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Prosperity for All?

Economic, Social and Political Change in New Zealand Since 1935

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The rise of Keynesianism and the post-war Keynesian consensus, 1935–72: 'Steady does it'

Introduction

In previous chapters, we considered the post-war long boom and its collapse in the mid-1970s, the major structures of social inequality, and the shifting balance of power between the dominant capitalist class and the working class majority of New Zealanders. Having analysed the changing social and economic context for politics and policy-making in Part I and Part II, we are now able to focus, in Part III, upon the rise of Keynesianism, the post-war Keynesian consensus, and the shift from Keynesianism to neoliberalism and the Third Way.

The account of New Zealand's political history since 1935 that forms the core of Part III examines the marked contrast between the economic, social and political conditions prevailing before and after the shift from Keynesianism to neoliberalism. Whereas the 1950s and 1960s were characterised by economic prosperity and political stability, the period from the late-1960 onwards has been characterised by political instability and, from the mid-1970s onwards, both economic stagnation and political instability. Specifically, this chapter focuses upon the epoch of prosperity and stability that emerged from the poverty, stagnation and instability of the Great Depression. It describes the First Labour Government's implementation of social democratic Keynesian policies from 1935 to 1949, explains why these policies helped the economy to recover from the Great Depression, identifies the central elements of the post-war Keynesian consensus, and explains the political stability that prevailed during the 1950s and 1960s.

5.1 The rise of Keynesianism, 1935–49

The New Zealand Labour Party (NZLP) was essentially a product of working-class political activism. It was formed in 1916 by a joint conference of the Social Democratic Party, United Federation of Labour, and the Labour Representation Committees, 'for the purpose of consolidating the political forces of labour' (Gustafson, 1980, p.92). The immediate background to the party's formation was the upsurge of industrial class struggle from 1908 to 1913 that not only 'was decisive in the making of New Zealand's working class', but was also crucial in breaking up the 'Lib–Lab coalition' that had previously wedded working class voters to the business dominated Liberal Party (Olssen, 1988, p.220). This struggle had culminated in the formation of the militant Red Federation of Labour that in July 1913 'summoned a "unity conference" ... from which emerged two new organisations, the Social Democratic Party and the United Federation of Labour. Together they were intended to unite the workers, the one in politics and the other in industry' (Richardson, 1992, p.215). The conference was only partially successful, since many industrially and politically moderate delegates left the conference and refused to join the Social Democratic Party. However, growing working-class discontent during World War I pushed the moderate and militant wings of the labour movement together in order to form the NZLP. Henceforth, the NZLP and the Federation of Labour were respectively the 'political and industrial wings' of the labour movement.

During the first four decades of its existence there is no doubt that the NZLP was predominantly, though never exclusively, a working-class party. This is clear from its electoral support, which was disproportionately concentrated in urban working-class suburbs, the predominantly working-class composition of the party membership, the working-class origins of party activists and leaders, the strong formal and informal links to the union movement, and the reliance upon the unions and working-class supporters for the funds that the party needed in order to function (Chapman, 1992; Gustafson, 1980; Richardson, 1992). However, despite the revolutionary politics of some within the early Labour Party, the bulk of the party was from the outset committed to reforming the capitalist system in the interests of workers, rather than transforming it in a revolutionary manner. Hence it was a pro-capitalist workers' party, that is, a party with a working class support base, nonetheless committed to managing and maintaining the capitalist system.

