) All of the “legislative ‘lynch-pins’” of the neoliberal program of macroeconomic management remained in place: “the Reserve Bank Act 1989, the Fiscal Responsibility Act 1994, and the Public Finance Act 1989 (the last two essentially incorporated within, rather than being fundamentally changed by, the Public Finance Management Amendment Act 2004).”\(^85\) Furthermore, the financial markets, including the FX market, and the domestic finance sector remained highly liberalised and deregulated. This suggests that the DWSR retained significant capacity to influence public policy formulation in New Zealand, and that, in particular, interests closely-linked to IPFMs continued to exert considerable pressure on the New Zealand state. We will return to this specific issue in the following two chapters where it will be addressed in detail.

---


\(^83\) Roper 2005b, 235.

\(^84\) Kelsey 2002, 69.

\(^85\) Roper 2005b, 234-235.
5.3) The Fifth Labour Government’s Macroeconomic Policy Nexus

Monetary Policy

In May 2000 internationally recognised monetary policy expert Professor Lars Svenssen of Stockholm University was appointed to undertake an independent review of monetary policy in New Zealand. The aim of the review was to examine how the legislative framework underpinning monetary policy and the RBNZ’s operations within this framework aligned with “the characteristics of the New Zealand economy” and, subsequently, whether they were “consistent with best international practice.” The results of the Svenssen review were announced by the Minister of Finance, Michael Cullen, on 7 August, 2001.

As Archibald outlines, there were two main areas that received the most attention and where the “most far-reaching changes were proposed.” The first major area of focus of the review was the monetary policy decision-making framework. Centrally, Svenssen argued that “vesting responsibility for monetary policy decisions in a single individual carried an inherent risk.” He suggested that instead the monetary policy decision-making framework should be altered to assign responsibility to a committee and, further, that this committee should necessarily include more external members (non-RBNZ employees) and private sector consultation. The second key strand of the review focused on the arrangements for ensuring that monetary policy

88 Ibid.
89 Ibid, 5.
90 Ibid, 7-8.
91 Ibid.
formulation was “subject to effective accountability and monitoring.” Here Svenssen was primarily “concerned about the conflicts of interest that could potentially arise from having the Governor and Deputy Governors of the Bank as Board members, given that the Board’s primary role is to monitor the performance of the Governor and the Bank.” Svenssen suggested “that it would be preferable to remove the Governor and the Deputy Governors from the Board completely.”

Beyond these central strands of critique, Svenssen only recommended various “marginal improvements, mostly of a technical nature” for the RBNZ to pursue. Perhaps most prominent amongst these was the recommendation that “at the beginning of the next term of the Governor, the Policy Targets Agreement (PTA) should be marginally modified to include the medium-term point target directly.” Although it was already effectively standard RBNZ operating practice, this latter recommendation was implemented, as suggested by Svenssen, when the FLG signed its next PTA with the new RBNZ Governor, Allan Bollard, on 17 September, 2002.

The broader body of recommendations made by the Svenssen review that were subsequently accepted by the FLG were implemented as a major portion of an amendment of the Reserve Bank Act 1989 (RBA) announced in August 2003. In regard to the first focal area of the Svenssen review, the Government maintained - with the support of both the RBNZ and its non-executive directors - “that there was little to be gained, …in terms of clarity of accountability and communications, by substantially altering a governance framework that has served this country well since its inception in 1989.”

92 Ibid, 5.
93 Ibid, 9.
94 Ibid, 9.
95 Ibid, 7.
Finance Minister Michael Cullen did admit, however, “that the monetary policy decision-making process might be further enhanced by expanding...its external consultation processes.”

Likewise in relation to the second key focal area of the Svenssen review “some, but not all, of Professor Svenssen’s recommendations with respect to the Board were adopted by the Government.” It was “agreed that the Deputy Governors should cease to be on the Board”, however the Governor was retained (although not as Chairman) “principally for the sake of facilitating information flow between the Bank’s executive and the Board.”

A further amendment of the RBA was passed in October 2006. This legislation primarily served to implement the FLG’s response to the recommendations of the Trans-Tasman Council of Banking Supervision. The 2006 Amendment was focused on adjusting Part 5 of the RBA in particular (introducing a new section; 68A). However, as DeSourdy observes, the 2006 Amendment essentially only served to formalise cooperation between New Zealand and Australian financial authorities that was already occurring.

The above account reveals that, fundamentally, the neoliberal legislative framework governing the operation of monetary policy in New Zealand underwent only very minor adjustment during the period from 1999 to 2008. This point is clearly highlighted through an examination of the content of the RBNZ and FLG’s final PTA, signed on 24 May, 2007. The key element to note here is the first and most important section of the PTA, Section 1a. This section states that “under Section 8 of the Act the Reserve Bank is required to conduct

---

99 Archibald, 8. The “consultation processes” that have been broadened and given more profile include the RBNZ’s business visits programme, its peer review process, and the appointment of part-time external advisors. See Archibald, 8-9.

100 Archibald, 9.


104 RBNZ 2007, Policy Target Agreement 2007 (Wellington: RBNZ).
monetary policy with the goal of maintaining a stable general level of prices.”105 This demonstrates that, despite obviously having ample opportunity to undertake substantive policy transformation in this area, at no point were the most integral features of the RBA considered for alteration. Indeed, it is worth noting that:

in announcing the terms of reference of the (Svenssen) review, the Treasurer, Hon. Dr Michael Cullen, emphasised that some central features of New Zealand’s monetary policy framework were not open for review. Dr Cullen stated that the statutory objective of monetary policy – price stability – was a critical feature of the monetary policy framework and would not be subject for review. The Government also indicated that it would not be considering changes that would lessen the Reserve Bank’s autonomy in formulating and implementing monetary policy.106

Thus, the various legislative adjustments implemented by the FLG did “not herald a major change” in their approach to monetary policy.107 In 2001 then RBNZ Governor Don Brash stated that “the reality is that, beyond the contribution they can make by maintaining inflation at a low level, central banks cannot have a substantial effect on trend growth in output or trend growth in employment.”108 It is apparent that those responsible for the formulation of the FLG’s monetary policy also subscribed to this core principal of neoliberal monetarist macroeconomic management. A “strong emphasis” continued to be placed on market-oriented self-discipline for the financial sector.109 The various adjustments simply aimed to “assist the Bank to reinforce

105 Ibid.
106 Archibald, 4.
109 Ibid.
market and corporate governance mechanisms for promoting a sound” financial system “through the…use of a more focused regulatory” regime.\textsuperscript{110}

Within this broader legislative framework guiding the RBNZ’s operation of monetary policy, it is also obvious that there was little change from the incumbent neoliberal policy regime in terms of policy implementation. The RBNZ’s overarching strategy for the implementation of monetary policy during the period from 1999 to 2008 continued to be based around the management of the level of settlement cash available to the domestic banking system. Moreover, the operation of this strategy continued to involve directly targeting levels of employment as a means of controlling the rate of inflation.

In Chapter Three it was shown that the post-1984 ‘monetarist’ macroeconomic reforms entailed a fundamental transformation of New Zealand’s monetary policy implementation strategy. The existing system based on strict regulatory controls was replaced with an approach oriented around the operation of significantly deregulated and liberalised financial markets. Under this new system the RBNZ’s main monetary policy implementation tool was (arguably) its control over the aggregate level of overnight settlement cash available to the domestic financial system.\textsuperscript{111} Based on Milton Friedman’s maxim that inflation was always a purely monetary phenomenon, official accounts maintained that control over the quantity of settlement cash available to the system enabled the RBNZ to, in turn, exert a significant degree of control over primary liquidity (and consequently inflation) in the New Zealand economy.

In February 1999, the RBNZ adopted a new “primary instrument for implementing monetary policy” in New Zealand.\textsuperscript{112} This new tool was the Overnight Cash Rate (OCR) system. Under the OCR system, the RBNZ no

\textsuperscript{110} Dalziel 2004, 59.

\textsuperscript{111} Dalziel 2004, 59.

longer strictly controls the quantity of settlement cash, but instead controls its price. This price is known as the OCR. The main features of the OCR regime are summarised in Table 5.1 below.

**Table 5.1: The Main Features of New Zealand’s OCR Monetary Policy Regime**

- The RBNZ reviews the domestic situation in regard to inflation every six weeks and adjusts the OCR accordingly.
- Banks have “Standing Facilities” with the RBNZ allowing them to obtain overnight settlement cash in unlimited quantities at an interest rate 25 basis points above the OCR and deposit overnight at 25 basis points below the OCR.
- The RBNZ continues to operate open market daily liquidity management operations (OMOs) by injecting or withdrawing settlement cash at market rates.
- The RBNZ’s OMOs aim to leave a quantity of settlement cash in the system approximate to a specified (but inherently adjustable) level.


The main implication of the adoption of the OCR system has been the establishment of a much more stable relationship between the RBNZ’s key monetary policy tool and the rest of the bank bill yield curve (broadly referring to the domestic interest rate markets). Under the previous regime, the RBNZ’s market intervention rate was tied to an inherently volatile market-determined interest rate. As Brookes and Hampton observe, however, because under the OCR-based regime the RBNZ “is now willing to borrow and lend unlimited quantities overnight to the market at predetermined rates, the new regime

---


114 Brookes and Hampton 2000, 56.
effectively constrains (but does not set directly) the overnight interest rate.”

This point is highlighted in Figure 5.1 below. As can be seen, fluctuations in overnight interest rates have reduced considerably since the adoption of the OCR system.

Figure 5.3) Daily Changes in New Zealand Overnight Interest Rates, January 1995 to January 2000

Source: Brookes and Hampton 2000, 54.

---

115 Ibid.
As Dalziel outlines, “the OCR is the interest rate that financial institutions have to pay the Reserve Bank to borrow cash.”\footnote{Dalziel 2004, 59.} Because of this, it effectively serves as a base rate on which all other domestic interest rates are set.\footnote{Ibid.} Due to the existence of the RBNZ’s standing facilities “no bank would normally pay another bank a higher interest rate for overnight cash than the rate at which it could borrow from the Reserve Bank.”\footnote{Brookes and Hampton, 54.} Likewise, “no bank would deposit with another bank at an interest rate lower than that offered by the Reserve Bank.”\footnote{ibid; Drew and Sethi, 9.} Thus, the RBNZ effectively controls domestic overnight interest rates because “the Bank’s willingness to transact in large volume effectively eliminates the need to do so.”\footnote{Brookes and Hampton, 55.}

Further, as can be seen from Figure 5.4 above, the introduction of the OCR has also had a marked impact on the short-term interest rate market. As Brookes and Hampton observe, “under the previous implementation
regime...day-to-day movements in the exchange rate were, to varying degrees, prompting movements in the 90 day and other short-term rates.” The introduction of the OCR system, however, has served to remove “the strong day-to-day link between exchange rate fluctuations and short-term interest rate fluctuations.” The OCR has tended to have a noticeable impact on forward interest rates out to around a year, but its impact has been most clearly signified by a marked decrease in volatility in the high-profile 90-day interest rate, both in actual volatility and expected volatility, as evidenced by trends in options prices.

However, despite the adoption of the OCR system, the FLG nevertheless continued to operate what Whitwell accurately labels an “anti-employment” monetary policy regime. New Zealand’s monetary policy implementation strategy during the period from 1999 to 2008 was still fundamentally “a thinly disguised incomes policy with a selective focus: the profitability of the traded goods sector.” The key difference was that the unemployment element of New Zealand’s monetary policy strategy was no longer implicit; unemployment is a crucial in-built aspect within official accounts of the RBNZ’s contemporary monetary policy transmission mechanism (MPTM).

A detailed flow chart illustrating the main features of New Zealand’s MPTM can be seen below in Figure 5.5. As can be seen from this, New Zealand’s OCR-based MPTM operates along three main channels: the interest rate channel; the exchange rate channel; and the expectations channel. It is also important to observe that especially in the latter portions of the monetary cycle there are significant overlaps of these channels. Briefly summarising the general operation of New Zealand’s OCR-based MPTM, Drew and Sethi

---

121 ibid, 59.
122 ibid, 60.
123 ibid.
124 Whitwell, 117-118.
125 Ibid, 102.
126 Drew and Sethi, 5.
describe three major stages in the contemporary monetary cycle. At the first stage of the monetary cycle, “the most immediate impact of a change in monetary policy settings is seen in the markets for short-term bank bills and bonds, and in those for highly liquid financial assets such as foreign exchange.” 127 The markets for longer-term bonds, equities and real estate will also respond during this first phase of the monetary cycle, but generally not to the same degree as the former. These comparatively illiquid asset classes are based around both a broader and longer ranging market-scope beyond the short-term changes in the OCR. 128 At the second stage of the monetary cycle, “the net effect of a change in these bond and asset prices is to prompt households and firms to re-assess their consumption, investment and other business decisions.” 129 Following an indeterminate lag, “these decisions” then “percolate through to aggregate spending in the economy.” 130 At the final stage of the monetary cycle, again usually following a lag, “these changes in aggregate activity influence pricing pressure in the economy” and thus exert control over inflation. 131 Overarching the whole monetary cycle, the expectations channel serves to reinforce the effectiveness of the RBNZ’s policy stance.

It is important to observe that the RBNZ now largely ignores the role of the money supply in the MPTM. As discussed above, under the incumbent OCR-based monetary policy regime the RBNZ effectively only controls the price of money. The quantity is now “created either directly by the Bank or by the banking system as necessary to satisfy demand for money.” 132 Consequently, the quantity of money in the domestic economy is not a policy target in itself. As Drew and Sethi observe, “this may seem at odds with Milton

127 Ibid, 8.
128 Ibid, 9.
129 Ibid, 8.
130 Ibid.
131 Ibid.
132 Ibid, 10.
Friedman’s maxim that ‘inflation is always and everywhere a monetary phenomenon’.”\textsuperscript{133} However, the RBNZ now upholds (in-line with Whitwell’s initial critique outlined in detail in Chapter 3) that “in practice the links between money growth, output and inflation are often quite weak and unstable” and that “as a result, monetary aggregates have generally not proven to be particularly useful indicators for monetary policy.”\textsuperscript{134}
Figure 5.5) The Transmission Mechanism of New Zealand Monetary Policy

Source: Drew and Sethi, 6.
Instead, as can be seen from Figure 5.5 above, the RBNZ’s OCR-based monetary policy regime is now quite openly oriented towards impacting on real economic activity, with unemployment constituting a key in-built feature of the MPTM. As Drew and Sethi delineate, “the dominant theory...for thinking about the link between aggregate activity and inflation is an economic relationship known as the expectations-augmented Phillips curve.” The key features of this relationship in New Zealand’s specific context are set out in Table 5.2 below.

**Table 5.2) The Key Features of New Zealand’s Expectations-Augmented Phillips Curve**

- When aggregate output expands above the economy’s “supply capacity” (also known as potential output) a positive “output gap” opens up and non-tradables inflation rises.
- A rise in inflation causes expectations of future inflation to increase.
- To prevent ever-increasing inflation and inflation expectations, a more than one-for-one monetary policy response is required to return output to potential levels and to re-anchor inflation expectations at the target rate.

Source: Based on Drew and Sethi, 16.

Centrally, the RBNZ’s conception of New Zealand’s Phillips curve upholds that “economic booms that expand the level of output significantly above its potential level are usually followed by a pick-up in domestic or non-tradables inflation.” In response the RBNZ initiates its monetary policy response via the raising of the OCR, which, as detailed above, serves to raise both short-term domestic interest rates as well as the FX rate (Figure 5.5 boxes 1

---

135 Ibid, 16.
136 Ibid, 17.
and 5). Put succinctly, these developments serve to prompt a decline in broader economic activity. The non-tradables sector, dominated by the real estate industry in New Zealand, is affected primarily in the form of declining demand for mortgages and other forms of consumer credit. However, it can be seen that the tradables sector will be especially negatively affected. Tradables are directly exposed to both the real-time transmission channels; the interest rate channel and the exchange rate channel. Thus while, like other firms, the tradables sector will find it more expensive to finance investment, New Zealand’s export producers will also experience declining profitability based on a generalised reduction in international competitiveness. (Figure 5.5 box 13).  

As a consequence, firms will look to rationalise overall activity and reduce employment (Figure 5.5 boxes 11 and 13). Drew and Sethi observe that, thus, the combined interest rate and exchange rate channels place “downward pressure on various income streams flowing to households, reducing overall discretionary consumption” (Figure 5.5 boxes 7 and 8). As can be seen from Figure 5.5 (box 15), this is the most significant contributor to the response of net output to the change in the RBNZ’s monetary policy stance, which, in turn, is shown to be the key driving factor behind domestic (non-tradables) inflation (box 16).

Thus, it can be seen that the OCR-based monetary policy strategy the RBNZ operated under the FLG from 1999 to 2008 worked in the same effective manner as the previous quantity-based settlement cash system. It provides a more stable link between the RBNZ’s official policy stance and their intended target (short-term financial asset markets), however, official RBNZ accounts now also uphold a central position within the MPTM for the impacts of their implementation on real economic activity, particularly the tradables sector (with the exchange rate channel being the main contributor to this). Indeed, the

---

137 Ibid, 16.
138 Ibid, 15.
139 Ibid.
RBNZ now specifically avoids any pretense of being able to exert any meaningful control over primary liquidity.

**Foreign Exchange Policy**

As outlined in Chapter Three, New Zealand adopted an independent floating exchange rate regime in 1985. During the period from 1999 to 2008, the FLG continued to endorse the operation of a free floating FX rate, “albeit with varying degrees of periodic intervention in foreign exchange markets.” 140 The maintenance of a floating FX regime essentially fits standard international practice. As illustrated by Table 5.3 below, since the beginning of 2000, of 22 ‘developed market economies’ “ten have opted to join the euro area, nine float their currencies independently, and the remaining three [Singapore, Hong Kong and Denmark] are special cases…” 141 Fundamentally, under the FLG, the RBNZ supported the retention of an independently floating currency. “The Bank believes strongly in the virtues of a floating exchange rate within a well managed economy”, it averred. 142 Indeed, in line with the prescriptions of the international neoliberal economic orthodoxy, the RBNZ upheld that “in general…the (floating) exchange rate can act as a significant buffer for the economy.” 143 In particular, the floating FX regime “helps the economy to adjust to ever-changing domestic and global conditions” by allowing “efficient absorption of shocks to the current account.” 144

141 ibid, 15.
144 Eckhold and Hunt, 13; Bjorksten and Brook, 16.
Table 5.3) Exchange Rate Arrangements in Developed Market Economies (as of 31 December 1999)

Key: NS = Arrangements with no separate legal tender  CB = Currency Board
     HB = Pegged rate in horizontal band  IF = Independently Floating
     MF = Managed Float with no pre-announced exchange rate path

<table>
<thead>
<tr>
<th>Euro Area</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>NS</td>
</tr>
<tr>
<td>Belgium</td>
<td>NS</td>
</tr>
<tr>
<td>Finland</td>
<td>NS</td>
</tr>
<tr>
<td>France</td>
<td>NS</td>
</tr>
<tr>
<td>Germany</td>
<td>NS</td>
</tr>
<tr>
<td>Ireland</td>
<td>NS</td>
</tr>
<tr>
<td>Italy</td>
<td>NS</td>
</tr>
<tr>
<td>Netherlands</td>
<td>NS</td>
</tr>
<tr>
<td>Portugal</td>
<td>NS</td>
</tr>
<tr>
<td>Spain</td>
<td>NS</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Based on Bjorksten and Brook, 15.

Following a two-part review of the RBNZ’s intervention capacity, on 30 March, 2004, the FLG adopted a new FX intervention policy into its monetary policy framework and simultaneously implemented minor changes to the existing ‘crisis management’ intervention policy.145 Since the inception of New Zealand’s floating FX regime, the RBNZ has possessed a limited scope for FX market intervention. Under the RBA, the RBNZ has a standing order from the Minister of Finance “to intervene at any time to ensure the continuous operation of the foreign exchange market.”146 The RBA also established an

146 Gordon, 4.
obligation for the RBNZ “to hold foreign reserves in order to carry out” this “intervention at short notice.”\textsuperscript{147} For this reason the RBNZ always maintains possession of a significant “portfolio of liquid, high quality, foreign currency assets.”\textsuperscript{148} As Gordon notes, the target level of reserves had remained largely unchanged at $4-5 billion since the policy’s inception in 1988.\textsuperscript{149} Consequently, the RBNZ recommended that its intervention capacity for ‘crisis management’ should be increased as ‘insurance’. The FLG Minister of Finance, Michael Cullen, agreed with this advice and in February 2004 increased the target level of foreign reserves “to a minimum of $7 billion.”\textsuperscript{150}

However, as Eckhold and Hunt outline, the focus of the RBNZ’s existing intervention capacity was purely “on preserving the functioning of the foreign exchange market in a crisis, rather than preserving any given level of the exchange rate \textit{per se}.“\textsuperscript{151} In contrast, the new FX intervention policy adopted by the FLG equips the RBNZ with “the capacity to use foreign exchange intervention in order to influence the level of the exchange rate.”\textsuperscript{152} In essence, RBNZ FX intervention involves the purchase/borrowing or sale/repayment of New Zealand dollars (NZD) in exchange for foreign currencies. Under the new approach to currency intervention, the RBNZ will intervene in the FX market when the NZD is considered to have “moved well in excess of any relevant economic fundamentals, such as relative productivity, commodity prices, growth, or inflation.”\textsuperscript{153} As detailed by Eckhold and Hunt, “intervention near the peaks of the exchange rate cycle will leave the Bank with an open (unhedged) net “long” foreign currency position.”\textsuperscript{154} Conversely, “intervention

\begin{flushleft}
\textsuperscript{147} Ibid.
\textsuperscript{148} Orr, 83.
\textsuperscript{149} Gordon, 11.
\textsuperscript{150} Ibid.
\textsuperscript{151} Eckhold and Hunt, 12.
\textsuperscript{152} Ibid
\textsuperscript{153} Orr, 83.
\textsuperscript{154} Eckhold and Hunt, 14.
\end{flushleft}
The Fifth Labour Government and Macroeconomic Policy

287

at troughs will result in an open net ‘short’ currency position.” The RBNZ subsequently closes its foreign currency position when it considers that the exchange rate has returned to near its long-term equilibrium value.

Centrally, the FLG introduced this new intervention tool into its FX policy framework to serve as an auxiliary monetary policy tool. “Foreign exchange intervention can be viewed as another instrument for the Bank, consistent with achieving our monetary policy objectives, albeit a very secondary instrument to our most powerful one of the Official Cash Rate.” As previously indicated, the OCR operates to achieve price stability while minimising unnecessary short-term financial market volatility. However, the FX market, forming one of the three major monetary transmission channels, remains inherently volatile. Indeed, Eckhold and Hunt observe that short-term speculative behavior and other “non-fundamental drivers may at times push the exchange rate to extreme levels”, rendering “the task of achieving price stability while minimising unnecessary volatility difficult.” The FLG’s new intervention element “is aimed specifically at trimming the peaks and troughs of medium-term fluctuations in the NZD exchange rate.” Thus, while the OCR forms the core of the RBNZ’s monetary policy tool-set, sometimes intervention may also be used to assist the RBNZ in upholding its PTA obligations.

Ultimately, however, in line with its monetary policy stance outlined above, the changes undertaken by the FLG in regard to New Zealand’s FX policy regime constituted only a very minimal shift away from the incumbent neoliberal macroeconomic policy regime. As indicated by the criteria for intervention set out in legislation by the RBNZ, on the electoral defeat of the

155 Ibid.
156 Ibid.
157 Orr, 84.
158 Eckhold and Hunt, 12, 13.
159 Ibid, 13.
160 Ibid, 12.
FLG on 8 November 2008, New Zealand’s FX regime was still fundamentally oriented towards the minimisation of interference in financial markets. In order to fulfill the criteria for intervention under the FLG’s new intervention policy, the RBNZ must be satisfied that: the exchange rate is exceptionally high or low; the exchange rate is unjustified by economic fundamentals; intervention is consistent with the requirements of the PTA; and conditions in the market are opportune and will allow intervention a reasonable chance of success.\(^{161}\) But, as Eckhold and Hunt point out, “instances where there is a significant misalignment between the exchange rate and its fundamental value are probably few and far between. Further, it can be hard to identify exchange rate misalignments. Consequently, it is likely that we will intervene…rarely.”\(^{162}\) As Orr observes, “by far the bulk of foreign exchange risk management responsibility remains in the hands of the businesses and individuals within New Zealand.”\(^{163}\) Thus, despite the adoption of an additional monetary tool enabling FX intervention targeting the value of the NZD, the FLG still ultimately intended to operate its FX policy regime within bounds of a ‘monetarist’ framework. Like its broader monetary policy stance it still sought to operate its FX policy regime in a way that maintained its credibility with financial markets in order to enable the achievement of price-level stability.

