

NEW ZEALAND GOVERNMENT'S INVOLVEMENT IN AGRICULTURE –
THE ROAD TO NON-SUSTAINABILITY

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Abstract

Why did a small urban based population think it could subsidise its dominantly export agriculture? What pre 1984 policies, created a non sustainable, subsidised New Zealand agriculture where increased output was worth less than the cost? The election of a Labour Government by an urban based population, World War II, introduction of modern agricultural technology and a commodity boom lead to policies aimed at increasing agricultural exports to fund the imports required by an expanding, protected manufacturing sector. These resulted in a burgeoning bureaucracy and an increasingly uncompetitive economy. Specific problems were fixed on an ad hoc basis but the watershed was the UK joining the EEC and NZ's loss of a guaranteed market. The policy response was to encourage farm production with a complex suite of measures, without regard to international competitiveness. This paper outlines the economic and agricultural policy context that lead to the radical surgery of 1984.

Keywords: New Zealand, non-sustainable, bureaucracy

In 1882 the first shipment of New Zealand refrigerated cargo left the Port of Otago, on the S.S.Dunedin for Great Britain. That event ushered in nearly a century of unrestricted agricultural trade, dominated by meat and milk products. Primary products were, and still are, the dominant components of New Zealand's export trade which provides the rationale for successive governments' involvement in agriculture in a variety of policy formats. The aim of this paper is to provide a summary of significant policies and dates relating to both production and marketing up to 1972, when Britain joined the EEC and then a more detailed discussion of the post 1972 period.

The breakup of "Ready Money" Robinson's Cheviot Hills Estate in 1893 established a pattern of Government purchase of land for further subdivision into commercial farms for on sale to individual settlers and with the ability to provide appropriate finance (Advances to Settlers Act 1894). This policy was greatly expanded to include the development of land before settlement in 1929 in order to meet the promises made to servicemen returning from overseas service. The Department of Lands & Survey operated a massive development programme, especially through the 1950-70 period, that was so successful that it was extended to selected young civilian farmers who had demonstrated their managerial ability, but lacked sufficient capital. The settlement of ex -servicemen was an instrument of deliberate social policy and the economics of the scheme were subordinate to the social aims. By 1960 over 3,500 ex-servicemen had been satisfactorily settled and by 1964 a further 80 with the addition of 494 civilians. The State Advances Corporation, which later became the Rural Bank (1974), was charged with the responsibility of providing appropriate finance and on-going budgetary supervision. The fundamental objective of these policies was to get young men established on economic, one man farms that had the potential for further development and growth. In 1964 the Government decided that a break even policy of development costs would be introduced which reduced the rate of settlement. The Rural Bank continued to develop various forms of assistance for those seeking farm ownership that by 1977 consisted of: Farm Ownership Savings Accounts, Loans to Sharemilkers and Lessees, Farm Worker Settlement

Loans, Agricultural Contractors Base Establishment loans, Standard Settlement Loans and Special Settlement Loans.

The period between the wars was one of boom and bust, culminating in the Depression of the 1930's. Following W.W. I and the withdrawal of a number of private firms from the agricultural processing and exporting market place the government was involved with the establishment of a number Producer Boards – Dairy, Meat, Wool etc which had varying responsibilities and powers of processing, marketing and exporting. Ensuring that agricultural products were appropriately processed and marketed was one thing but there was also a farm debt crisis to be resolved as well. In 1936 the first Labour Government enacted the Mortgagees and Lessees Rehabilitation Act which allowed farmers in financial distress to apply to the Land Court to have their debt restructured or written off. While it had some brutal side effects – a reluctance of private lenders to offer farm mortgages, this Act did help stabilize the land market. To help fill this mortgage gap a state bank – the State Advances Corporation (SAC) was formed. The SAC subsequently became the Rural Bank & Finance Corporation (RBFC) in 1974 and became a major player in the debt crisis of 1985.