Although electoral support for Labour had increased sufficiently for it to rival Reform and the Liberals during the 1920s and early 1930s, it was disadvantaged by an electoral system in which 'an artificial weighting supplied by the "country quota" produced eight more country seats than would otherwise have existed' because rural electorates contained an average of 18 per cent less eligible voters than urban electorates (Chapman, 1992, p.354; Johnston, 1992, p.41). This meant that Labour needed a substantial degree of electoral support in rural electorates in order to win a general election. The onset of the Great Depression after the Wall Street crash in 1929 led to a collapse of the prices for New Zealand's main agricultural exports, and a corresponding decline in farm incomes; 'from 1929 to 1931, export receipts fell by 37 per cent' (Hawke, 1985, p.127). Many small and middling farmers became disillusioned with the economic management of the Reform and United (formerly the Liberals) Coalition Government from 1931 to 1935, in congruence with similar sentiments among working and middle-class voters in the cities. Accordingly, in the 1935 election 'the biggest rise in votes for

Labour candidates came in the seventeen seats dominated by farmers. There the gain was a massive 24.2 per cent of all qualified to vote' (p.354). Labour won the election with 46.1 per cent of the vote and 66.3 per cent of the seats in Parliament (Harris, 1992, p.6). Indeed, it 'won a majority of seats over National in every class of electorate except the richer city electorates and pure farmer seats, and stood as the victorious party in both city and countryside: it had achieved the consensual basis necessary for reshaping society and the economy' (Chapman, 1992, p.354). Labour became the dominant party of government throughout the middle of the twentieth century.

The First Labour Government, 1935–49

The 1935 election marks a crucial turning point. The neoclassical economic policies of the conservative Coalition Government, centrally involving a three-fold commitment to maintaining low inflation ('the soundness of money'), balancing the budget, and free trade (at least within the British Empire), had evidently failed to drag the economy out of the Great Depression and the resulting austerity measures and unemployment undermined the confidence of workers, the unemployed and small farmers in the capitalist social order.[1] The First Labour Government was swept to power on the basis of an electoral alliance between the poorer 'working farmers' and the working class. It then rapidly implemented a comprehensive social democratic Keynesian program of reform in the areas of economic management, social policy, and industrial relations.

Throughout the Great Depression, the Coalition Government pursued a deflationary policy in order to 'balance the budget' (Condliffe, 1959, pp.37–42). As Martin observes, 'from a peak in 1925, government revenue had, by 1933, decreased by a total of 6 million pounds, or one-third of the total' (1981, pp.36–7). It then reduced government expenditure by five million pounds during the same period. Civil service salaries were cut by 10 per cent in 1931, shortly followed by a 10 per cent cut in private sector wages by order of the Arbitration Court and, in the wake of the collapse of national awards which meant that 'employers could impose wages and conditions as they liked', there was a further round of wage cuts (p.39). There was a major reduction in expenditure on public works, such as railways, roads, and public buildings. Old-age pensions and family allowances were cut, as were the rates of pay for relief work.

During the same period that the Government was cutting expenditure, it introduced measures to increase taxation revenue. A special regressive flat tax on all employed men was introduced to cover the costs of unemployment relief, income tax was increased, and additional revenue was generated 'by postal charges, raising customs and excise duties on such articles as tea, sugar, tobacco, beer, and petrol and by additional stamp duties' (Condliffe, 1959, p.38). In 1933, a 5 per cent sales tax was introduced. As Condliffe observes, 'While taxation was high, the graduation of income-tax was not steep and corporate taxation was not heavy. The result of depression financing therefore was regressive. A greater share

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1992
Student loan scheme introduced

... policy of more or less free ...nt allowances to a situation ...es and student allowances are ...ed above, the Fourth Labour ...1250 per annum for 1990 and ...tiary educational institutions ...me students (EFTS) and the ...National Government retained Labour's EFTS-based bulk funding and introduced its 'Study Right' scheme for tertiary education in 1992. The universal allowance that had been available to students under 25 for five years of study was replaced by a tightly targeted allowance, available for three years of study, to those commencing their studies under 22 years of age, subject to their parents' combined income being $27 872 or lower (in 1998). The allowance abated at the rate of 25 cents per dollar of parental income above this very low level of income. Single students over 25 and living away from home receive the equivalent of the unemployment benefit. However, 'because of the tightly targeted nature of the policy regime, only about a third of enrolled students are eligible for these forms of assistance' (p.200).