**Fiscal Policy**

A close examination of the overarching fiscal strategy pursued by the FLG during the period from 1999 to 2008 also highlights a fundamental commitment to maintaining the existing neoliberal macroeconomic policy framework. The FLG continued to exercise fiscal policy in accordance with all of the central tenets of the key neoliberal legislative lynch-pin in relation to

\(^{161}\) Ibid, 15.
\(^{162}\) Ibid, 13.
\(^{163}\) Orr, 85.
fiscal policy; the 1994 Fiscal Responsibility Act (discussed in the previous chapter). The FLG did eventually implement changes to this key piece of neoliberal legislation. In late 2004 it implemented the Public Finance Management Amendment Act (PFMA). This was to come into effect on 25 January, 2005.\textsuperscript{164} The ostensible purpose of the PFMA was to “amend the law governing the use of public financial resources.”\textsuperscript{165} However, as Roper has observed, rather than altering them in any fundamental way, the PFMA 2004 essentially only incorporated the existing Fiscal Responsibility Act 1994 and Public Finance Act 1989.\textsuperscript{166} Indeed, the FLG’s 2004 Fiscal Strategy Report specifically states that “the Public Finance (State Sector Management) Bill integrates the Fiscal Responsibility Act into the Public Finance Act.”\textsuperscript{167}

As stated in Budget 2000, the FLG’s overarching fiscal strategy for the period from 1999 to 2008 was to adopt what it termed a “cautious approach” to fiscal policy.\textsuperscript{168} In his first budget speech as Finance Minister, Michael Cullen averred that: “we have promised to be a fiscally conservative government and we will hold to that promise.”\textsuperscript{169} Latterly, in what would be his last budget speech as Finance Minister, Cullen reiterated that promise. In Budget 2008 he stated that the FLG was still primarily focused on ensuring “sensible fiscal management.”\textsuperscript{170} Under the guiding principle of fiscal ‘caution’, the FLG’s fiscal strategy was formed of three main elements: a ‘conservative’ stance in relation to public expenditure; the retirement of the public debt position; and a commitment to “a robust, broad based tax system” that ensured strong revenue

\textsuperscript{165} PFMA, 11.
\textsuperscript{166} Roper 2005b, 234-235.
\textsuperscript{169} Ibid, 2.
A detailed statistical account of this broader fiscal policy stance is set out in Table 5.4.

The FLG’s ‘conservative’ expenditure stance was centred around the running of successive large structural surpluses, whilst simultaneously building up a significant financial asset in the form of the New Zealand Superannuation Fund (NZSF). As can be seen from Table 5.4, the FLG consistently achieved sizeable fiscal surpluses throughout the period from 2000 to 2008. On average these surpluses were worth around $4.5 billion per annum. Simultaneously, from 2002 onwards, the FLG successfully corralled a substantial portion of these surpluses into the newly established NZSF. The cumulative value of the NZSF totaled over $14.2 billion by 2008. Furthermore, it was projected “to reach $29 billion by 30 June 2012.”

To ensure the successful operation of this approach to the management of public expenditure, the FLG initially adopted a fiscal cap. In Budget 2000 the FLG maintained “a fiscal cap of $5.9 billion over four years.” This fiscal restriction was effectively upheld through until to 2002, although it was increased by $200 million in 2001 due to unforeseen defense spending outlays. Budget 2000 included an allocation of just $420 million for new spending. The largest component of this allocation was $200 million earmarked for new education initiatives. Budget 2001, meanwhile, included an only slightly larger allocation for new operating spending of around $476 million (excluding contingency funding). Health received the largest portion of this new funding. Some $246 million of new operating funding was allocated to public healthcare provision in 2001. The bulk of the remainder went to

---

177 Ibid, 5.
education and social services, which received $76 million and $87 million respectively.\(^\text{179}\)

*Budget 2002* began a trend of expanding new governmental expenditure through to 2008.\(^\text{180}\) Table 5.4 shows, for example, that after remaining relatively stable during the first term of the FLG, total government expenditure as a proportion of GDP began to trend upwards from 2003 onwards. This expansion of new spending during the period from 2002 to 2008 was underpinned by a significant increase in government revenues, which, as is discussed in more detail below, primarily derived from the prolonged upswing in the domestic economy (described above, see Figure 5.1). Indeed, *Budget 2008* states unequivocally that it was the Government’s successful conservative fiscal management acting in combination with the strength of the domestic economy that ultimately enabled “the Government...to deliver growth dividends to New Zealanders” in the form of increased public spending.\(^\text{181}\)

---

\(^{179}\) Ibid, 4.


### Table 5.4) A Statistical Overview of the Fifth Labour Government’s Fiscal Policy Stance

<table>
<thead>
<tr>
<th>Year</th>
<th>NZSF Cumulative Net Worth (billion)</th>
<th>OBEGAL (billion)</th>
<th>Total Crown Expenses (% GDP)</th>
<th>GSID (excluding Settlement Cash, billion)</th>
<th>Total Crown Revenue (%GDP)</th>
<th>Tax Revenue (billion)</th>
<th>Tax Revenue (% GDP)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>0</td>
<td>594</td>
<td>36.9%</td>
<td>32.9%</td>
<td>37.5%</td>
<td>33864</td>
<td>30.5%</td>
</tr>
<tr>
<td>2001</td>
<td>0</td>
<td>1422</td>
<td>36.9%</td>
<td>31.4%</td>
<td>38.1%</td>
<td>36250</td>
<td>30.6%</td>
</tr>
<tr>
<td>2002</td>
<td>615</td>
<td>2471</td>
<td>37.8%</td>
<td>29.1%</td>
<td>39.7%</td>
<td>38862</td>
<td>30.9%</td>
</tr>
<tr>
<td>2003</td>
<td>1884</td>
<td>4366</td>
<td>39.4%</td>
<td>27.6%</td>
<td>42.6%</td>
<td>39842</td>
<td>30.0%</td>
</tr>
<tr>
<td>2004</td>
<td>3956</td>
<td>5573</td>
<td>37.5%</td>
<td>25.2%</td>
<td>41.1%</td>
<td>42777</td>
<td>29.9%</td>
</tr>
<tr>
<td>2005</td>
<td>6555</td>
<td>7075</td>
<td>38.4%</td>
<td>23.3%</td>
<td>43.0%</td>
<td>47571</td>
<td>31.3%</td>
</tr>
<tr>
<td>2006</td>
<td>9855</td>
<td>7091</td>
<td>40.6%</td>
<td>21.4%</td>
<td>45.4%</td>
<td>50507</td>
<td>31.9%</td>
</tr>
<tr>
<td>2007</td>
<td>12973</td>
<td>5860</td>
<td>40.7%</td>
<td>18.2%</td>
<td>44.2%</td>
<td>52157</td>
<td>30.9%</td>
</tr>
<tr>
<td>2008</td>
<td>14212</td>
<td>5637</td>
<td>42.1%</td>
<td>17.5%</td>
<td>45.2%</td>
<td>55168</td>
<td>30.6%</td>
</tr>
</tbody>
</table>


However, increased government spending during the period from 2002 to 2008 did not signal an underlying shift in the FLG’s broader expenditure stance. Simultaneous to their expansion of expenditure, the FLG issued proclamations of their commitment to “fiscal prudence” *ad nauseam*. Thus, it appears that under less favourable economic circumstances the FLG would have demonstrated a markedly reduced degree of enthusiasm for increasing overall expenditure. Furthermore, the actual value of the spending needs to be viewed with a degree of caution. As Figure 5.6 shows, over much of the period

---

182 The statistical measure of the fiscal surplus used here is the Operating Balance Before Gains and Losses (OBEGAL). Treasury states that this is a preferable measure because it provides a more accurate indication of the government’s overall fiscal performance.

of study New Zealand experienced levels of inflation either close to or, indeed, in breach of the top of the RBNZ’s 1-3% target band. Cumulatively, this acted to significantly undermine the value of the FLG’s major new spending programs in real terms.

**Figure 5.6) CPI Inflation, 2000 to 2008 (%)**

![CPI Inflation, 2000 to 2008 (%)](image)


As can be seen from Figure 5.7 below, the FLG steadily reduced debt throughout their three terms in power. When the FLG was elected to office gross sovereign-issued debt excluding Reserve Bank settlement cash (GSID) stood at 33.7% of GDP.\(^{184}\) From this starting point GSID was reduced each year so that by 2008 it stood at just 17.5% of GDP.\(^{185}\) In *Budget 2000* the FLG set public GSID and net debt targets of 30% and 20% respectively.\(^{186}\) Progress towards these goals was so strong that in *Budget 2004* the FLG reduced both these debt targets. The FLG’s new debt management goal involved GSID as a percentage


of GDP being “slowly reduced over the longer term and passing through 20 per cent of GDP before 2015” and net debt being reduced “towards minus 15% of GDP by 2015 (that is., a net financial asset position).” As can be seen from Figure 5.7, by the end of its third term the FLG was on track to meet both of these debt targets. GSID was cited above as being below the target level well in advance and, further, “in 2006 the Crown moved into a net positive financial asset position for the first time in New Zealand history.”

Figure 5.7) Gross Sovereign-Issued Debt (excluding settlement cash) and Net Debt, 1994 to 2008

![Graph showing Gross Sovereign-Issued Debt and Net Debt from 1994 to 2008.]


At the heart of the FLG’s stance in regard to revenue generation was its overseeing of a burgeoning of government revenues. Table 5.4 shows that total government revenue almost doubled in nominal terms during the period from

188 Sourced from ibid 2008, “Executive Summary”, 18.
1999 to 2008. From $41.6 billion in 2000, total government revenues had increased to $81.5 billion in 2008. As indicated above, the significant expansion of revenues under the FLG can be largely attributed to the impact on the revenue base of the strong cyclical economic upswing experienced in New Zealand from 1999 to 2007. Centrally, prolonged strong economic growth entailed strong parallel growth in New Zealand’s tax base (company profits, personal incomes and consumer spending) and also the Government’s other major sources of revenue (particularly income from investments and sales of goods and services).[^190] Table 5.4, for example, shows that while Government tax receipts increased significantly, from $33.9 billion in 2000 to $59.2 billion in 2008, the tax take remained relatively stable as a proportion of GDP, trending up only slightly in the latter years of the FLG. This indicates that revenue growth was indeed closely linked to the strong corresponding growth in the wider economy.

However, it also needs to be observed that the tax system maintained by the FLG was an important element contributing to the increase in revenues. As predicted, the FLG’s taxation policy did not involve any significant increases within the structure of the taxation system. Indeed, beyond the initial re-establishment of a top tier of 39% for personal income over $60,000 (as necessitated by its 1999 election campaign promise), for much of its time in office the FLG undertook little effective action to reverse the regressive taxation reforms it inherited from the Fourth National Government. The FLG’s overarching priority in the realm of taxation policy was to ensure that it was able to generate a level of revenue sufficient to fund each of the key facets of its ‘conservative’ fiscal policy stance. For Labour Finance Minister, Michael Cullen, the best way to achieve this was by retaining “a direct tax system augmented by broadly based indirect taxes.”[^191]

During the second half of their time in office, the FLG did begin to undertake significant reforms of the tax system. These began in 2004 with the expansion of family tax credit provisions as part of the WFF package. But the FLG’s tax reform programme did not begin in substantive terms until the implementation of the Business Tax Reform package as one of the central features of Budget 2005. This had an initial costing of $1.9 billion over four years and formed the bulk of the 26% of Budget 2005 spent on tax reductions. Budget 2007 introduced a significant additional cut to business tax. The core of this reform consisted of a reduction of the tax rate on company profits from 33% to 30% at a forecast cost of $3.4 billion over four years. In 2008 a comprehensive package of personal tax cuts was adopted and implemented. The details of this are set out in Table 5.5 below. Michael Cullen stated that: “Budget 2008 delivers a meaningful reduction in tax for all New Zealanders. It will return a dividend of $10.6 billion to hard-working New Zealanders over the next four years.”

Table 5.5) Overview of the 2008 Personal Tax Reforms

<table>
<thead>
<tr>
<th></th>
<th>Tax Rates and Thresholds</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current</strong></td>
<td>15% 21% 33% 39%</td>
</tr>
<tr>
<td>Up to $9,500</td>
<td>$38,000 $60,000 Above $60,000</td>
</tr>
<tr>
<td><strong>New</strong></td>
<td>12.5% 21% 33% 39%</td>
</tr>
<tr>
<td>From 1 Oct 2008</td>
<td>$14,000 $40,000 $70,000 Above $70,000</td>
</tr>
<tr>
<td>From 1 April 2010</td>
<td>$17,500 $40,000 $75,000 Above $75,000</td>
</tr>
<tr>
<td>From 1 April 2011</td>
<td>$20,000 $42,500 $80,000 Above $80,000</td>
</tr>
</tbody>
</table>


---

Overall, however, the fiscal significance of the FLG’s various tax reforms was restricted. The business tax reforms, for example, while significant in nominal terms (cumulatively approximately $1.5 billion per year by 2008/09), were implemented via a staggered process. Respectively, the FLG only began to deploy its 2008 personal tax cuts programme a mere 38 days before it was ousted from power and New Zealander’s would not feel its full effects until April 2011. Ultimately, each of the FLG’s major tax reforms were introduced relatively late in their time in office and, further, full funding of the tax packages was generally delayed. This effectively served to severely curtail the impact of the tax reforms on the FLG’s overall revenue stance.
Conclusion

From 1999 to 2008 the FLG presented itself as operating a so-called “Third Way” policy agenda. The Third Way is couched by its proponents as a pragmatic social democratic policy paradigm responding to the dynamic nature of contemporary social, economic and political conditions. The defining characteristic of the FLG’s Third Way policy agenda, however, was the retention and entrenchment of the core pillars of the neoliberal macroeconomic policy nexus pursued in New Zealand since 1984.

In the realm of monetary policy the FLG made only minimal adjustments to the RBA 1989. The FLG’s monetary policy framework remained fundamentally oriented around the achievement of the core monetarist goal of maintaining a low stable rate of inflation coincident with minimal financial regulation. To achieve this, the RBNZ continued to operate what effectively constitutes an incomes policy. With the RBNZ no longer upholding particular concern for the level of primary liquidity, the MPTM explicitly operated to squeeze out inflation through crude efforts at crushing profitability in the tradables sector. Further, the FLG remained committed to an independently floating FX regime. The FLG expanded the RBNZ’s intervention capacity, but this represented only an extremely limited adjustment of the incumbent regime. The FLG’s FX policy stance remained fundamentally aligned towards enabling the effective achievement of their overarching monetarist goal of achieving and maintaining low and stable inflation. Respectively, the FLG pursued a conservative fiscal policy strategy in accordance with the distinctively neoliberal FRA. Centrally, the FLG restricted expenditure while overseeing a significant expansion of revenue. This enabled the building of substantial operating surpluses in order to fund the establishment and growth of a significant new financial asset, the NZSF, and the substantial retirement of the Government’s debt position.
As will be explored in the following chapter, the FLG was subject to a variety of political economic influences seeking to ensure its continued adherence to the neoliberal macroeconomic regime. Amongst these, considerable pressures deriving from New Zealand’s ongoing integration into the DWSR featured prominently.
Introduction

The overarching macroeconomic policy programme developed and deployed by the FLG during the period from 1999 to 2008 was described in Chapter Five. It was emphasised that, despite adopting the ideas of the (at least nominally) social democratic ‘Third Way’, the FLG nevertheless retained all of the key features of the existing neoliberal macroeconomic policy regime. A ‘monetarist’ approach to macroeconomic management primarily focused on achieving and maintaining low stable inflation, an independently floating foreign exchange (FX) regime, and a conservative approach to fiscal policy – emphasising the retirement of public debt, restricted public expenditure and low, broad-based taxation - were all firmly entrenched during the period from 1999 to 2008.

Respectively, this chapter seeks to provide an account of why the FLG retained all of these key features of the incumbent neoliberal policy regime as the core of its own macroeconomic policy nexus. Particular focus will be placed on the impact that integration into the Dollar-Wall Street Regime (DWSR) – via the program of financial market liberalisation and deregulation outlined in Chapter Three - had on the New Zealand state’s operational autonomy and the operation of the New Zealand democratic political system during the period from 1999 to 2008. This comprehensive account will ultimately be used to
discern the value that Gowan’s DWSR analysis provides for a sophisticated neopluralist interpretation and explanation of the shift from Keynesianism to neoliberalism in New Zealand.

The chapter begins with a discussion of the major domestic factors constraining the FLG’s autonomous formulation of macroeconomic policy during the period from 1999 to 2008. To this end, the macroeconomic policy agendas of the FLG’s key institutional advisors, the Treasury and the Reserve Bank of New Zealand (RBNZ), and the groups representing New Zealand’s major business interests will be outlined. The significant countervailing impact of the historically specific economic and electoral contexts will then be briefly delineated, before the nature of the constraints imposed on the FLG’s macroeconomic policy formulation by New Zealand’s integration into the DWSR are explored and explained. In the final section, the subsequent apparent political implications of financial market liberalisation in New Zealand are identified. The chapter concludes with a brief summary of the central argument.

In anticipation, the central argument asserts that New Zealand’s integration into the DWSR significantly constrained the FLG’s capacity to autonomously formulate and implement macroeconomic policy during the period from 1999 to 2008. It did this, in the first instance, by fundamentally altering the structural relationship between the state and international private financial capital in New Zealand.
6.1) The Domestic Constraints on Government Macroeconomic Policy Formulation, 1999 to 2008

The main set of domestic constraints that prevailed on the FLG’s macroeconomic policy formulation during the period from 1999 to 2008 ultimately derived from the same powerful group of political forces which, as was shown in Chapters Three and Four drove the initial neoliberalisation of New Zealand’s political economy from 1984 onwards. As one contemporary newspaper editorial observed, “the trouble for Labour is that the forces which triumphed under the New Right Revolution are still here. They are powerful forces – perhaps too powerful for any Third Way government to resist.” Both of the Government’s key economic advisory bodies - the Treasury and the RBNZ - continued to actively propagate a pro-neoliberal policy agenda during the period from 1999 to 2008. Simultaneously, they also continued to import and promote within New Zealand developments in the international intellectual economic orthodoxy. Business interests, meanwhile, vigorously opposed any perceived attempt by the FLG at rolling back the existing neoliberal policy framework whilst concurrently advocating for its further extension.

As Roper argues, Treasury policy advice during the period from 1999 to 2008 was primarily “directed towards persuading the Fifth Labour Government to retain all of the key elements of the neoliberal policy regime established from 1984 to 1999.” The essential features of the Treasury’s macroeconomic policy agenda are set out in numerous publications and policy papers, most notably their post-election briefing papers of 1999, 2002 and 2005. The 2005 briefing paper *Sustaining Growth*, for example, argues that “while New Zealand has a...
sound macroeconomic framework”, “future budgets must involve less…spending” and the “high marginal personal tax rates (33% and 39%) and the company tax rate” must be reduced. Respectively, the key discussion paper New Zealand Economic Growth: An Analysis of Performance and Policy, stated that: “the main roles for monetary policy” continue to be “to ensure the stability and efficiency of the financial system and to achieve low inflation.” Further, it upheld that “fiscal policy requires…balances over time”, with the “foundational principle” of the taxation system being a “broad based-low rate” for both personal and corporate tax rates. Put succinctly, then, “the central message of the working papers and the briefs is to retain and extend, rather than abandon, the monetarist macroeconomic strategy”, including a conservative fiscal strategy primarily aimed at reducing public debt and maintaining tight expenditure control.

Comprehensive coverage of the RBNZ’s continued endorsement and implementation of a monetarist macroeconomic strategy has already been provided indirectly in Chapter Five. What is perhaps not particularly evident from this account, however, is the degree to which the RBNZ continued to actively serve as a major conduit for the importation and promotion of the international neoliberal economic orthodoxy into New Zealand. The most prominent example in this regard is the previously discussed Independent Review of the Operation of Monetary Policy in New Zealand. While the FLG, RBNZ and non-executive directors were each documented in the preceding chapter as opposing many of the Svenssen Review’s recommendations, the overall assessment of the review nevertheless concluded that “monetary policy in New Zealand is currently entirely consistent with international best practice of

---

8 Ibid, 53.
9 Roper 2005b, 171.
flexible inflation targeting.” But, the Svenssen Review represented only one aspect of the RBNZ’s academic importation activities. As could be reasonably expected, myriad articles within the Reserve Bank of New Zealand Bulletin provide commentaries on the apparent relevance of various developments in the international economic literature to macroeconomic policy in New Zealand. Furthermore, the RBNZ also volunteered for New Zealand’s financial sector to undergo an assessment by the IMF in 2003.

Constituting a “strong continuity” of business political activism from the late 1970s through into the 2000s, business political activity in New Zealand from 1999 to 2008 involved intensive lobbying of the FLG to retain and extend the neoliberal policy framework constructed from 1984 to 1999. As Roper has documented, the initial political response of business to the election of the FLG was focused on “opposition to the incoming government’s policies.” Policies considered not to be ‘business friendly’, included “the increase in the marginal rate of income tax for those earning over $60,000”, the “introduction of the Employment Relations Act [ERA], the re-nationalisation of the ACC scheme, and the introduction of paid parental leave.” Such sentiments were expressed by all of New Zealand’s major business associations - the New Zealand Employer’s Federation (NZEF), Federated Farmers (FF), the New Zealand Manufacturer’s Federation (NZMF), and the New Zealand Business Roundtable (NZBR) - during the period from 1999 to 2001.

However, as outlined in the previous chapter, it was soon made clear to business that, beyond limited peripheral adjustments, the FLG remained fundamentally committed to retaining all of the key elements of the neoliberal policy regime. As Kelsey details, at a business forum held in October 2000 the

---

10 Archibald, 5.
14 Ibid.
FLG Prime Minister, Helen Clark, clearly indicated to those assembled that the FLG “intended to build on, rather than revisit, the neoliberal policy paradigm.”16 Thereafter, the focus of business political activism began shifting back towards the extension of neoliberal policy agenda.17 For example, NZBR Chairman Rob McLeod stated that: “to its credit”, the FLG “has not fundamentally reversed the post-1984 reforms – indeed its main legacy may be to have advanced a consensus around them.” 18 Nevertheless “economic progress doesn’t pause for breath, and nor should the economic reform process.”19

As Roper again documents, fiscal policy was “at the core” of the broader New Zealand business political agenda from circa 2001 through to the end of the FLG’s tenure in 2008. 20 In particular, business desired a substantial reduction in government expenditure and a parallel reduction of the higher personal and company tax rates.21 A number of media releases made by Business NZ (a new business association formed in 2001 through an amalgamation of the NZEF and NZMF), for example, espoused that there was a need to exercise “great discipline” and “tight control” over government expenditure. This was alongside calls for “effective policy solutions” involving “well designed tax reform.”22 Roper notes that such messages were “echoed in multiple submissions and publications” by Business NZ, Chambers of Commerce, FF, and the NZBR.23

In regard to the other major areas of macroeconomic policy - monetary policy and foreign exchange (FX) policy - business political activity was

---

17 Roper 2006, 177.
19 Ibid.
20 Roper 2005b, 177.
21 Ibid.
23 Roper 2006, 177.
comparatively muted from *circa* 2001 onwards. Indeed, as exemplified by the Business NZ discussion paper *Business NZ Recommendations: Response to the Financial Crisis*, to a significant extent it merely involved the voicing of support for the FLG’s retention of the existing monetarist regime. “The Finance and Expenditure Select Committee... confirms that New Zealand’s monetary policy framework is fundamentally sound and rules out the need for any changes to the [1989 Reserve Bank] Act or the conduct of monetary policy.”24 Similarly, the major Business NZ submission on the 2007 “inquiry into the future monetary policy framework”, *OCR: The Sharpest Tool in the Box?*, states that “the overall conclusion that [has] emerged is that the essential elements of New Zealand’s macroeconomic policy are still fundamentally sound.”25

As was discussed in more detail in Chapter Three, outside of Cabinet, the Treasury and the RBNZ comprise the most influential institutional bodies within New Zealand’s state apparatus. In addition, as was argued at length in Chapter One, business generally represents the most powerful set of society-based interests in contemporary liberal democratic states such as New Zealand. Therefore, the combination of the Treasury, the RBNZ, and the broader business community undoubtedly constituted a major array of pressures from within the domestic political economy for the FLG to not only retain, but to also continue to extend the neoliberal policy agenda during the period from 1999 to 2008.