The outbreak of World War II led to the NZ and Australian governments purchasing all meat, wool and dairy production from farmers at fixed prices and on selling those products to the British Government. At the end of the war the Joint Organization, as it was known was wound-up, and the accumulated surpluses distributed to the respective governments. In New Zealand those profits were paid out the respective Producer Boards to be retained as capital reserves to underpin their activities, while in Australia the funds were disbursed to the individual farmers. The existence of these capital reserves had an important bearing on subsequent agricultural policy in New Zealand for the next three decades.

No sooner had the Joint organization been wound-up than the Korean War triggered a boom in wool prices which created a massive windfall gain for both New Zealand's export income and individual New Zealand sheep farmers. The Government was very concerned about the potential for explosive inflation in an economy just coming out of post World War II rationing and resource restrictions. It therefore decided to freeze one third of each farmer's wool income in a special individual IRD account. Furthermore the money was not to be taxed until withdrawn. Farmers saw the opportunity to use the frozen funds as a means of investing in tax deductible, on farm development over a period of years, and thus took advantage of all the types of new technologies becoming available in the market. Accelerated land development, increased stocking rates and a burgeoning product flow being sold into an undersupplied international market led to New Zealand achieving one of the highest per capita incomes in the world. At the same time the Government embarked on a strategy of developing protected secondary manufacturing in order to boost employment rates in a growing economy. The government introduced quantitative controls - import quotas, for manufactured goods, and this eventually led to the introduction of price regulations- tariffs, as well. Increased agricultural exports were required to bankroll the resource imports needed by the expanding manufacturing sector, even in the face of falling international prices.

The 1963 Agricultural Development Conference was a Government sponsored attempt to the policies and resources required to boost New Zealand's livestock stocking rate to 100million Stock Units with the attendant flow-on of primary product for export. It was assumed that the entire increased product could be satisfactorily marketed internationally. The influence of a liberal Commissioner of Inland Revenue was significant in the establishment of a generous taxation regime for farmers intent on development. Unfortunately some rude shocks were looming on the horizon. In 1966/67 the wool market suffered a significant price fall and eventually tumbled to levels comparable to those of the Depression, bar a brief respite in the early 1970's. The Wool Commission, backed by the accumulated Wool Board reserves bought the majority of the clip which not only took product out of the wool pipeline but confronted the economy with a shortage of foreign exchange and the Government with a significant internal deficit. The

position was unsustainable, especially when on 13 October 1967 the Commission bought 46.5% of the Dunedin catalogue, an action that precipitated a modification of Wool Commission operating strategy from wool purchase to price supplementation. In November 1967 the country devalued and a decade of inflation began. The lesson of the power of the market was not well learnt and the policy of economic insulation continued and indeed deepened.

1972 was a watershed, following Britain's decision to join the EEC and the loss of Commonwealth Preference. The New Zealand government was forced to renegotiate the access of all its primary products to that trading block. In addition it focused attention on the need to diversify New Zealand's primary production systems and international markets even though the country had reached a record level of overseas reserves. The first oil shock of 1973 confronted the newly elected Kirk Labour Government with a difficult decision and their solution was to borrow overseas in order to maintain the level of economic activity. This led in an era of increased manufacturing and local industry protection to a rapid increase in the rate of inflation and an economy that was not well managed. The problems created by fluctuating commodity prices generated considerable concern and the establishment of the Farm Income Advisory Committee. This committee was required to produce a Farm Income Policy consistent with a required rate of growth remaining market responsive, whose fluctuation effects could be cushioned from both the farmer and community standpoint. The Zanetti Report as it came to be called made a number of recommendations most of which were seen as unacceptable either by Government or farmers. Some of their recommendations did see the light of day in modified form at a later date.

In 1960 subsidies to agriculture hardly existed and they were then opposed by most farmers and their leaders. From then until 1984 there was a gradual and continuing acceleration of production grants and subsidies. By 1980 they were being demanded by the majority of farming leaders who believed they were necessary for their industry's survival in an economy operating under a relatively free wage bargaining system, a virtually fixed exchange rate and uncontrolled interest rates, plus of course import controls and restrictive practices of many kinds. A perusal of the annual New Zealand Budget and Estimates of Expenditure reveals the growing significance of assistance to agriculture (see Appendix I).