National had promised, in writing, before the election to abolish Labour's tertiary fee and did so superficially in 1991. However, it cunningly allowed universities to set their own fees and then proceeded gradually to reduce funding per student, thereby effectively forcing universities to raise their fees. In this respect, real expenditure per full-time student (EFTS) was reduced by nearly 10 per cent between 1992 and 1997, and by the late 1990s the level of funding per student was down to 75 per cent, compared with close to 100 per cent in the mid-1980s (p.201). Furthermore, 'whereas public expenditure on tertiary education was around 2.2 per cent of GDP in 1991, by the mid-1990s it had fallen to around 1.5 per cent' (p.201). This led to a corresponding rise in tuition fees to between $2200 and $3000 per annum for most university degree programs by the late 1990s.

A student loan scheme was introduced to replace the universal living allowance that had been available up to 1991. Subject to their own and parental income, students were able to borrow to pay their tuition fees; up to $1000 for course-related expenses such as textbooks, and $150 per week for living expenses. By 1997, 230 000 people had student loans, of whom 100 000 were still borrowing. Of those students who were eligible, approximately half borrowed money under the scheme. A significant real interest rate applied to student loans (for example, in 1998 the interest rate was 8.0 per cent while the inflation rate was 1.3 per cent). Repayment had to commence immediately and was through the taxation system at the rate of 10 cents in the dollar for income above $14 716 per annum. It is

1974
Accident Compensation scheme established

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in 1996 than it had been in 1989' (pp.140–1). The generalised underfunding of health services forced the CHEs into debt as they borrowed money in order to keep operating. In 1994 the Government announced a small increase in funding, but the CHE deficits continued to grow. So too did surgical waiting lists, forcing increasing numbers to use the private system for elective surgery. However, the increased demands on the private system 'led to an increase in private insurance premiums, particularly for the elderly and other high-risk groups', which resulted in 'private insurance as an alternative to public provision ... becoming increasingly inaccessible, especially for those most in need' (p.145). There is little evidence that these reforms generated increased 'efficiency', and strong evidence that it increased the costs of the managerial bureaucracy at all levels of the health system. Finally, whereas the Area Health Boards had been at least partially elected bodies, the RHAs and HFA were entirely appointed by government, undermining the democratic accountability of both funders and providers to the people reliant on public health services.

The Accident Compensation scheme (ACC) was established in 1974 'to replace an ad hoc, unfair, expensive and litigious approach to accidents' with a 'comprehensive entitlement for all accident victims to compensation without the need for recourse to the courts' (St John, 1999, p.54). It involved a 'social contract' in which workers gave up the right to sue in return for comprehensive accident compensation. Initially the scheme was generous, providing compensation set at 80 per cent of weekly income prior to the accident, as well as covering all medical and rehabilitation costs, and lump-sum payments set independently of income for 'loss of faculty, pain, suffering and loss of enjoyment of life' (p.158). Financial pressures on the scheme started to mount as the number of people receiving long-term compensation for incapacity grew, high levels of unemployment made it difficult for recipients of compensation to re-enter the workforce, and as employers successfully lobbied pro-business governments to cut their levies. By 1997, ACC expenditure had reached \$1.6 billion or 1.7 per cent of GDP, making it a significant component of the welfare state.

The vigorous lobbying efforts of the NZEF and NZBR persuaded the Government to push through major cuts to the scheme in the Accident Compensation Insurance Act 1992. It shifted the premiums for non-work accidents from employers to workers, eliminated the lump-sum payments that were important for those on low incomes or out of the paid workforce prior to their accident, abolished the Accident Compensation Appeal Authority, and introduced a new 'independence allowance' to compensate for the costs of living with a disability at the rate of \$40 per week (increased to \$60 in 1996). Large employers were allowed to opt out of the scheme. During the remainder of the 1990s employers' levies were cut further, and workers' levies were increased. In 1999, the Government privatised the scheme. Every major change to the scheme from 1984 to 1999 was actively promoted by employers, leading St John to conclude that 'the short-term financial interests of the employers are driving the reforms, to the detriment of society as