However, it is evident that, simultaneously, there were significant countervailing influences being exerted on the FLG during the period from 1999 to 2008.26 These primarily derived from the combined economic and electoral contexts prevalent from 1999 to 2008.27 It has already been shown in the

---

26 Roper 2005b, 236.
27 Although it should be noted that other “countervailing influences” over the FLG were in operation during the period in question. In particular there is evidence that fractional divisions within capital
previous chapter that the FLG presided over a prolonged upswing in economic growth during its period of tenure.\textsuperscript{28} Real economic growth averaged 3.8\% between 1999 and 2007. As I have argued elsewhere, this served to significantly offset the inherent structural power that business possessed over the FLG due to New Zealand’s status as a specifically \textit{capitalist} nation state.\textsuperscript{29} The prolonged period of relatively strong economic growth effectively served to reduce the fiscal pressures being exerted on the state by domestic capital. As a consequence, the FLG was endowed with a significant degree of scope with which to endeavour to formulate policy to help sustain its position of power electorally.

Vowles \textit{et al} have documented that, at least initially, the FLG was electorally reliant on a predominantly working class voter base. Their statistics show, for example, that political support for the FLG was partly derived from a partial rebuilding of its traditional working class support base to close to its 1984 election level.\textsuperscript{30} Moreover, as Roper documents, the FLG also maintained relatively strong links with trade unions. While only three unions remained official affiliates of the wider New Zealand Labour Party (the “Engineering, Printing and Manufacturing Union; Service and Food Workers Union, and the Dairy Workers Union”), the New Zealand Council of Trade Unions (NZCTU) nevertheless remained listed as a “partner” of the FLG.\textsuperscript{31}

Thus, it is unsurprising that, especially in the realm of social expenditure, “the data reveals a clear political business cycle in which fiscal interests may have played some part in offsetting the influence of business over the FLG. See I. Fraser 2006, “Keeping Government Business Friendly? A Case Study of the Relationship between Business NZ and the Fifth Labour Government” (Unpublished BA Hons Dissertation, University of Otago).

\textsuperscript{28} In contrast to Roper, however, this should be seen as more than merely ‘cyclical’. A major factor contributing to New Zealand’s high economic growth rates during the mid-2000s was undoubtedly the excessively ‘loose’ US monetary policy stance maintained under the Bush administration. This generated a global asset bubble that boosted economic growth in the short-term, but also ultimately brought about the Global Financial Crisis (GFC) in 2007-2008.

\textsuperscript{29} See Richards 2007, 46.

\textsuperscript{30} J. Vowles \textit{et al} 2002, 92-93.

\textsuperscript{31} Roper 2005b, 236-7.
policy was strongly expansionary in election years.”  

Budget 2002, for example, introduced $1.0 billion of new spending and significantly expanded outlays over the following four years. Budget 2005, meanwhile, introduced $2.0 billion of new spending, largely focused on expansions of the flagship Working For Families (WFF) and the interest-free student loans schemes. Respectively, Budget 2008 committed $4.8 billion in new spending, and simultaneously delivered “a dividend of $10.6 billion to hard-working New Zealanders over the next four years” in the form of the previously documented 2008 personal tax cuts package.

This evidence suggests that the political influence of the powerful array of pro-neoliberal interests within the New Zealand political economy (principally composed of Treasury, the RBNZ, and business), was, at least to some extent, diminished during the period from 1999 to 2008, relative to the situation which prevailed from 1984 to 1999. The prevailing economic and electoral conditions effectively combined to offset the pressures being exerted on the FLG by its principal institutional economic advisors and the business community. This serves to raise a question of central importance to this thesis. If the political influence of this powerful grouping of pro-market forces was indeed diminished (as the above analysis suggests), why did the FLG nevertheless display such a steadfast commitment to the core features of the neoliberal macroeconomic policy regime? As will be argued throughout the remainder of this chapter, a key factor contributing to the FLG’s documented retention and entrenchment of the key neoliberal macroeconomic policies was New Zealand’s continued integration into the DWSR.

---

32 Dalziel 2004, 57.
35 Ibid 2008, “Executive Summary”, 4. I would suggest that it is likely that the FLG’s switch from increased social spending to personal tax cuts, to a significant extent, reflected an attempt to counteract a noticeable shift in electoral support to a resurgent National Party campaigning hard on a tax policy platform (amongst others) prior to the 2005 election.
6.2) The Dollar-Wall Street Regime’s Constraints on Macroeconomic Policy Formulation, 1999 to 2008

Continued integration into the DWSR placed considerable constraints on the macroeconomic policy formulation of the FLG.36 In essence, it created an economic environment requiring the adoption and maintenance of an overarching policy stance oriented towards the minimisation of “country specific macroeconomic fragility.”37 As outlined in Chapter Two, major IPFM-related crises (particularly, but not exclusively, in ‘emerging markets’) have become an inherent feature of the global financial system under the DWSR. Indeed, it is worth reiterating that since as late as 1994 Mexico (1994), Thailand, Indonesia, Korea (1997), Russia, Brazil (1998), Turkey (2000), Argentina (2000 and again in 2003), and more recently Iceland (2007 and again in 2008), Ireland (2008), Portugal, Greece (2010), Cyprus, and Spain (2012) have all undergone significant ordeals of this order. The FLG’s macroeconomic nexus was formulated, at least in part, in order to diminish New Zealand’s susceptibility to such crises.

A principle factor underpinning the FLG’s overarching macroeconomic policy stance was the existence of what the international economic orthodoxy refers to as the “impossible trinity.”38 Also sometimes known as the ‘trilemma’ of contemporary macroeconomic management, this concept contends that it is impossible for a government to simultaneously uphold “a fixed exchange rate, capital mobility, and a monetary policy dedicated to domestic goals.”39 As discussed in Chapter Two, following the establishment of the DWSR in the mid-1970s, international financial transactions associated with investment and securities (as opposed to those associated with financing international trade flows) grew rapidly. New Zealand was not excluded from this broader

---

36 Richards 2010, 36.
37 Bjorksten and Brook, 14.
39 Bjorksten and Brook, 14.
development. Indeed, as Rosborough has documented, by 2001 international trade in goods and services accounted for less than 2% of FX market turnover in New Zealand.\footnote{L. Rosborough 2001, “Trends in Foreign Exchange Trading”, Reserve Bank of New Zealand Bulletin, Vol. 64, no. 4, 19-35.} Munro delineates that “as foreign exchange market turnover has become dominated by financial transactions rather than those related to trade, the exchange rate has increasingly come to be viewed as an asset price.”\footnote{A. Munro, “What Drives the New Zealand Dollar?”, Reserve Bank of New Zealand Bulletin, Vol. 67, No.2 (July), 22.} As an asset price, in the absence of capital controls “the exchange rate responds to the market’s current expectation of a discounted sum of returns to holding assets denominated in New Zealand dollars relative to those denominated in other currencies.”\footnote{Ibid.} Consequently, \textit{ceterus paribus} “the expected relative return to holding New Zealand dollar” denominated assets should be zero; “there is no incentive for arbitrage”, and thus, “uncovered interest rate parity [UIP] is said to hold.”\footnote{Ibid, 23.} Because, in theory, under contemporary conditions of financial ‘globalisation’ UIP holds, “the domestic interest rate must equal the world interest rate.”\footnote{Held \textit{et al}, 228.} Therefore if, for example, a government seeks to maintain a pegged FX regime, national monetary authorities must respond to the experience of an ‘economic shock’ that shifts the ‘fundamentals’ underpinning the equilibrium value of the official FX rate by targeting “the domestic money supply” (by adjusting domestic interest rates) in order to “sustain exchange rate parity.”\footnote{S. Fischer 2001, “Exchange Rate Regimes: Is the Bipolar View Correct?” (Distinguished Lecture on Economics in Government), Journal of Economic Perspectives, Vol. 15, No. 2 (Spring), 11.} In this way, for countries with liberalised capital controls, an effective FX policy option trade-off exists. A pegged FX regime is practicable, but only at the cost of subsuming domestic monetary policy to IPFMs. Likewise, it is possible for governments to exercise significant autonomy in the sphere of
monetary policy, but only “provided they are prepared to accept the exchange rate consequences” via the simultaneous adoption of a floating FX regime.\textsuperscript{46}

The existence of this ‘impossible trinity’, did not rule out the possibility of occasional strategic FX market forays being undertaken by the RBNZ during the period from 1999 to 2008. Indeed, as outlined in the previous chapter, in 2004 the FLG specifically equipped the RBNZ with the capacity to undertake such measures (provided certain strict criteria were first met). It is also now “widely accepted” that the RBNZ exercised its intervention capacity on several occasions during mid-2007.\textsuperscript{47} The RBNZ first intervened on Monday, 11 June.\textsuperscript{48} Targeting the New Zealand dollar after it reached a (up until that point) post-float high of US76.40c, this constituted the first FX currency intervention since the Fourth Labour Government decided to float the dollar in 1985 (see Chapter Three).\textsuperscript{49} Fresh interventions soon followed: the RBNZ sold a net total of $702 million worth of New Zealand currency in foreign exchange markets in June 2007; an additional $1.5 billion in July; and, after a brief lull in August, a further $138 million in September.\textsuperscript{50}

Ultimately, however, the presence of the ‘impossible trinity’, coupled with contemporary global financial conditions primarily characterised by deep and highly integrated IPFMs, effectively rendered unsustainable the adoption of a fixed-rate or ‘pegged’ FX regime by the FLG.\textsuperscript{51} Centrally, this is because, as Fischer observes, it is likely that “sooner or later, an irreconcilable conflict” will arise between the FX and monetary policy goals of a country seeking to maintain a pegged FX regime.\textsuperscript{52} If a disequilibrium resulting from an economic shock is substantial and persistent, “either because policy was slow to react or

\begin{footnotesize}
\textsuperscript{46} Held \textit{et al}, 228.
\textsuperscript{47} M. Gordon, quoted in C. Niesche 2007, “Kiwi shock tactics don’t work this time”, \textit{New Zealand Herald}, 20 June.
\textsuperscript{48} RBNZ 2007, “Reserve Bank confirms forex intervention”, media release, 11 June.
\textsuperscript{50} \textit{New Zealand Herald} 2007, “Reserve Bank eases up on currency intervention”, 29 September.
\textsuperscript{51} Richards 2010, 38.
\textsuperscript{52} Fischer, 10. See also, Bjorksten and Brook, 21.
\end{footnotesize}
because the country has been hit by a strong and lasting shock”, the required monetary policy response may not be sustainable; abnormally high domestic interest rates would severely undermine the viability of both the domestic economy and banking system. 53 If the required domestic interest rate adjustment is not made, however, an effective currency overvaluation exists and, as Fischer observes, “under these circumstances, speculators can be expected to attack the currency.” 54 Such actions are likely to be successful in the current global financial environment. As Held et al point out, “since capital controls were dismantled…defences against speculative attack are very limited.” 55 “Speculators can mobilise massive funds through derivatives markets” and “institutional investors and [multi-national corporations (MNCs)]…tend to move out of a currency if they believe it to be under threat.” 56

In New Zealand’s specific case, the Bank of International Settlements (BIS) has documented that daily FX market turnover in New Zealand averaged $US12 billion in April 2007. 57 Further, average daily ‘Over the Counter’ (OTC) derivatives turnover constituted an additional $US3 billion. 58 When these historically unprecedented levels of financial flows are compared with the level of reserves available to the RBNZ for the management of crises (documented in Chapter Five), the significance of the divergence between the relative resources of IPFMs and the New Zealand state is stark. As outlined in the previous chapter, from February 2004 onwards, the RBNZ maintained minimum FX reserves of only $7 billion specifically earmarked for emergency crisis management. The expected outcome of any attempt to defend the New Zealand dollar at a fixed rate is thus obvious. As Harvey summarises the point, hedge funds can potentially arm themselves “with trillions of dollars of leveraged

53 Ibid, 11.
54 Ibid; Held et al, 231.
55 Held et al, 231.
56 Ibid.
57 BIS 2007, 9.
58 Ibid, 14.
money”, which means that any attempt at staging a fixed FX-rate defence is virtually impossible under the DWSR.⁵⁹

Consequently, as Bjorksten and Brook observe, during the period from 1999 to 2008 the view of the FLG and its key economic advisors (Treasury and the RBNZ) was that, in terms of the formulation of the FLG’s macroeconomic policy nexus, “pegging the exchange rate” was simply “not an option to consider seriously.” ⁶⁰ Instead, the existence of the impossible trinity necessitated that the FLG retained New Zealand’s floating FX regime in order to maintain economic viability. In contrast to a pegged regime, in principle an independently floating regime can act as an effective “buffer against shocks to the current account” such as those that would be constituted by a transmutation of the underlying fundamentals of the value of the nominal exchange rate.⁶¹ Under a floating regime “the exchange rate moves to offset any difference between world and domestic interest rates”, effectively leaving monetary policy to be deployed discretely for the purpose of maintaining domestic economic stability.⁶²

However, just as major problems existed with attempting to maintain a pegged FX regime under the DWSR, so too has a significant problem emerged with the adoption of the trade-off floating FX option required under conditions of liberalised capital controls.⁶³ Principally, since the establishment of the DWSR and the parallel expansion of financial transactions in IPFMs, unexpected global FX market volatility has increased dramatically.⁶⁴ New Zealand’s experience has been no exception to this broader global trend. Munro’s (2004) correlation of recent RBNZ empirical work documents the key factors acting to determine

⁵⁹ Harvey 2003a, 72.
⁶⁰ Bjorksten and Brook, 21.
⁶¹ Held et al, 16, 21.
⁶² Held et al, 228.
the nominal FX rate of the New Zealand dollar. She identifies “factors that affect relative returns – short-term interest rates, commodity prices”, and “a notion of medium-term exchange rate equilibrium” as being very important in helping to “explain exchange rate movements.” However, Munro also observes of these factors that, whilst very important, they simply “do not explain all, or even most of, short-term exchange rate movements.” Some large currency fluctuations are clear market over-reactions disconnected from underlying economic determinants.

In other words, even after taking into account the explanatory power of the fundamental nominal FX rate determinants, during the period from 1999 to 2008, significant amplitude in the New Zealand FX rate persisted. The International Monetary Fund (IMF) notes, for example, that prior to 2006, despite an “uncomfortably large current account deficit”, the New Zealand dollar remained overvalued for an extended period and appeared “to have decoupled from the traditional fundamental determinants of the currency’s value” (see Figure 6.1). Following this, in the first quarter of 2006, the New Zealand dollar underwent a large depreciation of around 10%. The currency subsequently bounced back, but the onset of the GFC in late 2007 saw the currency once more take a large dive. As Cassino and Wallis observed, “the NZD fell, on a trade-weighted basis, by 35 percent over the period from 2007 to early 2009 during the peak of the crisis.” It is important to note that the movements of the New Zealand dollar during the GFC, what was undoubtedly

65 Munro.
66 Ibid, 32.
67 Ibid.
68 Bjorksten and Brook, 16.
69 Bjorksten and Brook, 20. See also Munro, 21.
71 This significant unsubstantiated FX market volatility also persisted under the subsequent Fifth National Government (FNG). The New Zealand dollar appreciated significantly (by around 50%), with the IMF subsequently considering the currency to be overvalued by around 10-25% in early 2010. See IMF 2010, New Zealand – 2010 Article IV Consultation Preliminary Concluding Statement of the IMF Mission (Washington: IMF).
“one of the most volatile periods in the history of financial markets”, were again not driven by domestic determinants.\textsuperscript{73} Instead, the RBNZ’s “in-house empirical model of the exchange rate” shows that “to a large extent, the NZD’s moves against other major currencies [were] driven substantially by the moves in fundamentals of the other economy or by shifts in risk appetite” in IPFMS.\textsuperscript{74}

Such an empirical reality constitutes a significant divergence from a logical expectation of outcomes if UIP did indeed hold as predicted by economic theory. Stiglitz details that, as a consequence, within the international economic orthodoxy the “notion that markets are rational has been called into question.”\textsuperscript{75} Instead, he states, it is now commonly upheld that “markets may suffer from irrational exuberance as well as irrational pessimism, and the swings between the two can be rapid.”\textsuperscript{76} As Rude points out, these dynamics are essentially an expression of “an increase in the tendency for the financial markets to over-and-under-estimate future profits.”\textsuperscript{77}

\textsuperscript{73} Ibid.
\textsuperscript{74} Ibid, 21.
\textsuperscript{76} Ibid.
The systemic escalation of FX market volatility represented a major problem for the FLG’s formulation of its core macroeconomic policy nexus – monetary policy, FX policy, and fiscal policy. Primarily, this is because of its serious potential consequences for domestic economic stability. Unduly large appreciations of the exchange rate will clearly undermine the profitability of the export sector by reducing the competitiveness of their products on the international market. Conversely, as Stiglitz argues, if firms and financial institutions have uncovered balance sheet positions, large sudden depreciations in the FX rate will undermine “normal trade adjustment” (that is, an increase in export activity and a parallel decrease in import activity) by imposing

---

78 Richards 2010, 41.
79 However, fear of adverse market reactions also influenced some of the FLG’s other policy choices, especially in its first two terms. Political ‘acrimony’ “regarding the effects of...a sharp drop in business and investor confidence” is cited as a major factor in scaling back proposed pro-labour changes to industrial relations legislation. See IMF 2000, IMF Staff Country Report No. 00/140: New Zealand: Selected Issues (Washington: IMF).
80 Empirical research has found that, in New Zealand, FX rate volatility does not generally impact heavily on export volumes, rather only on export earnings. This is due to New Zealand export firms generally being ‘price takers’ on the international market, characterised by little price elasticity of supply. See IMF 2005, IMF Staff Country Report No. 05/153: New Zealand Selected Issues (Washington: IMF), 18.
destabilising capital outflows and higher domestic interest rates. Thus, significant unpredicted swings in the exchange rate either way could result in serious economic contractions deriving from “corporate distress.” Furthermore, as Bjorksten and Brook observe, “the more important external trade is to an economy”, the greater the likely impact of such developments. Thus, in New Zealand’s case - as with other “relatively small, open, developed economies” such as “Iceland, Norway, Australia and Canada” - “with a moderately large tradables sector” the potential costs are comparatively high in the context of the global economy.

Thus, the FLG’s retention of New Zealand’s floating FX regime, itself, effectively generated significant ancillary pressures on the scope for government autonomy in the sphere of macroeconomic policy formulation. Centrally, the FLG faced pressure from IPFMs to adopt policies to mitigate the substantial threat to the domestic macroeconomy posed by destabilising international financial flows. In more specific terms, rather than being endowed with a significant degree of policy autonomy (as suggested by the underlying principle of the impossible trinity), during the period from 1999 to 2008, the FLG faced significant pressure from IPFMs to adhere to the neoliberal rules of the international monetary system. Due to the fact that the FX rate now effectively constitutes an asset value, inflation amounts to a key determining factor.

---

81 J. Stiglitz 2001, “Monetary and Exchange Rate Policy in Small Open Economies: The Case of Iceland”, *Central Bank of Iceland Working Papers*, No. 15 (November), 1, 4. It should be noted that there is a body of literature that upholds that the market only provides firms with limited means of covering FX positions. Indeed this empirical reality has been cited as a key factor contributing to the seriousness of the 1997-8 East Asian crisis.


83 Bjorksten and Brook, 20.

84 Ibid.

85 Richards 2010, 41.

86 As numerous authors have observed, such pressure has been experienced by most governments throughout the developed world. This is reflected in the well documented phenomenon of significant convergence towards similar overarching macroeconomic policy stances seeking to dampen malign financial transactions. See, for example, Held et al, 229; L. Mosely 2007, “The Political Economy of Globalisation”, in D. Held and A. McGrew (eds.), *Globalisation Theory* (Cambridge: Polity Press), 106-125; M. Webb 1995, *The Political Economy of Policy Co-ordination: International Adjustment since 1945* (Ithaca: Cornell University Press), ch.6.
factor of the risk *premia* attached to the New Zealand dollar by IPFMs. Consequently, the FLG retained and entrenched the incumbent ‘monetarist’ approach to monetary policy focused primarily on the achievement and maintenance of a stable low rate of inflation. As Held *et al* observe, integral to this was also the establishment and maintenance of the “credibility of domestic monetary authorities” to be able to successfully operate such a stance. Therefore, the FLG also preserved the RBNZ’s operational and constitutional autonomy within the state apparatus, while, as Munro observes, the RBNZ respectively promoted “a clear objective for monetary policy, a published model and regular OCR review dates.”

However, it is important to note that while exerting pressure on the FLG to retain a broadly monetarist approach to monetary policy, the DWSR simultaneously undermined the effectiveness of many “traditional instruments” of New Zealand’s domestic monetary policy. First, as Held *et al* delineate, the extensive domestic financial sector deregulation, the unprecedented international mobility of capital, and the high levels of financial innovation that have accompanied DWSR integration, effectively acted to subvert the RBNZ’s capacity to autonomously determine the domestic money supply and price level. Indeed, as was noted in Chapter Five, the RBNZ no longer even attempted to specifically target the domestic monetary supply. Second, as was also seen in Chapter Five, while the RBNZ could still wield some effective control over short-term interest rates operating under the *aegis* of the OCR system, determination of longer-term interest rates was effectively surrendered to IPFMs.

---

87 As upheld by the Purchasing Power Parity (PPP) model of the long-term equilibrium FX rate. See Munro, 25.
88 Held *et al*, 229.
89 Munro, 22.
90 Held *et al*, 229.
91 ibid.
New Zealand’s integration into the DWSR also placed significant constraints on the FLG in the realm of fiscal policy formulation.\(^92\) Most notably, DWSR integration exerted considerable pressure on the FLG to retire its underlying debt position. Held \textit{et al} observe that, in theory, one of the key advantages of liberalised capital controls is that international borrowing by a government should tend to put less upward pressure on domestic interest rates.\(^93\) As noted earlier, the resulting shift in the country’s current account position should be offset by a parallel adjustment of the FX rate. However, IPFMs are not just concerned with parity in relative returns, they are also interested in the likelihood of default. As a result, IPFMs “tend to impose a risk premium on borrowing countries.”\(^94\) Governments perceived to have weak debt positions may end up facing IPFMs seeking to reduce their exposure to perceived risk, resulting in both rising domestic interest rates in concert with a falling FX rate.\(^95\) It is at least partially for this reason that during the period from 1999 to 2008, the FLG placed the retirement of gross debt as a percentage of GDP as a major pillar of its overarching fiscal strategy. Indeed, the work of Faruqee implies that the long-run sustainability of New Zealand’s FX rate required a substantial reduction of foreign-held financial claims/assets.\(^96\) In essence, then, the FLG can be interpreted as seeking to be perceived as “responsible economic managers.”\(^97\) After “having scared the markets in the year 2000 in their first year of office” (see Chapter Five), the FLG was endeavouring to be seen as making a credible move towards achieving a more

\(^{92}\) Richards 2010, 42.  
^{93}\) Held \textit{et al}, 229.  
^{94}\) Ibid.  
^{95}\) Ibid.  
^{97}\) M. Reddell 2009, Interview with the Author. Friday, 27 November.
structurally sound current account position aimed at dampening the impact of FX volatility deriving from public debt.98

However, it should also be noted that, for the same fundamental reasons, New Zealand’s integration into the DWSR also exerted considerable influence over the FLG’s approach to expenditure.99 In particular, due to the constraint posed by volatile IPFMs over the current account, the FLG would have experienced mounting difficulty if attempting to adopt and implement any substantive new social democratic policy measures.100 Centrally, this is because, as Brawley observes, “states implementing social democratic...policies tend to have higher interest rates, and therefore have to pay more to carry their public debt.”101 Furthermore, in a similar manner to monetary policy (as discussed above), the FLG also had to be mindful of the potential inflationary effects of its expenditure.102

Thus, while it may be observed that government expenditure expanded under the FLG (see Table 5.4), it is important to recognise that New Zealand’s integration into the DWSR was simultaneously exerting downward pressure on the scope of this new expenditure.103 Perhaps most illuminating in this regard is the fact that, as documented in the previous chapter, despite overseeing the largest economic upswing in New Zealand since the end of the post-war ‘long boom’ (and, corresponding with this a veritable mushrooming of government revenues), FLG Finance Minister Michael Cullen constantly reiterated the need for a ‘cautious approach’ to fiscal policy in his annual budgets and fiscal

98 Ibid. It is important to note, however, that, despite the FLG’s successful programme of public debt reduction, a significant threat to New Zealand’s macroeconomic stability persisted. This took the form of significant and growing private sector debt. See IMF 2003. IMF Staff Country Report No. 03/122: New Zealand: Selected Issues (Washington: IMF); IMF 2005; 2007.