The election of the Muldoon National Government in 1975 led to a decade of increased Government involvement in agriculture. A policy of encouraging farmers to increase production was again implemented. Farm inputs were subsidized, particularly for finance, fertilizer and transport. Price support schemes were developed to stabilize incomes, thus providing a more certain environment for farmers to increase production. The total package was believed necessary to ensure an incentive to increase production, and also to compensate farmers for increased costs caused by the protection of the domestic economy. Essentially the government was operating a one sided devaluation – export subsidies for exporters and incentives and subsidies for farmers, that masked the impact a fixed exchange rate policy was having on the economy.

Farm gate prices were affected through policies in four areas: exchange rate, processing and transport costs, product price support, and producer board regulations and performance. The fixed exchange rate policy isolated New Zealand from ruling international product prices, whilst direct product price support came initially through government funded income stabilization measures (Livestock Incentive Scheme 1976) and later through a system of Supplementary Minimum Prices in 1978. At the time some Producer Boards (Dairy, Apple & Pear, and Kiwifruit) served as single desk export sellers and directly affected prices received by farmers. Other boards (Meat, Wool) did not act as single desk sellers but supported their sectors with promotion and licencing arrangements. Also in 1976 a revised Producer Board stabilization scheme for meat was established to join the schemes already in place for wool and dairy products. The schemes were financed through accounts with the Reserve Bank at a concessional interest rate of 1%.The overall effect of the policy environment was for farmers to expand production of traditional products with little regard for cost or marketing. The processing and servicing sectors managed to capture a significant share of the government support.

In its drive for increased agricultural output the Government paid subsidies on fertilizer and lime, major inputs on New Zealand grassland farms, compensated for natural climatic disasters and in addition it subsidized the use of land and capital. The Land Development Encouragement Loans Scheme of 1978 encouraged the intensification of pastoral land and the development of marginal land in an unsustainable economic environment. Cheap subsidized interest rates and taxation advantages encouraged farmers to borrow unrealistic amounts of development finance and eventually precipitated a debt crisis.

By 1984 agriculture in New Zealand had become highly dependent on government support – equivalent to 30% of its total output (Appendix II) This level had been growing inexorably for more than a decade and had distorted the economy. Farmers had followed internal price signals even though at variance international ones. They had developed marginal land and pushed tax loss farming to its limits, and used excessive amounts of fertilizer. The processing and service sectors had become less efficient and the generous levels of government support were capitalized into the value of land creating a farm debt problem. New Zealand agriculture had lost its international competitiveness, a very dangerous situation for a country that exports approximately 80% of its agricultural output, especially when that output contributes more than 50% of merchandise exports. Something had to give and it did. The government changed and with it a new market driven philosophy becoming the ruling economic policy. A 20% devaluation was followed by a floating of the NZ dollar and significant changes in taxation policy. Agriculture along with the finance sector took the major hits and went through a 5 year period of “cold turkey” recovery from Government assistance. The latter half of the 1980’s was devoted to a restructuring of the whole economy that has been well recorded in the literature. It was the period of “no gain without pain”. It led a decade later to a radical change of political representation system.

In the context of this paper – Government Intervention in N.Z. Agriculture, the period 1882 to 1972 was dominated by Government support for land settlement as the colony developed to be followed by measures to stabilize product prices through the 1930’s. Following World War II agriculture was increasingly relied on to support the development of manufacturing in an increasingly dual economy. That economy received a double shock in 1972 with Britain’s entry to the EEC and the “ Oil Shock” that followed shortly after. Direct subsidies to farmers became a growing part of their annual income so that by 198 the overall PSE figure had reached 34% on average and 90% on sheepmeat. The political and economic changes of the mid 1980’s were, dramatic and necessary, to stop farmers mainlining on the drug of Government support. Twenty years later the farmers would not want to return to the pre 1984 situation, they prefer the environment of clear price signals from the international food market and they have become accustomed to dealing with the vagaries of that market.