99 Held et al, 229.

100 Ibid, 230.


102 Ibid, 113.

103 Richards 2010, 43.
strategy reports.\textsuperscript{104} The vast increase in government revenues undoubtedly freed the FLG’s scope for increased government spending, especially from 2005 onwards. \textsuperscript{105} However, it is apparent that despite this, an underlying commitment to fiscal conservatism remained and at least partly derived from consideration of potential market reactions. As Michael Reddell (then a RBNZ official on secondment to the Treasury) observes, reflection on “the reaction to 2000” when the FLG’s proposed new policies brought about extremely negative reactions from both domestic business and IPFMs was one of “the factors of most importance to the Government’s approach to macro management.”\textsuperscript{106}
6.3) Explaining the Constraints: The Political Implications of Financial Market Liberalisation in New Zealand

It is perhaps worth highlighting from the outset that, in terms of an explanatory account, the influence of the DWSR does not, of course, explain everything in relation to the FLG’s formulation of macroeconomic policy. Other factors, such as: the major economic upswing from 1999 to 2007; continued business opposition to any substantive retrenchment of the neoliberal policy regime; the specific composition of parties making up the FLG in its various forms; and the specific prevailing electoral and domestic political conditions, also played significant roles in shaping the FLG’s macroeconomic policy decisions. As the evidence assembled above reveals, however, during the period from 1999 to 2008, New Zealand’s ongoing exposure to the increasingly deep and mobile IPFMs of the DWSR nevertheless constituted an important (yet often neglected) external variable that had a significant disciplinary effect on the macroeconomic policy formulation of the FLG. This IPFM-derived discipline ultimately served to enforce an ongoing commitment to all of the core pillars of the existing neoliberal macroeconomic policy framework.

Centrally, as Rude observes, New Zealand’s integration into the DWSR, via the maintenance of extensive financial market liberalisation, supported the existence of an economic environment in New Zealand where “recurrent financial crises set the pace and rhythm of economic activity.” Corresponding with the argument made in the previous section,

financial crises occur because imbalances build up between the financial system and the underlying macroeconomy – imbalances between stocks of financial assets and liabilities, on the one hand, and flows of national income, on the other – and they occur when

\begin{itemize}
\item Roper 2005b, 222.
\item Richards 2010, 43-44.
\end{itemize}
these macroeconomic financial stock/income flow imbalances become unsustainable.\textsuperscript{110}

The tendency for such macroeconomic imbalances to develop has increased significantly under the DWSR. The various financial instruments that constitute the global financial system exist “as discounted future expected profit streams”, and the increasingly deep and mobile nature of IPFMs has increased the propensity for both over and underestimation of the future profits to be derived from these streams.\textsuperscript{111} The result of this is the repeated substantial misallocation of capital by IPFMs, the rectification of which usually involves a sudden radical evolution in a country’s financial stock/income flow balance which has the distinct potential to destabilise “the underlying macroeconomy.”\textsuperscript{112}

The FLG’s retention of all of the key features of the incumbent neoliberal macroeconomic policy regime – a monetarist approach to macroeconomic management, an independently floating FX regime, and a commitment to fiscal conservatism – was formulated, at least in part, in response to this endemic instability and potential for crisis.\textsuperscript{113} As Held \textit{et al} argue, this is because the global financial conditions prevalent under the DWSR have fundamentally “altered the costs and benefits associated with different national macroeconomic policy options, at times so radically as to make some options prohibitively expensive.”\textsuperscript{114} In particular, because the government may have eventually faced “rising interest rates and a falling exchange rate as markets reduced their exposure to what they perceived as ‘high risk borrowers’”, integration into the DWSR has significantly raised the potential costs of adopting expansionary monetary and/or fiscal policy stances (including maintaining an overly large public debt position) in New Zealand. This means

\begin{itemize}
\item \textsuperscript{110} Ibid 2008, 200.
\item \textsuperscript{111} Ibid. For an account of New Zealand’s specific case see Bjorksten and Brook.
\item \textsuperscript{112} Rude 2008, 200, 208.
\item \textsuperscript{113} Richards 2010, 45.
\item \textsuperscript{114} Held \textit{et al}, 228.
\end{itemize}
that in the realm of social policy, for example, there was significant pressure on the FLG to curtail government expenditure in key areas such as health, education, and social welfare. Prime evidence of such pressures being exerted on the FLG can be found in the formulation of Budget 2004. Here the scope of the newly announced WFF package was officially restricted due to the probable interest rate increases that (marginally) higher levels of gross government borrowing would induce.\textsuperscript{115} As Finance Minister Michael Cullen observed in his 2004 budget speech, because “the gross sovereign-issued debt to GDP ratio will decline more slowly”, “there is very little room...for any further substantial fiscal loosening.”\textsuperscript{116} Any additional “loosening – whether by way of tax cuts or by way of expenditure increases – would place significant pressure on monetary policy with the likelihood of higher interest rates.”\textsuperscript{117} Further evidence of such pressures being exerted on the FLG can be found in the formulation of Budget 2006. The 2006 \textit{Fiscal Strategy Report} states that “spending more than currently projected or reducing taxes would lead to an increase in gross debt and put further pressure on monetary policy.”\textsuperscript{118}

Moreover, due to the valuable ‘dampening’ effects that may be gained from the reduction of risk premia attached to New Zealand dollar-denominated financial assets, contemporary financial conditions also expanded the expected macroeconomic benefits to be gained by the FLG from retaining the fiscal and monetary policy elements of the existing neoliberal macroeconomic policy regime.\textsuperscript{119} This meant that in the realm of monetary policy there was significant pressure to continue to closely adhere to the incumbent monetarist approach with its singular focus on achieving and maintaining a stable low level of domestic inflation. Additionally, in the realm of taxation policy, it meant that there was pressure on the FLG to look to reduce corporate tax rates. Reducing

\textsuperscript{116} Ibid.
\textsuperscript{117} Ibid.
\textsuperscript{119} Richards 2010, 45.
corporate taxes serves to increase business profitability and, thus, strengthens the underlying macroeconomy.

Thus, continued integration into the DWSR during the period from 1999 to 2008, imposed significant external constraints on the FLG’s “regime of financial autonomy.” The state’s capacity to autonomously “determine and implement its own independently formulated macroeconomic strategy” was, in effect, severely curtailed. Rather than reflecting the preferences of the democratic plurality to whom the state was nominally accountable, it is apparent that the “real underlying momentum” of the FLG’s macroeconomic policy formulation was consideration of the “discipline” imposed by the vagaries of inherently volatile IPFMs.

Yet, as Panitch and Gindin observe, while the serious crises that served to discipline the FLG’s macroeconomic policy formulation are seemingly inherent to the global financial system under the DWSR, “the relative containment of these crises in terms of their depth, duration and tendency to spread has been remarkable.” The analysis of Panitch and Gindin suggests that, in New Zealand’s specific case, we should look at the state action of the FLG as having played the vanguard role in increasing the capacity of New Zealand’s national financial system to withstand recurrent shocks. In effect, while it was subject to ruthless discipline deriving from the operation of IPFMs, it is evident that the FLG simultaneously played a key role in “regulating, but not eliminating, the turmoil” that New Zealand’s financial system is subjected to under the hegemony of the DWSR.

The basis of the FLG’s attempts to manage the systemic financial turmoil of the DWSR was “the institutional learning and development that has occurred over time” within the RBNZ and Treasury “in cooperation with international...”

---

120 Held et al, 229.
121 Ibid.
institutions such as the BIS, the IMF and the World Bank.”  

As Rude documents, following the 1997 Asian financial meltdown and 1998 Long Term Capital Management (LTCM) crisis, this body of learning would have been largely guided by the standards of what has come to be termed the “New International Financial Architecture” (NIFA).  

While the core features of the NIFA had been established by the early 1990s, the NIFA “took its final form in a New BIS Capital Accord” – popularly referred to as ‘Basel II’ - signed in 2004. 

Essentially, following the guidance provided by the NIFA, the FLG ensured the “prudential supervision and regulation” of the national banking and financial system and, if necessary, the provision of addition support via a properly timed relaxation of monetary conditions. This served to maintain a “robust and resilient” national “banking and financial system” better “able…to survive and function in a financial crisis.”

During the period from 1999 to 2008, then, the DWSR disciplined the FLG, in-effect constraining the scope for the independent formulation of public macroeconomic policy and undermining the democratic aspects of New Zealand’s liberal democratic political system. It did this through a particularly potent form of “economic intimidation” that ultimately necessitated the retention of the core features of the existing neoliberal macroeconomic policy nexus. While it was being disciplined by the vagaries of IPFM s, however, the FLG simultaneously provided a rigorous regulatory and supervisory framework in support of the national banking and financial systems aimed at ameliorating a system-wide collapse. In view of this, what is the ultimate contribution of Gowan’s Dollar-Wall Street Regime analysis to a sophisticated neopluralist theoretical model of New Zealand’s liberal democratic state?  

---

123 ibid, 40.  
124 Rude 2008, 199.  
125 The 2004 Basel II capital accord was superseded in 2010 by ‘Basel III’.  
126 Rude 2008, 199, 206.  
127 ibid, 216.  
128 ibid, 220.  
129 ibid, 220.
Of most importance in answering this question is the demonstration that a major shift in the structural relationship between the New Zealand state and globally-mobile international private financial capital has taken place. The economic interests of the state and IPFMs appear to have become much more closely intertwined under the DWSR. This has resulted in a discernable refinement of the structural constraint being exerted on the state. As argued in Chapter One, due to the fact that the contemporary liberal democratic state is fiscally reliant on the taxation of incomes generated by private capitalist enterprise, the state faces an implied pressure to formulate public policy in a manner that ensures the maintenance of conditions viable to the pursuit of profitable accumulation. To reiterate my previous argument, the state’s condition of fiscal dependence effectively forms a structural constraint on state neutrality by forcing policy-making officials to undertake an anticipatory consideration of the interests of business. Following integration into the DWSR, however, malign international flows have been shown to pose a constant threat to domestic economic viability regardless of whether or not business conditions are otherwise profitable. This is most pertinently demonstrated by the devastating experience undergone by Korea, Indonesia and Thailand at the hands of private hedge funds operating out of the advanced capitalist world’s major IPFMs during the 1997-1998 East Asian financial melt-down. Harvey has documented that otherwise profitable concerns were driven into bankruptcy after being deprived of sufficient credit following the massive speculative attacks carried out on their national currencies. As a consequence, there is now strong and constant economic and financial pressure for governments integrated into the DWSR to formulate their public macroeconomic policy frameworks in the interests of IPFMs, regardless of domestic economic conditions. States are now essentially “competing to provide macro- and micro-

130 Richards 2010, 46.
132 Harvey 2003a, 78.
economic, regulatory, and broader political frameworks” desired by IPFMs in order to induce the international financial flows necessary to ensure the integrity of their independently floating FX regime and underlying macroeconomy.133

Within the field of critical international political economy, this perceptible alteration of the structural relationship between capital and the modern liberal democratic state has generated a significant amount of scholarly debate. In particular, it has been interpreted by many as heralding a “decline of the nation state.”134 But, as Wood convincingly demonstrates in her widely praised work Empire of Capital, the establishment of the DWSR has not “made the national state increasingly irrelevant.”135 Instead, the evidence suggests that the reality is to the contrary; it is apparent that the state continues to play an “indispensable” role in the operation of the global system under the hegemony of the DWSR.136 Centrally, during the period from 1999 to 2008, it was the state that provided the necessary “extra-economic help” required by the DWSR to sustain the “imposition” of IPFM-derived discipline on New Zealand in order to keep the country “vulnerable to economic manipulation” by IPFMs.137 The FLG worked to ensure a certain level of “stability and predictability” in the complex national financial system “by supplying an elaborate legal and institutional framework” based around the principles of the NIFA, that was ultimately “backed up by coercive force.”138 As Wood points out: “no other institution, no transnational agency, has even begun to replace the nation state” as such “an administrative and coercive guarantor” of the financial order, stability and predictability required by contemporary IPFMs in their day-to-day

---

134 Harman, 40-41. Held et al refer to this perspective as the ‘hyperglobalisation’ paradigm.
137 Ibid, 21.
138 Ibid, 17.
Instead, she continues, “in the final analysis” the reality is that “it is...the state that has created the conditions enabling IPFMs to survive” their own inherent volatility, “and to navigate the world” by providing and maintaining the ‘circuits’ of the global financial system.\textsuperscript{140}

The financial discipline imposed by IPFMs has certainly reduced the overall flexibility of the state in the sphere of its macroeconomic policy formulation. As argued in the previous section, for example, the FLG was required to retain all of the core features of the neoliberal macroeconomic policy nexus during the period from 1999 to 2008 in order to maintain macroeconomic stability. But, in contrast to the perspective of the so-called ‘hyperglobalisers’, the inherent volatility of the global financial system under the DWSR has simultaneously served to increase the necessity for the New Zealand state to play its traditional functions. Fundamentally, IPFMs still require the “regularity, predictability, and legal order” provided by the state to help reduce the likelihood of a system-wide collapse.\textsuperscript{141}

Furthermore, as Wood observes, it is important to note that the system is fundamentally hierarchical; the DWSR operates through a system of nation-states “structured in a complex relation of domination and subordination.”\textsuperscript{142} In essence, what this means is that the degree to which a state’s operational autonomy is constrained under the DWSR is, to a significant extent, contingent on its position within the global political-economic hierarchy.\textsuperscript{143} The most important general dichotomy is between the states of the advanced capitalist world and those of the developing economies, but the states of the advanced capitalist world are also ordered hierarchically. At the top, of course, is the US, along with Japan and the Euro area, while the smaller advanced capitalist economies “outside of the [euro zone], such as New Zealand, Iceland, Norway,
Australia and Canada” are relegated to lower positions in the advanced capitalist hierarchy.144 As Bjorksten and Brook outline, this is primarily because the “unsubstantiated” FX swings intrinsic to the global financial system are substantially more disruptive to relatively small open economies with a reliance on foreign trade and high levels of foreign debt. 145 “Corresponding fluctuations” are documented as having a substantially reduced impact on the larger advanced capitalist economies.146

Thus, in contrast to the perspective of so-called ‘hyperglobalisers’, the power and operational autonomy of the New Zealand state is not simply “fading away” as a result of financial market liberalisation.147 Indeed, as Held et al argue, such metaphors as “the loss, diminution or erosion of state power” can wholly misrepresent the true underlying nature of the transformation of the conditions of state power.148 Instead, the distinctive transformation of the conditions of state power in New Zealand should be conceived of as constituting a reproduction and refinement of conditions of international economic domination within the domestic political economy.149 The central political implication of this has been a growing trend towards an ‘internationalisation’ of the state. Following the analysis of Panitch and Gindin, during the period from 1999 to 2008, “the nature of [New Zealand’s] integration into the global economy tended to tie the successful reproduction of [it’s] own social formations [i.e. the profitability of domestically-operating business] to the rules and structures of the American-led global order.”150 As a consequence of this (above discussed) disciplinary action, the FLG essentially “took responsibility for creating the necessary internal conditions for sustained

---

144 Bjorksten and Brook, 15.
145 Ibid, 19.
146 Ibid, 20.
147 Panitch and Gindin 2003, 20.
148 Held et al, 440.
international accumulation [in New Zealand], such as stable prices...and no restrictions on capital outflows.” 151 Thus, paralleling Poulantzas’ observations made in the early 1970s, the tendency that appears to have emerged in relation to the operation of state power in New Zealand post-DWSR integration, is an ‘internalised transformation’ “of the national state itself, aimed at taking charge of the internationalisation of public functions on [international financial] capital’s behalf.” 152

In other words, what is evident is that the state has actually effectively added to its responsibilities; it is no longer simply concerned with maintaining profitable business conditions for domestic capital, DWSR integration has also effectively made it responsible for maintaining an overarching macroeconomic framework (including the national financial regulatory and supervisory architecture) sufficient for profitable accumulation to be undertaken by highly mobile foreign financial capital. 153 This is not to say, of course, that this transformation was/is in any way inevitable or permanent. As Panitch points out, such a perspective would establish “a false counterposition between globalising capital and the power of states” by inferring a degree of economic determinism that cannot be empirically substantiated. 154 There is, after all, “nothing in the economic logic of accumulation” that “requires that ideological and political struggles must subsume other institutional orders and their logics under the principle of capital accumulation.” 155 Instead, as Cox emphasises, it is to say that this major transformation of the conditions of state power is still a fundamentally historically contingent phenomena; we must always remember that “in order to comprehend the real historical world it is necessary to consider

151 ibid. See also Harman, 2003, 42.
155 Jessop 1997, 566.
distinctive forms of state... [and] the characteristics of their historical blocs, i.e., the configuration of social forces upon which state power ultimately rests.”

Conclusion

During the period from 1999 to 2008, the main constraints on the FLG’s macroeconomic policy formulation derived from the same powerful set of constraints that drove New Zealand’s initial neoliberalisation. Both of the Government’s key institutional advisors, the Treasury and the RBNZ, as well as all of the country’s major business interests continued to propagate the retention of all of the key features of the incumbent neoliberal macroeconomic policy nexus. Electoral and economic conditions appear to have enabled the exertion of significant countervailing influences over the FLG’s broader program of public policy formulation, however New Zealand’s integration into the DWSR created an economic environment that ultimately necessitated the retention of all of the features of neoliberal macroeconomic policy agenda.

Underpinning this was the existence of what is known within the international economic orthodoxy as the ‘impossible trinity’. The impossible trinity necessitated that the FLG remain fundamentally committed to the existing independently floating FX regime. This was because its market-based adjustment serves to cushion the domestic economy from the impact of shocks on the nation’s current account. But a further crucial factor constraining the macroeconomic policy formulation of the FLG was the persistence of significant, unsubstantiated amplitude in IPFMs. The inherent volatility of contemporary IPFMs posed a serious, persistent threat to domestic macroeconomic stability. This effectively served to discipline the FLG in the sphere of its macroeconomic policy formulation. The FLG faced significant implied pressure from IPFMs to retain each of the other core features of the existing neoliberal macroeconomic policy framework – a monetarist approach to macroeconomic management and a conservative or ‘prudent’ approach to fiscal policy - so as to mitigate the potential impact of destabilising international financial flows.
Consequently, it appears that New Zealand’s continued integration into the DWSR during the period from 1999 to 2008 fundamentally acted to constrict the FLG’s scope for autonomous action in the realm of public finance. Centrally, this suggests that the major political implication of financial market liberalisation in New Zealand has been a major shift in the underlying structural relationship between the New Zealand state and globally-mobile international financial capital. The structural constraints exerted on the state by capital have been refined. There is now a strong and constant implied pressure on the DWSR-integrated state to adopt and implement all of the core features of the neoliberal macroeconomic policy regime in order to ensure the maintenance of national economic viability.

However, as numerous authors have observed, “the distinctive attributes” of the underlying structural shift that DWSR integration has entailed “by no means simply prefigure the demise of the nation-state or even the erosion of state power.” Rather, the state remains critical to the maintenance of the DWSR by providing the necessary ‘extra-economic’ power required by IPFMs, and, furthermore, the vulnerability of the state to IPFM-derived discipline is largely contingent on its position within the global political-economic hierarchy. Thus, the apparent shift in the structural relationship between state and capital only constitutes a refinement of the current conditions of economic domination in New Zealand. While the state’s operational autonomy can be severely curtailed by IPFM-derived discipline, this outcome is still historically contingent; the state remains the ultimate site of political power within New Zealand.

---

157 Held et al, 436.
The Global Financial Crisis and the Fifth National Government, 2008 to 2011

Introduction

The previous chapter examined the constraints on the macroeconomic policy formulation of the Fifth Labour Government (FLG) during the period from 1999 to 2008. It emphasised that, despite the existence of significant countervailing influences that endowed the government with a significant degree of flexibility in relation to the formulation of its broader public policy agenda, New Zealand’s integration into the Dollar-Wall Street Regime (DWSR) nevertheless imposed significant constraints on the FLG’s capacity to autonomously formulate and implement macroeconomic policy. Continued integration into the largely privately-operated and US-dominated global financial system ultimately required the FLG to retain and entrench all of the key features of the neoliberal macroeconomic policy nexus.

This chapter will seek to exemplify and corroborate the overall importance and explanatory power of this DWSR-based analysis for our understanding of the operation of the New Zealand state during the neoliberal-era. The account will focus on the significant degree of influence that international private financial markets (IPFMs) were able to exert over the formulation of the Fifth National Government’s (FNG) macroeconomic policy response to the Global Financial Crisis (GFC) during the period from 2008 to 2011. The discussion will begin with a detailed descriptive overview of the onset and subsequent evolution of the GFC during the period from mid-2006 to
late 2008. A brief account of the political circumstances that prevailed in New Zealand during the period from 2008 to 2011 will follow. The discussion will then move on to provide a more detailed account of the main features of the macroeconomic policy strategy pursued by the FNG during its first term in power. In the final section, the influential role played by IPFMs in determining the overall shape and scope of the FNG’s macroeconomic policy response to the GFC will be examined. Centrally, it will posited that due to the threat of a severe negative reaction from IPFMs, the FNG’s capacity to autonomously articulate a macroeconomic policy strategy was significantly constrained during the period from 2008 to 2011.
7.1) **The Global Financial Crisis**

In 2007, the world entered into what has come to be known as the global financial crisis. IPFM liquidity collapsed precipitously as vast swathes of participants endeavored to exit asset markets as swiftly as possible. The immediate trigger of the crisis was a mounting wave of defaults in the now infamous US ‘subprime’ mortgage market beginning in late 2006 and early 2007. Initially confined to a few states in the mid-west (Michigan and Ohio especially), the wave of defaults quickly spread to states in the south and west. Florida, California, Arizona, and Nevada were particularly hard hit.

Ultimately, the rapid spread of subprime mortgage defaults instigated the collapse or near collapse of a number of major US mortgage brokers in February and March 2007. Included amongst the ranks of these stressed institutions were the highly publicised New Century Financial, as well as other less well known, but nevertheless important lenders such as Ameriquest Mortgage, Fremont General, Ownit, ResMAE, and the General Motors subsidiary Residential Capital (which required a $1 billion bailout from its parent). As Blackburn observes, however, “the true scope of the problem only began to register in the late [northern] summer.” At this point, around July 2007, a significant number of leading financial institutions in both the US and Europe began to be seriously hit by faltering values for ‘residential mortgage-backed securities’ (MBSs).

The first major bank to report a problem was Wall Street investment bank Bear Stearns, the most active underwriter of MBSs. In July, two large hedge funds sponsored by Bear – the ‘High Grade Structured Credit Enhanced

---

3. Blackburn, 64.
5. Blackburn, 64.
6. Ibid, 63.
Leverage Fund’ and the ‘High-Grade Structured Credit Fund’ - got into serious trouble when they attempted to liquidate their substantial holdings of MBSs.\(^8\) But Bear Stearns was soon followed by many other US banks including powerhouses Goldman Sachs, JP Morgan Chase, and Merrill Lynch.\(^9\) Merrill Lynch had made the unfortunate mistake of becoming a ‘prime broker’ lending significant amounts to Bear Stearns for the purposes of establishing those same troubled subprime-laden hedge funds.\(^10\) In early August, it was the turn of European banks, in particular German bank IKB Deutsche Industriebank. IKB had become heavily involved in the US MBS market in previous years as a means of bolstering otherwise lacklustre profits. IKB ultimately required public rescue due to what the markets essentially deemed to be extremely “reckless exposure” to the subprime market.\(^11\) The attrition continued throughout August with attention variously turning to several Canadian banks and hedge funds, Citigroup in the US, several German ‘landesbanks’ (including, most prominently, WestLB and SachsenLB), major British banking groups Lloyds and HBOS, and French bank BMP Paribas.\(^12\)

The significant and, indeed, mounting losses being suffered by major banks due to their exposure to the collapsing market for MBSs fomented the emergence of a ‘credit crunch’ in the critically important interbank lending market in August 2007.\(^13\) Centrally, as Gamble outlines, this interbank ‘credit crunch’ was constituted by a “growing divergence” between the interest rates at which the central banks governing the world’s leading financial centres - the

\(^8\) M. Coote 2008, “Taxpayers may have to Rescue Failing Banks”, National Business Review, 20 March, 3; The Economist, “Cracks in the Facade”, 74; “Another Pounding”, 75; R. Dodd 2007, “Subprime: Tentacles of a Crisis”, Finance and Development, Vol. 44, no. 4, 16. It should be noted however, that Britain’s Hong Kong and Shanghai Banking Corporation (HSBC), then Europe’s biggest bank and one of the two largest subprime mortgage lenders, had taken significant action much earlier in 2007. It was forced to make provisions for over $10 billion in write downs at the end of 2006 following a 36% increase in its bad debt costs. Germany’s Deutschebank also reported significant subprime related problems in March 2007. See The Economist, “Rising Damp”; “Cracks in the Facade”.


\(^10\) The Economist, “Another Pounding”.


\(^12\) Ibid 61; Dodd 2007, 16.

European Central Bank, the Bank of England, and the US Federal Reserve were “prepared to lend to the banks and the interest rate[s] at which banks were prepared to lend to one another.” As The Economist reported, “on any normal business day the spreads would be only a few hundredths of a percentage point.” But

on August 9th and 10th the rates commercial banks charge each other for overnight borrowing spiked on both sides of the Atlantic. In America the rate hit almost 6%, well above the Fed’s target of 5.25%. In the Euro Area, money market rates peaked briefly at 4.7% sharply above the benchmark of 4%. In essence, despite generally being considered to be one of the most secure and highly liquid aspects of the global financial system, the interbank lending market had suddenly become dominated by a breakdown in mutual trust. Banks began to charge increasingly punitive rates when lending to one another, whilst simultaneously hoarding cash and other highly liquid assets in order to ensure the stability of their own balance sheets.

Two factors played a key role in feeding the emergence of this credit crunch. The first of these was the practice of ‘securitisation’ that had developed around the subprime mortgage market. In the decade leading up to the crisis, many leading banks and hedge funds had actively engaged in the bundling together of thousands of subprime and only marginally better ‘Alt-A’ loans into MBSs. These asset-backed securities were then divided up and grouped together with other loans, mortgages and credit derivatives to be formed into further financial instruments known as ‘collateralised debt obligations’ or

---

14 Gamble 2009, 24-25.
16 Ibid. In the UK, the London Interbank Offered Rate (LIBOR) rose to 6.79% in August, also well above the Bank of England’s official lending rate of 5.75%. See Gamble 2009, 25.
CDOs. From here, the cash flows from the resulting collective pool of debt were subdivided into ten segments known as ‘tranches’. Each tranche, now representing a claim on a portion of the income accruing to the CDO, was rated according to its credit worthiness. This would begin with the bottom tranche, known as the ‘equity’, which represented the portions of the CDO most vulnerable to default (and thus the lowest credit rating), and would proceed on through to the more senior levels which, in theory, became progressively less vulnerable to default (and thus often attracted an ‘investment grade’ triple A credit rating). Finally, “the different tranches’ vulnerability to default was hedged by taking out insurance” and the product was sold off.

This complicated, but ultimately extremely innovative process of securitising subprime mortgages into CDOs was believed to have eliminated serious risk from the system. In theory, by bundling risky loans into CDOs and then selling them off, any losses sustained as a result of default would be dispersed thinly across the entire system thus avoiding the possibility of any single lender facing overwhelming losses and subsequent collapse. The reality was, however, that the process left entire CDOs tainted. As Blackburn observes, a key “feature of the securitising and tranching process is that the holders of a tranche would not know which specific mortgages they held.” Consequently, when the rate of mortgage delinquencies increased dramatically (as occurred in late 2006) such assets could no longer be reliably valued; the market for subprime MBSs rapidly became illiquid because, essentially, no one could be sure where liability for potentially up to US$1.1 trillion of shaky subprime

---

18 It should be noted that this particular aspect of the securitisation process, the rating of structured financial products, was very lucrative. Rating agency Moody’s generated 40% of its revenues from this aspect of its business in 2006. See G. Tett and P. Davies 2007, “Out of the Shadows: How Banking’s Secret System Broke Down”, Financial Times, 17 December.
19 Blackburn, 75; Dodd 2007, 16-17.
21 The Economist 2007, “Another Pounding”.
22 Blackburn, 75.
lending lay. Former US Treasury Secretary Paul O’Neill aptly described the problem as follows: “If you had ten bottles of water and one bottle had poison in it, and you didn’t know which one, you probably wouldn’t drink any one.”

As events transpired, it was many of the major Wall Street and international European banks that were in possession of significant portions of the contaminated subprime securities when the bottom fell out of the market in July-August 2007. Many had bought up senior, ‘investment grade’ structured financial instruments in anticipation of new international bank capital regulations coming into effect as part of the new ‘Basel II’ agreement. Because of this, banks grew increasingly reticent about lending to one another. With the contamination of subprime-linked assets so widespread, few institutions wished to expose themselves to the ‘impaired’ asset base of another.

The second factor that played a key role in feeding the development of the credit crunch was that a significant number of major US and European financial institutions had become heavily involved in a ‘shadow’ banking system that had developed during the decade prior to the onset of the crisis. This secondary, ‘hidden’, banking system was made up of an abundance of obscure ‘structured investment vehicles’ (SIVs), ‘conduits’, and “bank sponsored hedge funds” owned and controlled by the major banks. Often based offshore for ‘tax planning’ purposes, these so-called ‘shadow’ investment vehicles were generally used to issue high quality (and thus lower yielding) commercial bonds which would in turn be used to fund the purchase of what turned out to be low quality but high-yielding assets, such as tranches of the

---

23 Dodd 2007, 17.
28 Tett and Davies; Blackburn 68, 70.
afore mentioned subprime MBS-based CDOs. The shadow investment vehicles would then generate significant profits for their parent institution by exploiting the differential between the rate at which they borrowed funds and the rate of return on the assets they purchased with said funds (a common investment practice known as ‘arbitrage’). Profits would often be multiplied many times over by becoming highly ‘leveraged’ through further debt issues.

The banks’ involvement in this so-called shadow banking system played a key role in feeding the development of the credit crisis because it effectively acted to “hide much of their exposure” to the cancerous subprime mortgage market. In July-August 2007, US and European banks’ SIVs, conduits and hedge funds “held scores of billions of dollars” worth of now toxic MBSs and CDOs. But, as Blackburn observes, the major banks’ various shadow investment vehicles were, as a rule, generally retained “off balance sheet, so that the bank’s stake in them was an asset, while the liabilities stowed away did not show up.” As a result, when the markets for MBSs and CDOs collapsed, banks quickly became cagey about lending to one another. It was apparent that many banks (but no one knew exactly which ones) were likely to be hiding significant problems created by major off-balance sheet lending sprees and so prudence dictated subscription to risk aversion lest “poisonous securities turned out to constitute a major portion of their [counter-party’s] asset base.”

In response to the onset of the severe interbank credit crunch, the world’s central banks began to inject large amounts of official liquidity into the system in order to try and restore liquidity to the interbank lending market. The first to take action was the European Central Bank. On 9 August the European

---

29 Indeed, in mid-August 2007, rating agency Standard and Poor’s estimated that around 23% of SIVs assets were made up of MBSs, with around half of these being from the US. See The Economist, “A Conduit to Nowhere”.

30 Blackburn, 68, 75-76.

31 Ibid, 64.

32 Ibid, 75.

33 Ibid, 63, 69.

34 Ibid, 64; Gamble, 24.
Central Bank provided some US$131 billion of funds on easy terms to the banking sector. This would form the first of four progressively smaller interventions carried out by the European Central Bank on successive days. Other central banks quickly followed suit; the US Federal Reserve injected significant amounts of cash into the money market on 9, 10, and 15 August, and the respective central banks of a significant number of other countries, including Canada, Japan, England and Australia, undertook similar operations. Led by the US, additional official liquidity operations continued sporadically throughout late 2007 and on into 2008.

The repeated provision of fresh reserves by central banks had some limited success in pushing interbank lending rates back down. However, the impact was only temporary. During the period from July 2007 to March 2008, “the Wall Street investment banks and brokerages hemorrhaged $175 billion of capital.” In addition, in September the persistently high cost of liquidity led to a run on major British mortgage lender Northern Rock. As a consequence, the combined liquidity measures of the world’s central bankers were, quite simply, insufficient; the interbank lending market remained tightly gripped by fears of the potential exposure of other banks to significant liabilities arising from the collapse in the market for MBSs.

On 16 March 2008, the seemingly irrepressible credit crunch claimed its first major victim on Wall Street. In a Federal Reserve sponsored deal, the fifth largest Wall Street investment bank, Bear Stearns, was bought out in a ‘fire sale’ by rival JP Morgan Chase for $2 a share (a year before Bear shares had topped

---

35 The Economist, “Bankers’ Mistrust”, 60.
36 Ibid.
37 Blackburn, 65; Gamble 2009, 26-29.
39 Blackburn, 64.
40 Ibid, 63.
$170 each). During the week prior to its forced sale, from 13 March onwards, Bear Stearns’ clients had withdrawn some $17 billion from the company. Bear could not readily withstand the pressure this run placed on its balance sheet; more so than any of the other major Wall Street investment banks, Bear was heavily reliant on short term borrowing and the so-called ‘repo’ market for its funding. With a gaping hole apparent in its balance sheet, Bear could not readily ‘roll-over’ this crucial source of financing. Thus, as The Economist details, with Bear effectively facing bankruptcy, “the Fed moved in with emergency funding, using JP Morgan Chase, Bear’s clearing bank, as a conduit. But it was clear that no one would want to do business with a bank reliant on 28-day loans from the central bank.” Consequently, JP Morgan Chase moved in, picking up its long-time Wall Street rival for just $236 million, and with some $29 billion of backing finance for Bear’s weakest assets from the Federal Reserve.

As would be expected, the near collapse of Bear Stearns drove global financial markets into turmoil. Centrally, as Marco Annunziata, chief economist at UniCredit (a major Italy-based financial institution) observes, because Bear was “rescued by selling it at such a large discount”, the financial markets assumed “its balance sheet was seriously and fundamentally impaired.” Concerns consequently arose “that other institutions might be in a similar predicament.” Subsequently, led by banking and other financial sector stocks,

---

43 The Economist 2008, “The $2 Bail-out”, 22 March, 75. The original $2 a share offer made by JPMorgan Chase for Bear Stearns was later raised to $10 a share on 24 March. See The Economist 2008, “No Picnic”, 29 March, 79.
44 White 2008.
46 White 2008.
48 Ibid. In the same deal that saw JP Morgan Chase’s offer for Bear Stearns shares increase from $2 to $10, the Federal Reserves pledged backing finance was also somewhat reduced. JPMorgan Chase agreed to shoulder the first $1 billion of losses, however, the Federal Reserve still potentially remained exposed to losses counted in the ($US) billions. Again, see The Economist, “No Picnic”, 79.
50 Ibid.
global equity markets sank. The US dollar plunged to record and near record lows against other ‘safe haven’ currencies (the euro, yen, and Swiss franc). Gold and US Government bond prices soared, and credit spreads (a measure of the market’s appetite for risk) “widen[ed] to record levels on both sides of the Atlantic.”\textsuperscript{51} Interbank lending, meanwhile, “virtually ground to a halt.”\textsuperscript{52}

In order to restore confidence in the system, the world’s major central banks responded by launching a fresh wave of liquidity provision initiatives. In quick succession, the US Federal Reserve announced a pair of additional $50 billion auctions of one-month loans to banks through its ‘Term Auction Facility’ (TAF), the European Central Bank announced €50 billion worth of additional six-month loans (also to be distributed via two separate auctions) and renewed €100 billion of existing three-month loans, and the Bank of England began to offer a new three-month loan service.\textsuperscript{53} These initial measures in March were followed on 21 April by the Bank of England introducing a ‘Special Liquidity Scheme’. As Mervyn King, governor of the Bank of England, stated, this scheme was fundamentally intended to “take the liquidity issue off the table in a decisive way” by allowing UK banks to swap MBSs for highly liquid Treasury bills for up to three years.\textsuperscript{54} Shortly thereafter, the US Federal Reserve again moved aggressively against the seemingly intractable interbank lending market. It increased the size of its TAF by an additional $50 billion, bringing it to a total of $150 billion.\textsuperscript{55}

Following these various moves made by central banks, market sentiment improved. As The Economist observed at the time, “just six weeks later, everything seems a lot calmer. Stockmarkets have stabilised and corporate credit spreads (the excess interest rates paid by risky borrowers) have come

\textsuperscript{51} Ibid.
\textsuperscript{52} Ibid.
\textsuperscript{55} K. Guha and M. Mackenzie 2008, “Central Banks in New Move to Ease Credit Strains”, Financial Times, 2 May.
down sharply. Gold is cheaper. Bankers talk about having put the worst behind
them.” It was widely acknowledged amongst market participants and
observers that a significant amount of ‘deleveraging’ would need to take place
and that downside risks remained. But it was also considered that the credit
losses from the turmoil were likely to be significantly overstated. Consequently,
the widely held view was that “the most likely path ahead” was that the severe
financial instability would decrease gradually, as “confidence and risk appetite”
returned to the market.

Improving market sentiment enabled many banks and other financial
institutions to seek to rebuild their balance sheets. Through various new share
and debt issues the Royal Bank of Scotland (£12 billion), HBOS (£4 billion),
Barclays (£4.5 billion), UBS ($15.5 billion), Wachovia ($7 billion), Citigroup ($9
billion), and Lehman Brothers ($4 billion) were amongst dozens of banks both
in the US and Europe to raise significant new capital during the period from
April to early July. However, despite improving sentiment and such efforts at
recapitalisation, a number of significant problems remained. Firstly, the malaise
afflicting the US housing market that was the genesis of the financial crisis, was
only getting worse. Defaults were continuing to mount and more were
inevitable; declining house prices were placing more and more households in a
negative equity position. Secondly, significant credit losses were beginning to
emerge “in areas other than housing.” A weakening US labour market was
fuelling major increases in consumer credit defaults, and corporate loan

58 Gamble 2009, 31; C. Hughes, M. Mackenzie, H. Simonian, P. Thal Larsen, B. White, and A. van Duyn
Deals: What’s in them for Investors”, Wall Street Journal, 15 April; D. Enrich and A. Dowell 2008, “Credit
Crunch: Citi Seeks $3 billion more --- Common Stock Sale Would Lift Infusion to $39 Billion Total”, Wall
Street Journal, 30 April. Other major institutions to raise capital included JP Morgan Chase, Bank of
America, and AIG in the US, Societe Generale in France, and Bradford and Bingley in the UK.
59 The Economist 2008, “Too Soon to Relax”. A negative equity position greatly increases incentives for a
mortgagee to simply walk away from a property rather than to repay a mortgage.
defaults were also beginning to mount. Finally, in the global money markets, banks were still being faced with having to pay “high margins over official rates to borrow short-term money”, with the LIBOR remaining well above average historical levels. As Peter Oppenheimer, a Goldman Sachs investment strategist, summed up the overall situation at the time, “the Fed may have underwritten the solvency of the banks but the economic problems haven’t gone away.”

Consequently, “although most serious analysts thought the worst was over in the [northern] spring”, the crisis proceeded to deepen. In early July, a leading US mortgage lender, Pasadena-based IndyMac Bank, collapsed in what was then the third largest bank failure in US history. IndyMac’s seizure by federal regulators followed an 11 day ‘run’ on the bank, during which $1.3 billion was withdrawn by depositors. The collapse of IndyMac was immediately followed the next day by official intervention to prevent the collapse of Fannie Mae and Freddie Mac, the veritable cornerstones of the US housing market.

The rapid demise of IndyMac, coupled with the apparent distress of Fannie Mae and Freddie Mac clearly indicated that serious problems continued to afflict the US financial system. It was not until September, however, that this latest phase of the financial crisis culminated. First, on 7 September, Fannie Mae and Freddie Mac were nationalised. The massive debts these two institutions had accumulated were seen by the US authorities to pose an unacceptable threat to systemic stability. Then, on 15 September 2008, Wall Street investment bank Lehman Brothers collapsed. Lehman had posted a crippling

61 Ibid.
67 Ibid.
third-quarter loss of $3.9 billion on 10 September and, despite some considerable government-facilitated efforts, had failed to find a buyer willing to take over its assets.\textsuperscript{68}

As Gamble observes, “the failure of Lehman Brothers seemed to open the floodgates.”\textsuperscript{69} Over the following days and weeks in the US, Lehman’s fellow Wall Street investment bank Merrill Lynch was bought by Bank of America for $50 billion; the US’s largest insurance company AIG was nationalised in a $85 billion rescue operation; Washington Mutual was seized by federal regulators and underwent a fire sale to JP Morgan Chase in order “to prevent the largest bank failure in US history”; and the fourth-largest bank in the US, Wachovia, was taken over by Citigroup.\textsuperscript{70} Similar events occurred on the other side of the Atlantic. In the UK, Bradford and Bingley, a buy-to-let mortgage specialist, was nationalised and some of its assets sold to Spanish bank Santander, and “HBOS, the country’s largest mortgage lender”, was bought out by Lloyds. In Germany, the second-largest mortgage lender, Hypo Real Estate required a €35 billion loan from German banks and the German government to prevent its collapse. Elsewhere in Europe, Fortis bank was partially nationalised by the Dutch, Belgian and Luxembourg governments, Belgian-French bank Dexia obtained a €6.4 billion capital injection from government, and Iceland’s third-largest bank, Glitnir, was fully nationalised.\textsuperscript{71}

Facing what appeared to be the threat of systemic financial collapse, the world’s governments were forced to intervene. After an initial plan was rejected on 29 September, the US took the lead in this with a $700 billion bailout package passed by Congress on 3 October. On 8 October the UK followed suit, announcing a £50 billion bailout plan as well as up to £200 billion in new short-term loans to banks. Similar measures were undertaken in Sweden, the

\textsuperscript{68} Ibid.  
\textsuperscript{69} Ibid, 32.  
\textsuperscript{70} Albo, Gindin and Panitch, 67; Gamble 2009, 32. Wachovia’s sale to Citibank was later cancelled and Wachovia was instead sold to Wells Fargo.  
Netherlands, France, Germany and Russia. Other European governments also undertook assorted actions in support for their banking systems. In Ireland, for example, the government announced a guarantee covering all deposits in the country’s six largest banks, potentially exposing itself to up to €400 billion of liabilities. The Icelandic government meanwhile, nationalised their second largest bank, Landsbanki. Coinciding with all these various government interventions, central banks liberally slashed official interest rates.

In support of these initial measures, several governments purchased large equity stakes in major banks in order to be able to inject new capital directly into key financial institutions. The UK government was in the vanguard of this action. Following a meeting of the G7 finance ministers in Washington on 11 October, it announced that it would provide £20 billion of new capital to the Royal Bank of Scotland in exchange for a massive 60% stake and a further £17 billion of new capital to newly merging HBOS and Lloyds in exchange for a 40% shareholding. Other governments quickly followed suit. The US announced that it would provide $250 billion for bank recapitalisation in exchange for “non-voting preference shares.” Included in the queue for this government-sponsored recapitalisation were Wall Street survivors (but now legally commercial rather than investment banks) Goldman Sachs and Morgan Stanley, as well as behemoths Bank of America, Citibank, and JP Morgan Chase. Respectively, the French government announced the provision of €40 billion of funds for bank recapitalisation, and the Swiss government took a 9% equity stake in UBS in exchange for a $60 billion fund to write off toxic assets.

---

73 Ibid.
74 Gamble 2009, 33.
75 Ibid.
76 Albo et al 69; Gamble 2009, 33.
Despite all of these measures, the crisis continued to widen and deepen. In the global money markets interbank lending effectively ceased.\textsuperscript{78} Short-term lending – for periods of three-, six-, or twelve-months – disappeared, and overnight borrowing costs skyrocketed. As the \textit{Economist} reported,

banks used to borrow from each other at about 0.08 percentage points above official rates; on September 30\textsuperscript{th} they paid more than four percentage points more. In one auction to get dollar funds overnight from the European Central Bank, banks were prepared to pay interest of 11\%, five times the pre-crisis rate.\textsuperscript{79}

Moreover, as McNally observes, the geographic scope of the financial crisis was “no longer largely about the US.” Instead, it had “gone global.”\textsuperscript{80} A wave of systemic financial instability was spreading throughout the advanced capitalist and ‘emerging market’ economies, igniting a string “of devastating national and regional crises” as it went.\textsuperscript{81}

By November, the prospect of a deep generalised global economic downturn had emerged. The Eurozone economies were already mired in recession. As \textit{The Economist} reports, “output in the Euro area fell at an annualised rate of 0.8\% in the second quarter. GDP shrank in the currency zone’s three largest countries – Germany, France, and Italy. The fourth largest, Spain, barely grew.”\textsuperscript{82} The Japanese economy was faring even worse. “Its economy shrank at an annualised rate of 3\% in the second quarter as exports fell, investment slowed and high food and fuel prices dented consumer confidence.”\textsuperscript{83} The other economies of the advanced capitalist ‘triad’, the US and the UK, were on the very brink, if they had not already slipped into recession.

\textsuperscript{78} \textit{The Economist} 2008, “When Fortune Frowned”, 9 October, 3-4.
\textsuperscript{79} \textit{The Economist} 2008, “World on the Edge”.
\textsuperscript{81} Ibid.
\textsuperscript{82} \textit{The Economist} 2008, “Bad, or Worse”, 11 October, 88.
\textsuperscript{83} Ibid.
As Harvey observes, by this stage “all segments of the US economy were in deep trouble” and “the British economy was in equally serious difficulty.” Consumer spending, construction, and manufacturing output were all in steep decline. Added to this, unemployment was increasing rapidly, with hundreds of thousands of jobs disappearing from the US economy alone. China’s economy, for so long the apparent driver of global economic growth, was also slowing. “In the third quarter” of 2008, “GDP growth had slipped to 9%, the slowest quarterly pace since 2003.”

---

84 Harvey 2010, 5.
85 The Economist 2008, “Bad, or Worse.”
7.2) The Fifth National Government: A Political Overview

It was into this extremely unstable international financial and economic environment that the centre-right FNG came into power in New Zealand. On Saturday 8 November, 2008, the New Zealand National Party was elected to office, decisively defeating the incumbent Labour-led Government that had held power for almost a decade. National secured 44.9% of the party vote and 58 parliamentary seats to Labour’s 34% and 43 seats, having attracted the votes of significant numbers of previously Labour supporters, as well as large numbers of votes from previous supporters of the conservative centrist New Zealand First and United Future parties. Combined with the 5 MPs secured by the hardline neoliberal ACT Party, the sole surviving United Future MP, and the 5 MPs gained by the Maori Party (with all of whom National now formed a multi-party coalition), this electoral result enabled National to call on support from 68 MPs out of a total house of 122, a decisive majority.

National won the 2008 election campaigning on a platform of change and renewal in government. At the party’s election campaign launch, party leader John Key stated that:

You are all rightly sick of political sideshows, bossy government, and yesterday’s fights... You are looking for a Government with...fresh ideas and the energy to meet the challenges this country faces. At this election National is offering exactly that.

National clearly signaled, however, that a change in government would not necessarily entail radical changes in public policy. If elected, National promised to pursue only a moderate centre-right agenda that would notably entail the

---

88 Additional support on certain issues could also be found within the Green Party. The new government signed an official ‘memorandum of understanding’ with the Greens on 8 April, 2009, potentially providing the new FNG with the support of a further 9 MPs. See ibid, 342-344.
retention of many of Labour’s most popular policies, including *Working For Families* (WFF), interest-free student loans, and free early childhood education.\(^{90}\)

A National Party victory at the 2008 general election was widely anticipated within both the electorate and commentariat.\(^ {91}\) Indeed, as noted by Levine and Roberts, “even those intending to vote for parties other than National fully expected a change of government, with Labour going into opposition against a government led by National.”\(^ {92}\) Widespread electoral fatigue appears to have been an important factor in National securing power. After nine years in office, Labour’s politicians were increasingly seen as arrogant and its policies as ‘out of touch’.\(^ {93}\) Ultimately, however, it appears that the leadership of John Key was the deciding factor.\(^ {94}\) Unlike his predecessor, Don Brash, “the apparently amiable (and ideologically flexible) John Key” appeared to offer voters a safe and viable alternative to Helen Clark as the nation’s leader.\(^ {95}\)

As expected, global economic conditions continued to deteriorate following the election of the FNG. After having already slowed considerably in 2008, the world economy underwent a sharp contraction in 2009. Total world economic output for the year declined by 0.7%.\(^ {96}\) The specific performance of the major advanced capitalist economies was far worse. The US, the Euro area and Japan recorded official growth rates of -3.5% -4.3% and -6.3% respectively.\(^ {97}\) Global economic growth subsequently rebounded in 2010, but nevertheless remained relatively weak throughout the remainder of the FNG’s first term in


\(^{96}\) IMF 2011, *World Economic Outlook* (Washington: IMF), 2

\(^{97}\) Ibid.
power. Overall global economic performance during the period spanning from the onset of the GFC to the end of 2011 is illustrated below in Table 7.1.

**Table 7.1) World Economic Growth, 2005 to 2011 (%GDP)**

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>World Output</td>
<td>4.8</td>
<td>5.1</td>
<td>5.2</td>
<td>2.8</td>
<td>-0.7</td>
<td>5.1</td>
<td>3.9</td>
</tr>
<tr>
<td>US</td>
<td>3.1</td>
<td>2.8</td>
<td>2.1</td>
<td>0.0</td>
<td>-3.5</td>
<td>2.4</td>
<td>1.8</td>
</tr>
<tr>
<td>Euro area</td>
<td>1.5</td>
<td>2.8</td>
<td>2.7</td>
<td>0.5</td>
<td>-4.3</td>
<td>2.0</td>
<td>1.5</td>
</tr>
<tr>
<td>Japan</td>
<td>1.9</td>
<td>2.4</td>
<td>2.3</td>
<td>-1.2</td>
<td>-6.3</td>
<td>4.5</td>
<td>-0.6</td>
</tr>
<tr>
<td>China</td>
<td>10.4</td>
<td>11.6</td>
<td>13.0</td>
<td>9.6</td>
<td>9.2</td>
<td>10.4</td>
<td>9.3</td>
</tr>
<tr>
<td>Australia 58</td>
<td>2.9</td>
<td>2.9</td>
<td>4.5</td>
<td>3.4</td>
<td>1.2</td>
<td>2.1</td>
<td>1.7</td>
</tr>
</tbody>
</table>


Despite being sheltered somewhat by the relative resilience of its largest trading partners (Australia and China, see Table 7.1), New Zealand was not immune to these international economic developments. The real economic growth rate slumped in 2008, falling from 3.4% in 2007 to just 1.3%.99 In 2009 the New Zealand economy entered into a short, sharp recession. The economy contracted by 2.9% in real terms that year.100 Although the economy subsequently recovered, it nevertheless remained fragile through until the end of the Fifth National Government’s first term; the real rate of economic growth was only 1.2% in 2011.101 The manifestation of the global recession in New Zealand is set out statistically in Figure 7.1 below.

---

58 GDP data for Australia is based on years ending in March.
100 Ibid.
101 Ibid.
On 22 February, 2011, New Zealand’s second largest city, Christchurch, was struck by a powerful earthquake. Measuring 6.3 on the Richter scale, the earthquake caused significant damage throughout the city and killed a total of 185 people. The official estimate of the cost of rebuilding Christchurch was $40 billion. As Prime Minister John Key observed in 2013, this made it “the largest and most complex, single economic project in New Zealand’s history.” Through the EQC, a substantial portion of the rebuild costs were covered by insurance. However, the earthquake nevertheless entailed sizeable fiscal costs for central government. In particular, “the Government bore the cost of repairing damage to capital assets it owned, and some of the cost to local government too.” In 2014, “the Government’s contribution to the rebuild [was]

---

102 GDP data based on years ending in March.
expected to be $15.4 billion, of which $7.3 billion [would] be incurred by the Earthquake Commission, net of reinsurance proceeds.”

107 Treasury 2014, 11.
7.3) The Macroeconomic Policy Response of the Fifth National Government

Initial Response

The FNG’s initial macroeconomic policy response to the onset of the global financial crisis and subsequent recession was centred around the implementation of a modest ‘discretionary’ fiscal stimulus package.\(^{108}\) This fiscal expansion broadly mirrored the actions of most other advanced capitalist economies, and was fundamentally designed to “create much needed jobs and economic stimulus” and to “equip New Zealanders with some much needed extra cash in tough economic times.”\(^{109}\) The cornerstone of the FNG’s initial fiscal stimulus package was “a three-year programme of personal tax cuts” in concert with a “step-up” in public infrastructure investment.\(^ {110}\) As can be seen from Table 7.2, over three years, from 1 April, 2009, the top marginal income tax rate would be dropped from 39% to 37%, the upper threshold for the lower middle income tax bracket would be raised from $40,000 p.a. to $50,000 p.a., and the lower middle marginal rate reduced from 21% to 20%. A new ‘Independent Earner Tax Credit’ worth around $10 a week would also come into effect. Overall, the personal tax cut package introduced from 1 April, 2009 was expected to inject around $1 billion into the domestic economy.\(^ {111}\)

Simultaneous to these tax cuts, the FNG advanced around $500 million of planned infrastructure spending on roads, housing, and schools which would start ahead of schedule.\(^ {112}\) Other important elements of the fiscal stimulus package implemented by the FNG were a new tax assistance package for small and medium-sized businesses (SMEs), injecting over $480 million of extra cash

\(^{108}\) In comparison to the FNG’s stimulus package, Australia implemented a A$42 billion stimulus package, with around A$12.7 billion being pumped into the Australian economy in the first six months of 2009. See N. Smith 2009, “Key throws SMEs a Slender Lifeline”, The Independent Financial Review, 5 February.

\(^{109}\) Key 2008, “Speech from the Throne.”

\(^{110}\) Ibid; Treasury 2009, Personal Tax Cuts Info Sheet (Wellington: Treasury).


\(^{112}\) J. Key 2009, “Securing a Brighter Future: One Year In.”
into SMEs over four years (including $270 million immediately for the five remaining months of the 2008/2009 financial year through “changes to the timing and payment of provisional tax”), and the introduction of a ‘ReStart’ package, providing extra financial support for four months to “Kiwi families hit hard by redundancy.”

Table 7.2) Details of FNG’s April 1 2009 Tax Cuts

<table>
<thead>
<tr>
<th>Income Level</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Lower Income</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>12.5%</td>
<td>12.5%</td>
<td>12.5%</td>
<td>12.5%</td>
</tr>
<tr>
<td>Bracket</td>
<td>&lt;$14,000</td>
<td>&lt;$14,000</td>
<td>&lt;$14,000</td>
<td>&lt;$14,000</td>
</tr>
<tr>
<td><strong>Lower Middle Income</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>21%</td>
<td>21%</td>
<td>21%</td>
<td>20%</td>
</tr>
<tr>
<td>Bracket</td>
<td>$14,001-$40,000</td>
<td>$14,001-$48,000</td>
<td>$14,001-$50,000</td>
<td>$14,001-$50,000</td>
</tr>
<tr>
<td><strong>Higher Middle Income</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>33%</td>
<td>33%</td>
<td>33%</td>
<td>33%</td>
</tr>
<tr>
<td>Bracket</td>
<td>$40,001-$70,000</td>
<td>$48,001-$70,000</td>
<td>$50,001-$70,000</td>
<td>$50,001-$70,000</td>
</tr>
<tr>
<td><strong>Higher Income</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>39%</td>
<td>38%</td>
<td>37%</td>
<td>37%</td>
</tr>
<tr>
<td>Bracket</td>
<td>&gt;$70,000</td>
<td>&gt;$70,000</td>
<td>&gt;$70,000</td>
<td>&gt;$70,000</td>
</tr>
</tbody>
</table>


In support of its initial stimulus package, the FNG held a so-called ‘jobs summit’ on 27 February, 2009. This gathering brought together around 200 business leaders, union officials and industry sector interest group representatives for the purposes of generating “ideas for keeping Kiwis in work and providing new job opportunities.” The key outcomes of the FNG’s jobs summit were the adoption of a new ‘Jobs Support Scheme’ (JSS) and the

---

113 Ibid”; N. Smith 2009; A. Young 2009, “PM Determined not to Saddle Future Generations with a Mountain of Debt”, New Zealand Herald, 5 February. The SMEs tax assistance package primarily involved reducing penal interest rates paid on underpaid tax from 14.24% to 9.73% and removing the 5% ‘uplift’ rate on the provisional tax paid by SMEs. By late November 2009, the FNG’s ReStart temporary redundancy assistance package had been utilised by around 5000 workers.

114 Key 2009, “Securing a Brighter Future.”
announcement of the construction of a national cycleway. With significant support from both employers and unions, the FNG’s new JSS essentially involved allowing struggling businesses to adopt a nine-day working fortnight, with government subsidised training made available to workers for the tenth day. The proposed national cycleway, meanwhile, was intended to create up to 4000 extra jobs at the cost of tens of millions of dollars and, ultimately, to provide a boost to tourism.

The FNG also maintained New Zealand’s retail deposit and wholesale funding guarantee schemes. These had been introduced with cross-party support by the previous Fifth Labour Government on 12 October and 1 November 2008 respectively, in order to ensure the continued stability of the domestic financial system. New Zealand was sheltered from much of the international banking instability surrounding the global financial crisis due to the generally sound balance sheets of the major Australian banks that dominate the New Zealand finance system. Nevertheless, vulnerability did exist in their heavy reliance on international short-term credit markets for funding due to a generalised paucity of sufficient domestic savings. Consequently, the retail deposit and wholesale funding guarantees were implemented to “facilitate improved access to international funding markets for New Zealand banks”, while at the same time giving “assurance to New Zealand depositors.”

---


118 M. Cullen 2008, “Deposit Guarantee Scheme Introduced”, 12 October; “Wholesale Funding Guarantee Facility”, 1 November. The FNG later extended the retail deposit guarantee scheme out to 31 December, 2011 on 25 August 2009 and, as a result, became liable for $1.6 billion of deposits when the country’s largest non-bank financial institution, South Canterbury Finance, collapsed on 31 August, 2010. See T. Parker 2010, ”Three bidders but deal proved too hard”, *The New Zealand Herald*, 1 September.
Budget 2009

A major focus of Budget 2009, the FNG’s first, was to provide further fiscal stimulus to the flagging New Zealand economy. The lead elements of this extended fiscal stimulus program took the form of increased spending on public services and infrastructure. The FNG announced $5.8 billion of new spending on front-line services, “particularly in health, education, and justice”, to be delivered over four years in Budget 2009. Some of this new public services spending was also “front-loaded into 2009/10” in order to further ameliorate the “worst...effects of the recession.” Alongside this, the FNG introduced $1.45 billion of new capital initiatives to be commenced in the following five years, and a further $6 billion (for a total of around $7.5 billion) of new capital initiatives to be announced in the following four budgets (starting from 2010).

Key elements included within this new infrastructure spending were: $1 billion over three years for roading (in addition to the $142 million announced as part of the FNG’s initial fiscal stimulus package); $258 million for newly re-nationalised KiwiRail (as well as a new operating debt facility); $1.5 billion over six years for the accelerated roll-out of ultra-fast broadband; and $243.7 million for the ‘HeatSmart’ home insulation and clean heating initiative.

Coupled with these further stimulus measures, the FNG also allowed “the so-called automatic stabilisers” to operate in Budget 2009, so as to provide a fiscal cushion sufficient to protect “New Zealanders from the hardest edges of recession.” The FNG ensured the continued provision of the country’s various income support entitlements and maintained at existing levels “New Zealand
Superannuation, [unemployment, domestic purposes, sickness, and invalids] benefits, and the Working for Families scheme.”¹²⁴ This policy stance would effectively allow social welfare disbursements to increase substantially, as required, as the recession began to take hold.¹²⁵

The combination of new stimulus measures and the operation of New Zealand’s automatic fiscal stabilisers resulted in a sizeable short-term fiscal expansion.¹²⁶ The operating balance before gains and losses (OBEGAL) was a deficit of $7.6 billion (equivalent to 4.3% of GDP) in the 2009/10 financial year, and a deficit of $8.6 billion (4.2% of GDP) was recorded in the following 2010/11 financial year.¹²⁷ However, this was only to be a temporary emergency measure.¹²⁸ Alongside the various expansionary policy moves “laid out” in Budget 2009, the FNG also outlined its broader, medium-term fiscal strategy.¹²⁹ This fiscal strategy was fundamentally aimed at “ongoing expenditure restraint” and the limitation of public debt growth.¹³⁰

The “main driver” of this ongoing ‘austerity’ program was a permanent reduction in budget operating allowances for new government expenditure.¹³¹ The Budget 2009 operating allowance was “revised” down by $300 million from $1.75 billion to $1.45 billion, and “the operating allowance for future budgets” was cut even more severely, by some 37% “from $1.75 billion to a maximum of $1.1 billion from 2010/11, growing at 2% thereafter.”¹³² Another major facet of the FNG’s ongoing drive for fiscal austerity was a significantly increased focus on efficiency and savings in the public sector. The core government

¹²⁴ Ibid, 3.
¹²⁶ Roper 2011b, 23.
¹²⁷ Treasury 2009, Key Facts for Taxpayers (Wellington: Treasury); ibid 2010, Key Facts for Taxpayers (Wellington: Treasury). OBEGAL deficits continued, although at much lower levels, through until 2014. See data appendix.
¹³¹ NZPA 2008.
bureaucracy was officially capped, and “a line-by-line review” of all
government expenditure (some $64 billion in 2009) was conducted, resulting in
“a total of more than $2 billion in spending over four years” being earmarked
for redeployment to the FNG’s “priority areas.”\(^{133}\) Other important components
of the FNG’s austerity strategy announced in Budget 2009 were the delaying of
“the second (1 April, 2010) and third (1 April, 2011) tranches” of the FNG’s
planned tax cuts “until such a time as economic and fiscal conditions allow a
reconsideration”, and the suspension of the FNG’s “required capital
contributions” to the New Zealand Superannuation Fund (NZSF) “until the
operating balance is sufficient in terms of cash flow to meet contributions and
other capital spending” – estimated to be around 2020/21.\(^{134}\) Figures 7.2 and 7.3
(below) illustrate the intended cumulative impact of the FNG’s fiscal austerity
strategy on future government expenditure and debt respectively.

Statements of the Government of New Zealand for the Year Ended 30 June 2009} (Wellington: Treasury),
5; 2010, “Executive Summary”, 10.
\(^{134}\) Treasury 2009, “Executive Summary”, 11.
Figure 7.2) Forecast Impact of FNG’s medium-term Fiscal Strategy on Future Government Operating Expenses, 2009 to 2023

% of GDP

Year ended 30 June


Total Crown expenses
Core Crown expenses
Core Crown expenses less finance costs


Figure 7.3) Forecast Impact of FNG’s medium-term Fiscal Strategy on Future Government Debt, 2009 to 2023

% of GDP

Year ended 30 June


Budget 2009
Without policy response

Source: Treasury 2009, FSR, 42.
### Budget 2010

Ostensibly marking “a new phase in the Government’s economic strategy”, a major focus of Budget 2010, delivered on Thursday, 20 May, was on “strengthening the recovery” of the domestic economy that had begun in the latter stages of 2009. Although it identified “six key drivers of stronger economic performance”, an extensive program of regressive taxation reform formed the “centrepiece” of the FNG’s efforts to “accelerate” New Zealand’s economic recovery in Budget 2010. As can be seen from Table 7.3, from 1 October, 2010, the top marginal income tax rate would be reduced from 38% to 33%, the top middle income tax bracket would be reduced from 33% to 30%, the lower middle income tax bracket would be reduced from 21% to 17.5%, and the rate on personal income of $14,000 or less would fall from 12.5% to 10.5%. Simultaneous to these cuts to personal tax rates, the company tax rate would be dropped from 30% to 28%, and “the top tax rate for portfolio investment entities (PIEs), superannuation funds, unit trusts, group investment funds and life insurance policyholder income” likewise reduced so as to remain in alignment. Other important components of the FNG’s ‘recovery strengthening’ policy program included within Budget 2010 were a significant increase in spending on science, research and development, and the initiation of a number of “major infrastructure investments.” New spending of “$321 million over four years” was announced “for a range of science, research and development initiatives, lifting total spending to $750 million a year”, and “around $1 billion over four years to support key infrastructure projects” including “the electrification of Auckland commuter rail” and the roll out of a nationwide, ultra-fast Broadband network.

---

137 Ibid, 23.
139 Ibid; ibid 2010, “Fiscal Strategy Report”, 40. One of the FNG’s major new science, research, and development initiatives was the so-called ‘Primary Growth Partnership’. This was centrally aimed at
But *Budget 2010* ultimately adhered to the medium-term austerity strategy set out by the FNG in *Budget 2009*. New spending stayed within the strict $1.1 billion operating and $1.45 billion capital allowances provided in *Budget 2009*. The only other source of new funding was $1.8 billion over four years freed up from existing baselines following another ‘line-by-line’ review of departmental spending.\(^{140}\) Aside from the new outlays on science, research and development outlined above, most new funding was redirected to the FNG’s ‘priority areas’ of health and education; as in *Budget 2009*, “most agencies received no additional funding.”\(^{141}\) The tax reforms implemented as the official “centrepiece” of *Budget 2010*, meanwhile, were intended to be ‘fiscally neutral’. The package of personal tax cuts to come into effect on 1 October, 2010 effectively constituted a $4.5 billion per annum reduction in personal taxes. However, the FNG’s broader taxation reform program as a whole was fully-funded by a corresponding increase in GST (increased from 12.5 to 15%) and the implementation of other so-called ‘base-broadening’ and ‘integrity’ measures.\(^{142}\)

---

\(^{140}\) Ibid “Executive Summary”, 10.


\(^{142}\) Ibid, “Executive Summary”, 6. The major base broadening measure implemented by the FNG was the removal of the 20% depreciation allowance for residential property investment. Figures contained in *Budget 2010* indicate that the FNG expected this move to boost taxation revenues by $3.12 billion over the four years from 2010-14. See Treasury 2010, “Executive Summary”, 8.
Table 7.3) Details of FNG’s October 1 2010 Tax Cuts

<table>
<thead>
<tr>
<th></th>
<th>Existing</th>
<th>New</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Lower Income</strong></td>
<td>Rate</td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>12.5%</td>
<td>10.5%</td>
</tr>
<tr>
<td>Bracket</td>
<td>&lt;$14,000</td>
<td>&lt;$14,000</td>
</tr>
<tr>
<td><strong>Lower Middle income</strong></td>
<td>Rate</td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>21%</td>
<td>17.5%</td>
</tr>
<tr>
<td>Bracket</td>
<td>$14,001-$40,000</td>
<td>$14,001-$48,000</td>
</tr>
<tr>
<td><strong>Higher Middle Income</strong></td>
<td>Rate</td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>33%</td>
<td>30%</td>
</tr>
<tr>
<td>Bracket</td>
<td>$40,001-$70,000</td>
<td>$48,001-$70,000</td>
</tr>
<tr>
<td><strong>Higher Income</strong></td>
<td>Rate</td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>38%</td>
<td>33%</td>
</tr>
<tr>
<td>Bracket</td>
<td>&gt;$70,000</td>
<td>&gt;$70,000</td>
</tr>
<tr>
<td><strong>GST</strong></td>
<td>Rate</td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>12.5%</td>
<td>15%</td>
</tr>
<tr>
<td><strong>Company Profit</strong></td>
<td>Rate</td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>30%</td>
<td>28%</td>
</tr>
<tr>
<td><strong>PIEs and “other savings vehicles”</strong></td>
<td>Rate</td>
<td></td>
</tr>
<tr>
<td>Rate</td>
<td>33%</td>
<td>28%</td>
</tr>
</tbody>
</table>


Budget 2011

As could be reasonably expected, a major aspect of Budget 2011 was the provision of funds for the rebuilding of Christchurch. Treasury estimates put “the direct impact on Crown expenses from the two earthquakes” at $8.8 billion. This overall cost was comprised of two main components:

“$3.3 billion to recognise the Crown’s Earthquake Commission (EQC) obligation ($1.5 billion for each event) and Accident Compensation Corporation (ACC) costs, and $5.5 billion for central government’s costs, such as its share of local government infrastructure, roads, insurance excesses on schools and hospitals, temporary housing and other policy responses.”\textsuperscript{143}

Budget 2011 established “a Canterbury Earthquake Recovery Fund” (CERF) in order to “ensure transparency and control” over these costs.\textsuperscript{144} The CERF had an initial endowment of $5.5 billion, including $740 million sourced from within relevant agencies existing funding baselines. The remaining $3.3 billion of the anticipated costs of the earthquakes were to be covered from levy-funded EQC and ACC reserves.\textsuperscript{145} Table 7.4 (below) sets out the expected costs of the earthquakes and the methods proposed to fund them.

**Table 7.4) Christchurch Earthquake Costs and Funding Sources**

<table>
<thead>
<tr>
<th>Instrument</th>
<th>Canterbury Earthquake Recovery Fund</th>
<th>EQC + ACC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Estimated costs</td>
<td>$5.5 billion</td>
<td>$3.3 billion</td>
</tr>
<tr>
<td>Funding source</td>
<td>$4.8 billion new funding including from Canterbury Earthquake Kiwi Bonds</td>
<td>$740 million from existing funding</td>
</tr>
</tbody>
</table>


**Table 7.5) Summary of Budget 2011 Spending versus the Operating Allowance**

<table>
<thead>
<tr>
<th>$million increase/(decrease)</th>
<th>Operating</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2010/11</td>
</tr>
<tr>
<td>New spending</td>
<td>110</td>
</tr>
<tr>
<td>Savings (including revenue initiatives)</td>
<td>145</td>
</tr>
<tr>
<td>Net increase/(decrease)</td>
<td>(35)</td>
</tr>
</tbody>
</table>


Aside from this, however, in Budget 2011 the FNG ‘pressed ahead’ its medium-term fiscal austerity agenda, “exercising [even] greater spending restraint” than it had in previous budgets.\textsuperscript{146} Operating allowances for new

\textsuperscript{144} ibid.
\textsuperscript{145} ibid.
\textsuperscript{146} ibid, 1, 5.
spending were reduced by $400 million over four years, from the $4.4 billion level established in *Budget 2009* to just $4 billion.\textsuperscript{147} Simultaneously, $5.2 billion was cut from existing government expenditure over five years.\textsuperscript{148} The bulk of these latter cuts were made to the core public service and major social policy initiatives: Government contributions to the ‘Kiwisaver’ retirement savings scheme were reduced by $2.5 billion over four years; funding for the previous FLG’s flagship *Working For Families* (WFF) programme was cut by $448 million over four years; student loan accessibility was tightened (reducing the Government’s expected outlays by $447 million over five years); and $980 million over three years of so-called “efficiency savings” were imposed “across the state sector.”\textsuperscript{149} The cumulative result of this ‘acceleration’ of the FNG’s medium-term austerity agenda was to slash discretionary new operating spending by $1.2 billion over four years and, more importantly, to achieve a $5.6 billion reduction in the FNG’s overall expenditure over the same period.\textsuperscript{150} Table 7.5 (above) provides a year-by-year breakdown of these intended funding cuts.

Thus, in response to the global financial crisis and ensuing economic recession, the FNG initially implemented a modest fiscal stimulus package and a so-called ‘jobs summit’ in order to support economic activity and employment, thereby providing a counter-cyclical fiscal buffer for the economy. The FNG also maintained the wholesale and retail deposit guarantee schemes implemented by the FLG in order to ensure the stability of the nation’s financial system. This was immediately followed by further ‘discretionary’ stimulus measures, as well as a substantial generalised fiscal expansion in *Budget 2009*. However, this macroeconomic policy response was only a temporary solution.

\textsuperscript{147} Ibid, 5.
\textsuperscript{148} Ibid, 1.
\textsuperscript{149} Ibid 9. The FNG also signaled in *Budget 2011* that it was likely seek further “efficiencies in the public sector” in future budgets. See ibid, 5.
emergency measure. Before the economy was even fully recovered, the FNG reverted back to a neoliberal austerity agenda fundamentally aimed at cutting back public spending and reducing public debt. Budget 2010 implemented a number of measures designed to help boost the economic recovery, but it did so from within the limited means prescribed by the FNG’s medium-term austerity agenda it set out in Budget 2009. Budget 2011, respectively, primarily acted to extend the FNG’s broader fiscal austerity agenda even further.

---

151 Roper 2011b, 25.
7.4) “A Dark Cloud on the Horizon”: The ‘Dollar-Wall Street Regime’ and the Fifth National Government’s Macroeconomic Policy Agenda

The FNG implemented its distinctively neoliberal macroeconomic policy response in the wake of the GFC primarily because there was, in Finance Minister Bill English’s own words, “a dark cloud on the horizon.” This ‘dark cloud’ constituted the prospect of a decline in New Zealand’s ‘creditworthiness’ in IPFMs. Other factors were of course important in influencing the formulation of the FNG’s overarching policy program. Roper notes, for example, that Business New Zealand played a key role in pushing for the 90-day trial period for new workers in SMEs that was introduced by the FNG in 2009. But in terms of the formulation of macroeconomic policy, the ‘dark cloud’ of a potential decline in the country’s international creditworthiness should be considered to be the determining factor. As Prime Minister John Key himself admitted immediately prior to the unveiling of Budget 2009, the “primary focus of this Budget is to avoid a credit ratings downgrade.”

As numerous authors have documented, prior to the onset of the GFC, New Zealand was already a heavily indebted nation by international standards. New Zealand has consistently run high current account deficits since the mid-1970s which has necessarily resulted in the progressive accumulation of a substantial stock of overseas debt. As noted in Chapter Four, the best measure of this stock of external liabilities is contained within Statistics New Zealand’s regularly updated International Investment Position data series.
The key relevant elements of this extremely detailed data set are set out in Table 7.6 (below). As can be seen, by early 2008, just before the full onset of the GFC in September, New Zealand had accrued net external liabilities totaling $-138,659 million, or 76% of nominal GDP. This level of international indebtedness was particularly high in an international context.

<table>
<thead>
<tr>
<th>New Zealand’s International Assets</th>
<th>$million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banks</td>
<td>26,673</td>
</tr>
<tr>
<td>General Government</td>
<td>8,813</td>
</tr>
<tr>
<td>Monetary Authorities</td>
<td>19,737</td>
</tr>
<tr>
<td>Other Sectors</td>
<td>33,041</td>
</tr>
<tr>
<td>Total International Assets</td>
<td>88,264</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>New Zealand’s International Liabilities</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Banks</td>
<td>137,513</td>
</tr>
<tr>
<td>General Government</td>
<td>17,616</td>
</tr>
<tr>
<td>Monetary Authorities</td>
<td>540</td>
</tr>
<tr>
<td>Other Sectors</td>
<td>71,254</td>
</tr>
<tr>
<td>Total International Liabilities</td>
<td>226,923</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>New Zealand’s Net International Asset Position</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>-138,659</td>
</tr>
</tbody>
</table>

| Nominal GDP                                  | 182,478  |
| Total IIP as % of Nominal GDP                | 76%      |
| Total International Liabilities as % of Nominal GDP | 124%     |


The main component of New Zealand’s external debt prior to the onset of the GFC was comprised of the overseas borrowing undertaken by New Zealand’s largely Australian-owned banks (see Table 7.7). As Bertram outlines, New Zealand’s persistent current account deficits since the 1970s have

---

157 My figures show slight variation from those cited by Bertram 2009 as they are for the period ending March 2008, whereas Bertram’s were for the period up to June.

158 Bedford, 19.

159 The vast bulk of this offshore borrowing was to fund the domestic housing market. As Snively observes, in December 2008, “housing [was] the biggest asset in the ‘NZ inc.’ portfolio (valued at $617 billion...)” Mortgages lent on this set of assets were by far “the biggest liability of the New Zealand financial system.” In 2007 “housing accounted for 98 percent of the new lending by the five major trading banks.” See S. Snively 2009, *New Zealand Monetary Policy and the Residential Housing Market – A Scoping Study Working Paper* (Wellington: Centre for Housing Research Aotearoa New Zealand (CHRANZ), 52, 123.)
been financed “by borrowing offshore, in three successive waves.”\textsuperscript{160} From 1975 through to the late 1980s, the bulk of offshore borrowing was undertaken by government. Total offshore debt reached 70\% of GDP, of which, roughly half was made up of public borrowing.\textsuperscript{161} During the early to mid-1990s, “the overseas debt [was] privatised.”\textsuperscript{162} Following a massive sell off of state assets by the Fourth National Government, New Zealand’s gross external liabilities reached $113 billion in 1997, of which private inward equity investment made up around half.\textsuperscript{163} Since the 1997-8 East Asian crisis, however, “the hole in the New Zealand balance of payments” has been filled by an “extraordinary inflow” of funds into New Zealand banks from offshore.\textsuperscript{164} This inexorable rise in banks offshore borrowing prior to the impact of the GFC is presented in Figure 7.4. As can be seen, the component of New Zealand’s gross external liabilities made up of the offshore borrowing of banks totaled $137,513 million, or the equivalent of 60.6\% of nominal GDP, in March 2008.

\textsuperscript{160} Bertram 2009, 13.
\textsuperscript{161} Ibid.
\textsuperscript{162} Ibid.
\textsuperscript{163} Ibid.
\textsuperscript{164} Ibid.
Table 7.7) Asset Structure of New Zealand Banking System, December 2008 ($billion)

<table>
<thead>
<tr>
<th>Australian Banks:</th>
<th>Assets:</th>
</tr>
</thead>
<tbody>
<tr>
<td>ANZ National (1)</td>
<td>$107.79</td>
</tr>
<tr>
<td>Westpac (2)</td>
<td>$64.71</td>
</tr>
<tr>
<td>ASB (3)</td>
<td>$59.35</td>
</tr>
<tr>
<td>National Australia Bank (BNZ, 4)</td>
<td>$56.38</td>
</tr>
<tr>
<td>Total:</td>
<td>$288.22</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Other Foreign Banks:</th>
</tr>
</thead>
<tbody>
<tr>
<td>HSBC (6)</td>
</tr>
<tr>
<td>Deutschebank (7)</td>
</tr>
<tr>
<td>Rabobank (8)</td>
</tr>
<tr>
<td>Citibank NA (9)</td>
</tr>
<tr>
<td>Total:</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>New Zealand Banks:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kiwi Bank (5)</td>
</tr>
<tr>
<td>TSB Bank (11)</td>
</tr>
<tr>
<td>SBS (13)</td>
</tr>
<tr>
<td>Total:</td>
</tr>
</tbody>
</table>

**Total Banking System Assets** $321.25


In comparison, the component comprised of public debt was relatively small and remained more or less stable (in gross terms) during the decade prior to the onset of the GFC. As outlined in Chapter Five, during the period from 1999 to 2008 the FLG ran a generally conservative fiscal stance. Substantial and ongoing fiscal surpluses were run and financial assets were simultaneously built up, primarily in the form of the so-called ‘Cullen Fund’. As a result of this conservative fiscal approach, net government debt tracked down significantly during the period from 1999 to 2008 (reaching and then moving below zero net debt in 2006), while government debt remained more or less stable in gross
terms. The comparative path of external general government debt prior the GFC is also set out in Figure 7.4.

**Figure 7.4) New Zealand Bank and General Government Offshore Debt, March 2001 to March 2008 ($million)**

![Graph showing the comparative path of external general government debt from March 2001 to March 2008](image)

Source: Statistics New Zealand.

Mirroring developments elsewhere in the advanced capitalist world, the events surrounding the GFC significantly undermined the FNG’s financial position. A steep decline in international prices and demand for key export commodities (especially Dairy)\(^{166}\), combined with the effects of a domestic economy that had already entered a moderate downturn before the full impact of the GFC, as well as a significant package of tax cuts coming into effect in October 2008, meant that government revenues were substantially reduced

---


\(^{166}\) The IMF estimates “that the high terms of trade added about 1¾ of GDP to government revenue” (for instance, reflected in high export commodity prices) prior to the onset of the GFC. Consequently, “the projected decline in the terms of trade will therefore have a strong negative impact on [government] revenue” post-GFC. See Brooks *et al* 2009, “New Zealand: Selected Issues”, *IMF Country Report*, No.09/146 (Washington: IMF), 24.
from late 2008 onwards. Simultaneously, government expenditure trended upwards, as the FNG introduced its modest discretionary fiscal stimulus and simultaneously exercised the country’s previously mentioned ‘automatic stabilisers’ to maintain existing welfare entitlements and, in the FNG’s words, to absorb “much of the shock of the recession on the Government’s balance sheet.” As a result, a large gap between the FNG’s revenue and expenditure began to emerge from early 2009 onwards. This revenue gap was necessarily funded from increased public borrowing (mainly from overseas investors). At the time of the announcement of Budget 2009, projections showed public debt reaching 48 percent of GDP by 2013 and 70 percent by 2023. The official projected trajectory of public debt provided in Budget 2009 is presented in Figure 7.5 below. In addition to this mounting international public debt, the previous FLG had also “recently taken on significant contingent liabilities to maintain confidence in the financial system.” This was the government guarantee of the overseas wholesale funding of the largely Australian-owned domestic banking system, which, as we have seen, the FNG chose to maintain. Michael Cullen, Minister of Finance under the previous FLG, estimated that “the contingent liability for the New Zealand taxpayer” had the guarantee been ‘called’ could have reached as high as $150 billion. However, looking closely at the overall structure of New Zealand bank’s funding, Bertram suggests contingent liability would more-likely have been somewhat smaller; between $20 billion and $70 billion.

167 Bowing to mounting political pressure, the previous FLG announced a $10.5 billion program of tax cuts coming into effect on 1 October as part of Budget 2008. Thus it is perhaps not coincidental that the FNG’s operating deficit for the subsequent year was $9.6 billion. See Treasury 2008, Key Facts for Taxpayers (Wellington: Treasury).
169 Ibid, 2.
Figure 7.5) Forecast Increase in Gross Government Debt Contained in *Budget 2009* (%GDP)

The FNG’s rapidly deteriorating financial position acted to highlight for IPFMs a number of “systemic vulnerabilities” already present within the broader macroeconomy that generally sound government finances had previously acted to offset. In particular, vulnerabilities associated with the domestic banking system’s heavy reliance “on offshore funding became a looming issue.” As Bedford outlines, “the major Australian banks obtain a material amount of non-tradable debt funding directly from their Australian parents.” However, Australian Prudential Standard (APS) 222 Section 32 (12), enforced by the Australian Prudential Regulation Authority (APRA), places a quantitative restriction on the amount the parent banks are allowed to advance.

---

to their New Zealand subsidiaries. Consequently, “the banks...also borrow externally by issuing debt securities in offshore credit markets” such as Wall Street and the City of London. By mid-2008, “in nominal terms, the banks [had] borrowed nearly $140 billion...from international investors.”

Immediately prior to the onset of the GFC, the maturity profile of this offshore borrowing was dominated by short-term financial instruments (such as 90-day bills). Indeed, “40 percent of the bank’s offshore debt was typically due to mature within 90 days”, with a significant amount more due to mature within a year. In addition, a substantial proportion of this debt was also denominated in foreign currency. As Bedford observes, “around half of New Zealand’s international debt liabilities were denominated in foreign currency (mostly US dollars)” in June 2008. Unsurprisingly, considering their dominance of the external liabilities ledger, the banks accounted “for a sizeable fraction” of these foreign-currency liabilities.

The dependence of the New Zealand banking system on short-term borrowing in international credit markets exposed the banks (and, subsequent to the introduction of the wholesale guarantee scheme, the FNG) to significant “rollover risk.” If for whatever reason offshore lenders became unwilling to provide new financing for maturing loans, New Zealand banks could have quickly faced “severe balance sheet distress” as funding and system-wide liquidity dried up. This would not only severely impact on the banks apparently ubiquitous business operations, but could also potentially destabilise the wider macroeconomy (discussed in more detail below). Respectively, the bank’s predominantly foreign currency denominated offshore

---

175 This is primarily to limit the exposure of Australian banking system to any major crisis developing offshore.
176 Bedford, 23.
178 Bedford, 23.
180 Ibid, 20; Woolford, Reddell and Comber, 14-15.
181 Bedford, 18.
182 Bertram 2009, 14.
debt exposed New Zealand to significant “exchange rate risk.”\textsuperscript{183} Over time, a steadily falling nominal FX rate could progressively raise the local currency value of a large portion of the country’s foreign liabilities, thereby increasing debt servicing costs and also the risk of default.\textsuperscript{184}

As a result, in early 2009 international credit rating agency Standard and Poor’s began to threaten to downgrade New Zealand’s sovereign credit rating. Having placed New Zealand on a negative ratings watch in January 2009, three Standard and Poor’s executives (Kyran Curry, David Beers, and Brendan Flynn) made a highly publicised visit to New Zealand in May during the week immediately prior to the announcement of the Budget.\textsuperscript{185} On arrival it was stated that Standard and Poor’s were looking for the FNG “to articulate a path to a more fiscally conservative or a more stable fiscal position.” More specifically, Curry stated that it was expected “that over the cycle of the [Fifth National] Government [it] would be recording operating surpluses within...the next three to five years.”\textsuperscript{186} Without such moves, it was intimated that New Zealand’s AA+ sovereign credit rating would be downgraded.

The immediate impact of such a rating downgrade would likely have been to increase the country’s interest rates and public debt servicing costs. There existed some “uncertainty about the [exact] quantitative impact” that a downgrade of New Zealand’s international credit rating would have had “on the size of New Zealand’s sovereign risk premium.”\textsuperscript{187} However, Treasury Secretary John Whitehead observed that “based on Ireland’s [March 2009}
downgrade from AAA to AA, a downgrade for New Zealand would result in a 1.5 percent rise in [domestic] interest rates”, as well as an increase of around “$600 million to government debt interest costs.” 188

But this was potentially only the ‘tip of the iceberg’. “A growing mountain of government debt” and a subsequent downgrade of the country’s sovereign credit rating could have also put “New Zealand at risk of a [serious] adverse reaction” from IPFMs that could have resulted in severe macroeconomic instability. 189 As a number of commentators have observed, if for any reason foreign lenders were to continue to lose confidence in the underlying ‘creditworthiness’ of New Zealand borrowers – interpreting, for example, the initial downgrade of New Zealand’s official sovereign credit rating as a signal of incipient weakness in the country’s macroeconomy and related public policy settings - the country’s banks may have eventually found that they were unable “to refinance [their rapidly] maturing international debt at any price.” 190 IPFMs may have begun to target New Zealand as a “weak link” in the global economy and subsequently raised “its borrowing costs to unsustainable levels.” 191 Based on the recent experiences of fellow small open developed free-market economies Iceland (2006, 2008) and Ireland (2010), which likewise had large stocks of external liabilities residing on the balance sheets of their banks, (although of different character and quantities 192), were such an eventuality to occur, there is a very real possibility that what would have followed would be the onset of a severe “economic disruption.” 193 The nation’s sovereign credit rating would have plunged. A large-scale capital

190 Bedford, 21. A similar outcome is likely to be produced if risk aversion increases in IPFMs, or there is a generalised freezing up of international credit markets. See W. Rosenberg 2009, “Financial Crises, Trilemmas, and a Time to Rethink”, 2. www.converge.org.nz/watchdog/20/02.htm. Accessed 22/2/11, 4:06pm.
192 Iceland’s banks, for example, had been attracting large numbers of small non-resident deposits for the purposes of reinvesting offshore.
193 Bedford, 21.
The local currency value of any unhedged foreign liabilities would consequently rise and, as the “sustainability” of the banks’ foreign-currency debts became a ‘public’ problem under the government’s wholesale guarantee scheme, what began as a banking crisis would quickly morph into a classic sovereign debt crisis. The local share market - the NZX - would collapse. Domestic interest rates would shoot up as the banks became increasingly reticent about lending out increasingly scarce funds and the RBNZ moved to stamp out any potential spike in inflation beyond its 1-3% target band. Productive investment would stall and many businesses would collapse following loan defaults, resulting in a spike in unemployment.

At some point, the IMF would be prompted to act in order to provide the country with “a crisis management programme.” Recent IMF country reports provide a fairly good indication of the likely shape of such a policy plan. In exchange for a sizeable debt relief package, the IMF would require: “transfers to middle-income households”, including Working for Families, social welfare, and student allowance entitlements, to be cut; the age of eligibility for national superannuation to be raised; “higher consumption taxes” (GST) coinciding with “a cut in capital taxes”; a significant generalised downsizing of the state, likely to include major cuts to the core public service, large-scale privatisations of remaining state-owned commercial assets, and increased private sector ‘competition’ in the provision of remaining public services (such as prisons and

---

196 Rosenberg 2009, 2.
197 Wade and Sigurgeirsottir, 22. The RBNZ notes that in late 2008 the IMF had “more than USD 200 billion to lend to member countries experiencing short term financial distress” as a result of mounting “global risk aversion and the associated outflow of short-term capital.” See RBNZ 2008, Financial Stability Report (November) (Wellington: RBNZ), 8.
schools); and an even more ‘ambitious’ programme of so-called ‘supply-side’ regulatory reforms than the FNG has already pushed through parliament.  

Simultaneously, what remained of the New Zealand economy would be systematically plundered by predatory foreign capital. The sharp fall in the FX rate would temporarily produce “a stock of devalued, and in many instances undervalued, assets” in New Zealand. These assets, comprising the country’s most productive and profitable resources and enterprises not already owned by foreign multinational corporations, would undoubtedly be bought up by predatory capital from North America, Europe, Japan, and to a lesser extent China and Russia, as part of a process of what eminent Marxist geographer David Harvey described as “accumulation by dispossession.” Indeed, as was the case with the East Asian crisis of 1997-8, alongside the currency and bond market speculators, the big winners of such a financial crisis in New Zealand would be foreign hedge funds and corporations.

As FNG Finance Minister Bill English explained in his speech announcing Budget 2009, the adoption of a neoliberal macroeconomic policy stance in the wake of the GFC would help to avert this looming ‘dark cloud on the horizon’. A milder programme of voluntary neoliberal structural adjustment, implemented pre-emptively, would avoid a much harsher neoliberal “adjustment...forced on us by lenders reluctant to pay our bills.”

The implementation of pre-emptive fiscal austerity measures would help to avert a national credit rating downgrade primarily by lowering the expected future track of government debt. As outlined in Budget 2010, the FNG’s various moves in Budget 2009 to curtail new and existing government expenditure,  

---

200 Although both China and Russia have made highly publicised FDI forays into New Zealand in recent years North American, European and Japanese capitals are still by far the most dominant FDI players in New Zealand.
defer the government’s annual contributions to the NZSF, and impose ‘efficiencies’ in the core public service (via so-called ‘razor-gangs’), had a significant cumulative impact on the “explosive debt levels which the government faced in late 2008.”

From a projected zenith of 36% of GDP in 2018/19, net public debt was instead expected to peak at only 27% of GDP in 2015/16. This impact of the FNG’s austerity measures introduced as part of Budget 2009 on the future path of net government debt is displayed in Figure 7.7 (below). Lowering the government’s future debt path would mean that the government would retain sufficient financial capacity to step in, should the need arise, as a ‘lender of last resort’ to support any private banks in New Zealand that found themselves in serious funding difficulty.

The state’s own balance sheet would effectively act as a fiscal bulwark against any further shocks to the New Zealand financial system, and offset the significant downward ‘dragging’ effect that the country’s comparatively weak private foreign debt position has on the nation’s overall creditworthiness.

---

204 Ibid.
205 Young 2009, “Credit Team Gives tough Warning on Government Budget.”
Figure 7.7) Forecast Impact of FNG’s Austerity Measures on the Future Track of Net New Zealand Government Debt Contained within Budget 2009

Respectively, the FNG’s neoliberal taxation reforms would help to maintain New Zealand’s creditworthiness in IPFMs by significantly bolstering the profitability of business (at the expense of workers). As discussed earlier, the tax reform programme contained within Budget 2010 entailed cuts to marginal personal and corporate tax rates which totaled around $15 billion over four years. Based on the data contained within the 2010 Budget document Key Facts for Taxpayers which, amongst other things, outlines the government’s gross revenue sourced from corporate taxation, the business share of this would be between $1.5 and $2 billion over three years.\(^{206}\) Business profitability would effectively be gaining a major boost via a substantial structural reduction in the overall tax burden shouldered by business. Fundamentally, bolstering the

---

\(^{206}\) Treasury 2009, *Key Facts for Taxpayers*. The calculation this figure is based on is 6.67% (the effective reduction in the corporate tax take resulting from dropping the corporate tax rate from 30% to 28%), multiplied by $8.9 billion (the pre-cut corporate tax take), multiplied by 3 (as the business tax cut kicked in the 2011/12 financial year, a year later than the personal income tax cuts contained within the same tax package). Obviously, the realised reduction in business tax will depend on a variety of factors, not the least of which is the overall health of the economy during those three years.
profitability of business (especially in the ‘tradables’ sector) supports the underlying creditworthiness of the country by improving “the economy’s capacity to service its external debt”, thus reducing likelihood of a major default on international borrowing.²⁰⁷

The FNG’s program of infrastructure investment would similarly aide in the maintenance of New Zealand’s international creditworthiness. As outlined in the previous section above, the infrastructure component of the FNG’s discretionary stimulus programme would total $7.5 billion over four years, concentrated in the areas of transport and telecommunications. This $7.5 billion effectively constitutes a massive public subsidy of private business investment. Substantial productivity (and, therefore, profit) advantages would accrue to business as a result of the spending programme without requiring any reciprocal private capital outlays (which would normally be a requirement).

A number of observers have suggested that the level of threat faced by New Zealand in the wake of the GFC may have been exaggerated by the FNG in order to help justify its extension of the neoliberal policy agenda. Opposition MPs have been particularly vocal in this regard. However, the prevailing threat of a potential downgrade of New Zealand’s credit rating was real and the implications of such a development should not be underestimated.

As outlined in Section One, the degree of disruption experienced by IPFMs during the GFC - especially between September 2008 and May 2009 - was unprecedented in recent history. IPFMs were characterised by considerable volatility and many international lending and credit markets virtually ceased to operate altogether. Included within the sphere of the “extreme disorder” were the “key bank funding markets.”²⁰⁸ “The commercial paper market”, for

²⁰⁷ OECD 2009, 9.
²⁰⁸ RBNZ 2008, 3, 7. See also A. Bollard 2010, Crisis Auckland: Auckland University Press, 52.
example, “which is a key source of funds for many [major New Zealand financial] institutions..., essentially became frozen over this period.”

As a result, New Zealand banks’ balance sheets were being “severely stretched” and becoming “strapped for cash” during the GFC. Indicative of the extent of New Zealand bank’s funding difficulties is the fact that RBNZ governor Alan Bollard and other top officials were required to undertake a so-called “road trip” during the GFC, travelling “to several world financial markets [to] convince them of the desirability of lending to banks in New Zealand.” Further evidence is the scale of local bank’s uptake of the RBNZ’s MBS-backed liquidity scheme implemented in December 2008; as Bollard observes, “by the end of January 2009 [the RBNZ] had lent out $5 billion to the banks.” Thus, with the banking system facing a severe shortage of funds, New Zealand faced the distinct risk of a liquidity crisis developing. Indeed, Bollard characterised the country as being perched precariously “on a [financial] tight rope.”

It should be noted that it was in fact possible for New Zealand banks to secure some funding in the credit markets of Wall Street and the City of London during the height of the GFC, “albeit at a penalty price”, only in small amounts, for short term, and only if backed by a government guarantee. This was demonstrated by the ANZ in March 2009. However, generally speaking, New Zealand banks were extremely reticent about going offshore “to seek funding for fear that it would not be available.” Rejection by IPFMs would severely strain even a fundamentally sound bank’s reputation, leading to the possibility

---

211 Ibid.
212 Ibid, 89,100.
213 Ibid, 108.
215 Ibid, 152. ANZ secured funding at 7.5% for three years. Bollard notes that this “was very expensive...and set a high benchmark price for future issues” pursued by other New Zealand banks.
216 Ibid, 100.
of the withdrawal of existing funding or even a full-blown bank run. Moreover, as Bollard notes in his first-hand account of the GFC, it was clearly intimated to him by international investors that “if the government were to receive a credit rating downgrade, all bets would be off.” Bank funding would completely dry up, and the Government would likely face a full blown liquidity crisis.

---

217 Ibid.
Conclusion

In August 2007, the world entered into the worst financial crisis in post-world war two history. A mounting wave of defaults on loans in the now infamous US ‘subprime’ mortgage market brought about a major ‘credit crunch’ in international inter-bank lending markets beginning in mid-2007. This ‘credit crunch’ brought about the collapse, or near collapse, of three of the five major Wall Street investment banks – Bear Stearns, Lehman Brothers, and Merrill Lynch – in 2008 and ultimately seriously undermined the stability of the entire global financial system. From there, in late-2008, the world descended into what some have come to refer to as the ‘Great Recession’.

The FNG took power in the midst of this prolonged period of global financial and economic turmoil. In response, the FNG initially implemented a modest discretionary fiscal stimulus package, held a ‘jobs summit’, and maintained the existing wholesale and retail deposit guarantee schemes implemented by the previous FLG. This initial policy response was followed soon after by further ‘discretionary’ fiscal stimulus measures, as well as a substantial generalised fiscal expansion in Budget 2009. However, this macroeconomic policy response only constituted a temporary emergency measure designed to help ensure short-term economic stability. The FNG almost immediately reverted back to a medium-term fiscal strategy primarily characterised by neoliberal austerity measures which it closely adhered to throughout the remainder of its first term in power.

The FNG formulated and implemented this macroeconomic policy strategy in the wake of the GFC in a large part due to the threat posed by a significant decline in New Zealand’s perceived international ‘creditworthiness’. The FNG’s financial position rapidly deteriorated following the GFC. A large gap opened up between revenue and expenditure and this gap was necessarily funded by extensive offshore borrowing. The prospect of a significant increase in public debt served to highlight a number of vulnerabilities already existing
within the nation’s macroeconomy, particularly those linked to the domestic banking system’s heavy reliance on offshore short-term debt funding markets. New Zealand’s international creditworthiness was subsequently called into question, exposing New Zealand to the possibility of a negative reaction from IPFMIs resulting in severe macroeconomic instability. Fundamentally, the various core aspects of the medium-term macroeconomic policy strategy pursued by the FNG were designed to help alleviate this threat.
Conclusion

Thesis Summary

Since the early 1970s, international financial relations have operated under a system of governance that has come to be known as the Dollar-Wall Street Regime (DWSR). The DWSR is underpinned by the twin, self-reinforcing pillars of a pure US dollar standard in international monetary relations and increasingly deep and geographically expansive international private financial markets (IPFMs) occupying a central position in international financial relations. The pure US dollar standard in international monetary relations, in particular, has provided the US with a large number of important economic and political privileges. These privileges include, most prominently, considerable balance of payments flexibility, seigniorage, significant private sector commercial advantages, and greatly enhanced influence and capacity in international relations. The centrality of IPFMs, meanwhile, has relegated states and international financial agencies to an entirely secondary position in relation to the management of international financial relations. Under the DWSR, the US has been invested with the capacity to exercise an unprecedented degree of power in the realm of international economic affairs. Simultaneously, developments in IPFMs – often heavily influenced by US macroeconomic decision-making - play a key role in determining the outcome of domestic-level macroeconomic policy formulation undertaken by individual states in the international system.
The DWSR initially emerged due to the emergence of mounting systemic pressures on the existing BWS of international monetary relations and the onset of severe economic malaise in the early 1970s. During the long post-war boom, capitalism had become increasingly internationalised and unregulated financial markets had re-emerged. These major developments within the underlying structure of the global economy exerted unbearable pressure on the existing BWS arrangements from the perspective of the US. At the same time as the BWS was being effectively undermined, economic growth slowed considerably in the US and elsewhere as the rate of profit across the advanced capitalist world fell precipitously and a generalised crisis of over-accumulation set in. In response, the US asserted its power on the international stage by abandoning the official link between the USD and gold, and subsequently overseeing the cancellation of the BWS capital and exchange controls.

Subsequently, economic growth was restored and the DWSR became firmly established in its hegemonic position governing international financial relations via the geographically uneven process of global neoliberalisation. Extensively sponsored by the US and also reflecting a major shift in the orientation of global capitalism towards finance that had occurred during the post-war boom, the historic rise and spread of neoliberalism across the globe privileged the interests of international private financial capital and facilitated a substantial deepening and geographic expansion of IPFMs. Primarily based around a combination of the ideas of classical liberalism and neoclassical economics, neoliberalism (as a class-based political project) served to free private financial capital from what they perceived to be onerous cross-border and domestic regulatory constraints that had previously curtailed (but not entirely prevented) its ability to exploit potentially profitable investment opportunities. In effect, the financial systems of the world were opened to increased penetration by internationally-mobile private financial capital. Thus,
via global neoliberalisation, states increasingly became firmly enmeshed into the DWSR.

During the period from 1984 to 1990, New Zealand followed the broader global political trend and underwent a comprehensive process of neoliberal ‘structural adjustment’. Throughout their two terms in power, the Fourth Labour Government implemented a wide-ranging radical neoliberal policy agenda. As part of this neoliberalisation process, New Zealand became integrated into the DWSR. The country’s financial markets and capital controls were comprehensively liberalised, the currency was floated, and the domestic financial system was extensively deregulated. Indeed, these necessary prerequisites of DWSR integration formed the absolute vanguard of the greater programme of neoliberal policy reform implemented by the Fourth Labour Government. As intimated by the analysis developed in Chapter 2, from this point forward, the formulation of public macroeconomic policy in New Zealand began to be heavily influenced by the vagaries of IPFM.

New Zealand’s historic shift to neoliberalism was initially propelled by a small, yet highly influential, group of political actors operating in Wellington. This ‘Wellington Policy Community’ (WPC) included key members of the Cabinet under the Fourth Labour Government (most notably, the Finance Ministry ‘troika’ comprised of Roger Douglas, Richard Prebble, and David Caygill), high-ranked bureaucrats in Treasury and the Reserve Bank (most notably Graham Scott and Rod Deane), and prominent business leaders. However, the fundamentally political project advanced by this group was heavily influenced by a broad range of developments, both within New Zealand’s domestic political economy and internationally. These developments included, most prominently: the worldwide onset of ‘stagflation’ during the mid-1970s; a major shift in the balance of power within New Zealand society in favour of business and, simultaneously, business becoming much more
industrially militant and politically active; and the shift in the prevailing international economic orthodoxy from Keynesianism to neoliberalism.

During the period from 1990 to 1994, the Fourth National Government continued New Zealand’s historic shift to neoliberalism. In the realm of macroeconomic policy, this primarily involved the implementation of a radical neoliberal fiscal austerity strategy. The cornerstone of the Fourth National Government’s first term austerity strategy was a fundamental redesign of the New Zealand welfare state. This was implemented in two main stages; the Economic and Social Initiative (ESI) of December, 1990 and the 1991 ‘Mother of All Budgets’. After successfully imposing fiscal austerity via this key pair of policy packages, the Fourth National Government subsequently continued to closely adhere to a neoliberal approach to the formulation of fiscal policy. Between 1994 and 1999, the National administration steadfastly pursued a surplus-driven, low debt fiscal strategy.

The second major phase of New Zealand’s neoliberalisation was driven forward by the Fourth National Government’s first Minister of Finance, Ruth Richardson. Surrounded by close allies in cabinet, Richardson received considerable support for the advancement of the neoliberal policy agenda from Treasury. She was also aided by the specific institutional structure of the state in New Zealand (or, more specifically, the dominance of Cabinet within the executive arm of government) and external pressures exerted on the Fourth National Government by IPFMs. Ultimately, however, to a significant extent, the Fourth National Government’s fiscal austerity agenda reflected the macroeconomic policy preferences of big business.

A key factor contributing to the Fourth National Government’s ongoing adherence to a neoliberal fiscal austerity strategy during the period from 1994 to 1999 was New Zealand’s integration into the DWSR. Centrally, the Fourth National Government faced significant implied pressure from IPFMs to closely adhere to a neoliberal fiscal strategy focused on running budget surpluses and
reducing public debt in order to partially mitigate the significant latent threat that adverse external capital flows posed to New Zealand’s ongoing macroeconomic stability. External constraints imposed by IPFMNs were not the only or even the most decisive factor that determined the outcome of fiscal policy formulation during the period from 1994 to 1999. For example, both major business interests and Treasury are documented as having also exerted considerable influence over the Fourth National Government’s overall policy direction. IPFM-derived external constraints were nevertheless highly significant. Furthermore, integration into the DWSR continued to place major constraints on macroeconomic policy formulation in New Zealand subsequent to the electoral defeat of the Fourth National Government in 1999.

In 1999, the centre-left Fifth Labour Government (FLG) was elected to power in New Zealand. Centrally, the FLG presented itself as pursuing an ostensibly pragmatic social democratic policy agenda. However, this so-called ‘Third Way’ effectively only constituted a moderation of the prevailing neoliberal policy framework. Fundamentally, in the realm of macroeconomic policy, the FLG retained (and ultimately helped to entrench) all of the key features of the neoliberal macroeconomic policy nexus constructed by the previous Labour and National governments during the period from 1984 to 1999. A ‘monetarist’ approach to monetary policy primarily aimed at maintaining low, stable levels of inflation, a freely-floating foreign exchange (FX) regime, and a conservative ‘surplus-driven, low debt’ approach to fiscal policy formulation all remained firmly in place and essentially unchanged under the FLG.

While certainly not explaining everything in terms of an explanatory account of the FLG’s formulation of macroeconomic policy, New Zealand’s ongoing integration into the DWSR during the period from 1999 to 2008 nevertheless placed significant constraints on the macroeconomic policy formulation of the FLG. The principle factor underpinning this was the
existence of what is known within the international economic orthodoxy as the ‘impossible trinity’. The ‘impossible trinity’ necessitated that the FLG remain fundamentally committed to the existing independently floating FX regime. This was because its market-based adjustment serves to cushion the domestic economy from the impact of shocks to the nation’s current account. But a further crucial factor constraining the macroeconomic policy formulation of the FLG was the persistence of significant, unsubstantiated amplitude in IPFMs. Ultimately, each of the other core features of the neoliberal macroeconomic nexus – a ‘monetarist’ approach to macroeconomic management and a conservative approach to fiscal policy – were, at least in part, due to the potential to ‘dampen’ excessive financial volatility.

Thus, it appears that New Zealand’s integration into the DWSR - via the historic process of neoliberalisation - has fundamentally acted to constrict successive New Zealand governments’ scope for autonomous action in to the realm of public monetary and financial management. The major political implication of financial market liberalisation in New Zealand has been a transformation of the underlying structural relationship between the state and internationally-mobile financial capital. The constant threat to ongoing economic viability posed by inherently volatile financial flows has effectively more closely intertwined the interests of the New Zealand state and IPFMs. This is not to suggest, however, that the power of the New Zealand state is in decline; while financial market discipline certainly serves to restrict its overall operational flexibility, the inherent volatility of the DWSR has simultaneously served to increase the necessity for the state to play its traditional functions. Moreover, this transformation of the conditions of state power is far from permanent. The apparent shift in the underlying structural relationship between internationally-mobile financial capital and the New Zealand state, fundamentally, remains historically contingent in important respects.
Key Achievements

This thesis constitutes an original contribution to the scholarly literature seeking to explain New Zealand’s historic shift to, and subsequent retention and entrenchment of neoliberalism. Rather than focusing on the role of specific societal, economic, and state-based factors within a relatively restricted national context, it primarily concentrated on the particular role played by IPFMs. Centrally, the thesis investigated the major political implications flowing from the rapid and wholesale liberalisation of New Zealand’s financial markets. This comprehensive, in-depth investigation integrated a unique application of Gowan’s DWSR analysis into a detailed historical study of New Zealand’s political economy during the period from 1984 to 2011. The resulting DWSR-based analysis usefully supplements existing scholarly accounts of New Zealand’s political economy. Fundamentally, it goes beyond merely observing and, subsequently, describing the influence exerted by IPFMs over the state in New Zealand. Instead, it explains and critically evaluates in a coherent, theoretically-informed, and empirically-grounded way, exactly why and how the international financial system plays such an important role within New Zealand’s contemporary political economy.

Agenda for Further Research

In Chapter Two, it was shown that an important factor driving the global proliferation of neoliberalism was a process of increasingly significant international expansion of US-dominated private financial capital and foreign direct investment (FDI) during the 1960s and 1970s. Major financial institutions and multi-national corporations (MNCs) dramatically expanded their offshore activities during this period, fundamentally acting to create powerful pro-
neoliberal constituencies within most of the states of the advanced capitalist world.¹

It is readily apparent that New Zealand was not left entirely undisturbed by these wider developments in the global political economy. As comprehensively documented by Cronin in his (2001) PhD thesis, *The Politics of New Zealand Business Internationalisation 1972-1996*, during the decade prior to the commencement of the neoliberal reforms, there was a steady upswing in inward business internationalisation (in terms of foreign ownership of assets) within the New Zealand economy.² A major target of inward FDI during the period from 1972 to 1984 was industrial capital. Manufacturing resources, in particular, were of increasing interest to offshore investors.³ However, the financial sector was also a major target of this increasing FDI in the New Zealand economy. As Cronin observes, while already dominated by foreign interests prior to 1972, the financial sector of the economy experienced further increases in foreign direct ownership “from 1972 to 1981 and a very rapid rise from 1981 onwards.”⁴

At a high level of generality, it is possible to posit a brief preliminary analysis of the significance of these economic developments to our broader understanding of New Zealand’s historic shift to neoliberalism. As with other states of the advanced capitalist world, these developments directly affected the structure of New Zealand’s capitalist class.⁵ Those fractions of domestically-operating capital closely associated with foreign and finance-oriented business interests became a much more powerful “social force” within the New Zealand political economy during the decade prior to 1984.⁶ Such intra-capital power

---

² Cronin, 171.
³ Ibid, 323.
⁴ Ibid, 183.
⁵ Panitch and Gindin 2003, 19.
⁶ Ibid. This contention is upheld by a number of authors. See B. Jesson 1992, “The New Elite”, *The Republican*, October-November; 1999, 39-40; Roper 2005b, 107; Kelsey 2015, 47.
shifts engendered a significant alteration of the political-economic pressures being exerted on the state in New Zealand. In particular, with significant elements within domestically-operating capital becoming progressively more internationalised, there was increasing pressure on the state to take “responsibility for creating the necessary internal conditions for sustained international accumulation.” It is suggested that at the vanguard of this dynamic was steadily mounting pressure for extensive economic liberalisation and deregulation, core components of the radical programme of neoliberal reform subsequently implemented in New Zealand from 1984 to 1999.

Closer examination of the issue of the increasing involvement of foreign private financial capital and expanding FDI within the economy prior to 1984 would undoubtedly offer considerable utility. Centrally, a more detailed analysis would add a new degree of depth and sophistication to our understanding of the historical trajectory of neoliberalism in New Zealand. However, this thesis does not seek to examine the explanatory significance of this particular issue in great detail. Ultimately, these particular historical economic trends primarily relate to the initial implementation of neoliberalism in New Zealand. In contrast, as indicated at the outset of the thesis, the overarching focus of this study is on the important role played by IPFMs in the retention and entrenchment of the neoliberal macroeconomic policy regime in New Zealand. It would have therefore been outside of the ambit of this thesis to seek to undertake an extended empirical investigation of the explanatory significance of trends towards increasing internationalisation of productive investment and the financialisation of capitalism prior to 1984.

Consequently, further research is required that undertakes a comprehensive investigation and systematic analysis of the role played by

---

8 Nevertheless, an expanded preliminary analysis of the explanatory significance of processes of economic financialisation and business internationalisation during the period from 1972 to 1984 to New Zealand’s historic shift to neoliberalism is contained in Appendix A.
international finance and internationalising business interests in the historic shift to neoliberalism in New Zealand. This research could productively draw on the analyses developed by radical international political economists Leo Panitch and Sam Gindin in their seminal (2003) work *Global Capitalism and American Empire* and, more recently, in *The Making of Global Capitalism.* This research would effectively serve to integrate the valuable insights contained within the extensive critical literature relating to international political economy into existing explanatory accounts of New Zealand’s historic shift to neoliberalism.

This thesis also highlights a number of other areas where further research would be valuable. In relation to the domestic political sphere, for example, it indicates that further research into the constraints imposed on the free formulation of industrial relations policy flowing from New Zealand’s continued integration into the DWSR is required. In this thesis I have primarily focused upon the implications of financial market liberalisation for the formulation of core macroeconomic policy. As a result, I have covered only in passing the role of IPFMs in helping to entrench a highly deregulated domestic labour market characterised by generally unfavourable employment conditions for workers (including extensive underemployment and casualisation, especially for younger workers), relatively poor job security, and weak union membership (by historical standards). The constraints imposed by IPFMs on New Zealand governments in the realm of monetary policy formulation have thus had powerful flow on effects carrying over into the realm of industrial relations policy formulation. In particular, the constraints on public monetary policy formulation have placed strong secondary pressures on governments to maintain a highly liberalised industrial relations regime. This is because, with the existing ‘monetarist’ approach to monetary policy effectively operating as

---

an anti-employment strategy (see Chapter Five), the overall efficacy of monetary policy is heavily reliant on a high degree of ‘flexibility’ in the domestic labour market.

Consequently, further research is needed to trace the role played by IPFM in the retention of the neoliberal industrial relations regime in New Zealand. This research could be conducted by undertaking a detailed empirical study focusing on the decision-making of the FLG in relation to the implementation of the 2000 ERA. Here, a popular centre-left government retained many of the core features of the neoliberal ECA as part of the ERA. This was despite a strong relationship with the NZCTU, suggesting other powerful pressures were also acting on the FLG. I contend that constraints deriving from New Zealand’s integration into the DWSR played an important role amongst the pressures arrayed against the left-leaning FLG, even if these constraints were not the most causally important factor.

**Implications for Public Policy Formulation**

This thesis also implies that if a liberal democratic political system that fosters true polyarchy is to prevail in New Zealand, substantive public policy initiatives are required. At a broad level, these policies would need to fundamentally curtail the power of financial capital within New Zealand’s political economy. More concretely, such a radical (and, ultimately, counter-neoliberal) reform agenda would necessarily require the reintroduction of capital controls. The existence of robust capital controls would effectively blunt the ability of IPFM to exert influence over the formulation of public policy. The largely unimpeded cross-border movement of capital into and out of New Zealand would be slowed drastically, thereby eliminating the key source of IPFM’s political-economic leverage - the enduring risk posed to the nation’s macroeconomic stability by a sudden episode of capital flight. The
reintroduction of robust capital controls could be supported by the implementation of an effective financial transactions tax. Comprising a micro-levy targeting the vast multitude of individual financial transactions which take place in New Zealand’s financial markets each day, this tax would primarily function to dissuade IPFM participants from engaging in extensive (and potentially destabilising) speculative activity in New Zealand dollar-denominated financial instruments.\(^\text{10}\)

However, the successful unilateral implementation of such policies would undoubtedly prove difficult. For example, significant practical barriers exist to the reintroduction of strong capital controls. As both Treasury and the RBNZ would hasten to point out, ultimately, the isolated reestablishment of controls over cross-border capital flows would almost certainly prove unworkable in practice. Even with a strongly sympathetic economic bureaucracy, financial innovation on the part of IPFMs would likely see the efficacy of any newly implemented capital controls rapidly compromised.\(^\text{11}\)

Furthermore, while it is unlikely that the introduction of a financial transactions tax would prove to be entirely redundant, it is also doubtful that it would prove particularly effective in achieving its goal of significantly reducing speculative activity. A substantial portion of trading in New Zealand dollar-denominated financial instruments takes place far from Aotearoa. The important ‘eurokiwi’ market, for example, is primarily centred on the City of London.\(^\text{12}\)

Consequently, much of the speculative financial asset trading targeted by a financial transactions tax lies outside the enforcement scope of local authorities and would therefore remain unaffected.

\(^{10}\) Speculative investment is a prominent aspect of IPFM trading in New Zealand dollar-denominated assets. This is illustrated by BIS data which shows the New Zealand dollar is the tenth most traded currency in the world. See BIS 2013, 10.

\(^{11}\) Reddell 2009.

Conclusion

Given the considerable practical difficulties associated with unilateral implementation of both capital controls and a financial transactions tax, an alternative approach to strictly domestically-focused public policy initiatives might therefore be found in a cosmopolitan social democracy (CSD) agenda, such as that espoused by Held. Centrally, this would entail (amongst other things) reformed global governance institutions instead taking ultimate responsibility for the implementation of such policies designed to curtail the power of private international financial capital both within domestic political economies and globally. This thesis provides broad intellectual justification for such a policy approach. Most notably, reflecting on the seemingly inherent abilities of contemporary private financial capital to effectively “escape the control of the nation-state”, it intimates that, at the very least, the geographic boundaries of financial market regulation need to be fundamentally restructured along the lines espoused by proponents of a cosmopolitan social democracy. Although there is widespread agreement across the left that reforms of this nature are desirable, its feasibility in the context of globalised, neoliberalised, and financialised capitalism is hotly contested. Nonetheless, this thesis is relevant to this debate by focusing attention on the powerful political effects of IPFMs.

Bibliography


Attorney-General v Ngati Apa [2003] 3 NZLR 643 (CA).


Krippner, G. 2004. “What is Financialisation?” mimeo, Department of Sociology, UCLA.


Parker, T. 2010 "Three bidders but deal proved too hard", The New Zealand Herald, 1 September.


Reddell, M. 2009. Interview with the Author. Friday, 27 November.


Reserve Bank of New Zealand 2013, E3: New Zealand’s Overseas Debt. Wellington: RBNZ.


Statistics New Zealand, New Zealand’s IIP. Wellington: Statistics NZ.


Young, A. 2009. “A National Campaign to Save or Create Thousands of Jobs and Stabilise Shaky Businesses”, New Zealand Herald, 28 February.

Young, A. 2009. “Standard and Poor’s to get Budget Peek”, New Zealand Herald, 23 May.
Young, A. 2009, “Budget: It’s all about Keeping Control of our Debt”, New Zealand Herald, 28 May.
