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Wolfgang Kasper\*

## Right to Work: Job Creation New Zealand Style

*Between 1984 and 1994, successive New Zealand governments – first of the left, then of the right – managed the most dramatic and comprehensive deregulation exercise of any OECD country in decades. What have been the effects of this on the labour market?*

The Employment Contracts Act (ECA) of 1991 was an integral, though belated part of the deregulation strategy.<sup>1</sup> The ECA placed New Zealand labour markets on completely new institutional foundations. On the assumption of unequal power between the suppliers and the hirers of labour, successive New Zealand governments had heavily intervened in the freedom to contract labour services, ever since a Fabian minister had pushed the Industrial Conciliation and Arbitration Act through parliament in 1894. For nearly one hundred years, unions were given special privileges in exchange for the promise to give up their right to strike. Wages were fixed centrally. In short, the work relation was taken out of the purview of the common law and the market. The promise not to strike was, however, frequently ignored by those unions that had “hold-up leverage”,<sup>2</sup> because they handled large chunks of capital and/or because the products of the industry were protected from international competitors. The centralised award system was underpinned by fairly strong popular support for “outcome-egalitarianism” and a belief that central intervention in economic life indeed has only the intended effects and no contrary long-term side effects.

Since the onset of economy-wide reforms in 1984, the prop-ups of the traditional award system fell – one after the other – by the wayside. The key elements of New Zealand’s economic reforms, which were in essence put in place in two waves of consistent

deregulation (Labour, 1984-87; National 1991-93), were:

□ A resolute liberalisation of international trade and payments brought indirect international competitive pressures to bear on New Zealand job markets. Concurrently, subsidies to industry and agriculture were eliminated and many domestic markets were deregulated, reinforcing competitive discipline on labour from product markets. However, the Labour government felt it could not deregulate the heavily unionised, centrally controlled labour “market”. Indeed, labour was re-regulated out of concern that workers needed to be protected from the assumed adverse consequences of general deregulation. Predictably, profits were squeezed and rising unemployment ensued. Eventually, these unintended consequences made job deregulation under the Employment Contracts Act of 1991 “politically realistic”.

□ The constitutional commitment to price-level stability by the newly independent Reserve Bank of New Zealand (enshrined in the Reserve Bank Act of 1989) put greater pressure on the fiscal arm of macroeconomic policy and paved the way for an overdue budget consolidation by the National government post-1990. The Fiscal Responsibility Act of 1994 – the third leg in the central triad of NZ constitutional reforms – made governments more accountable, applied the same accounting rules to government which parliament demands of business (i.e. not only an account of receipt and expenditure

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<sup>1</sup> L. Evans et al.: Economic Reform in New Zealand 1984-95: The Pursuit of Efficiency, in: Journal of Economic Literature, 1996, Vol. xxxiv, No. 4, pp. 1856-1902.

<sup>2</sup> O. Williamson: The Economic Institutions of Capitalism, Free Press, New York 1985.

flows, but a fully audited balance sheet) and entrenched rules that make for small, transparent government and hamper parliamentary opportunism and rent-seeking.<sup>3</sup> As a result, government lost the last remnants of capability for fiscal and monetary job-creation in the Keynesian style.

The sequence of reforms may not have been what academics might advise. The New Zealand policy approach was to grasp political opportunities wherever they appeared so as to push deregulation forward – combined with resistance to backsliding.<sup>4</sup> This was based on the hope that complementary institutional arrangements would sooner or later inevitably have to be made in order to bring the areas into line where political resistance to change is great. Military scholars would probably term this procedure an “indirect strategy”, i.e. to conquer terrain where this is feasible with an economy of effort, trusting that the fortresses will eventually fall, too. To convey the pragmatic can-do spirit of the reforms let me cite Sir Roger Douglas – the pioneering reformer in the first Labour government – on sequencing, the hobby-horse of neoclassical economists:

“A great deal of technical debate has been aired worldwide about the optimum sequencing of structural reform. At a purely analytical level the debate is entertaining, but no clear-cut messages emerge. Moreover, from my point of view as a practitioner, the question is irrelevant. Before you can plan your perfect move in the perfect way at the perfect time, the situation has already changed. Instead of a perfect result, you will have a missed opportunity.

Some decisions take full effect the date they are made. Others take two to five years’ hard work before they can be fully implemented. Perfect sequencing is just not achievable. If a window of opportunity opens up for a decision or action that makes sense in the medium term, use it before the window closes!”<sup>5</sup>

Another long-standing, though less visible prop that had supported the dirigiste approach to labour markets had been a statist-collectivist intellectual climate and the pervasive adherence of academics and officials to “know-all neoclassical economics”.

This came under challenge in the wake of the Thatcher and Reagan changes and the advent of economic analysis in the evolutionary, Austrian mode.<sup>6</sup> A small elite of Treasury and business economists undermined the ideological underpinnings of top-down guidance and focused attention on the need to create simple, stable, non-discriminatory rules that give private, self-responsible operators confidence and the capacity to make the best of a complex, evolving economic system. The conclusions from chaos theory – that one should not interfere with complex, open systems for fear of unforeseen, unintended side effects, which the *intelligentia* readily adopted for eco systems and human medicine – also began to be accepted for the complex, evolving economic system. Academic economists and industrial relations experts have opposed this intellectual sea change, but their influence has greatly decreased in New Zealand.

### Codifying the Freedom to Work

The Labour government’s treatment of public welfare, budget cutting and labour markets as holy cows produced massive job destruction towards the end of the 1980s. Unemployment stood at near 11% in 1990 when the conservative opposition (the National Party) campaigned – amongst others – with an Employment Contracts Bill that promised the freedom to compete for labour and for jobs, as well as the freedom of association (or non-association). They won the election resoundingly and promptly proceeded to implement moderate welfare reform and resolute budget consolidation; and, by May 1991, the Employment Contracts Act had become law.

The ECA made the following institutional innovations:

- ☐ It allowed the contracting parties to choose the type of employment contract and gave the contracting parties (almost entire) freedom to determine what terms their contracts should cover.
- ☐ Membership in unions or other associations was to be voluntary; restrictive practices such as closed shops were now prohibited.

<sup>3</sup> R. Richardson: *Making a Difference*, Shoal Bay Press, Christchurch 1995, pp. 162-171 and 234-243; G. Scott: *New Zealand’s Fiscal Responsibility Act*, in: *Agenda*, 1995, Vol. 2, No. 1, pp. 3-16.

<sup>4</sup> R. Douglas: *Ten Principles of Structural Reform*, in: *Policy*, 1990, Vol. 6, No. 1, pp. 2-6.

<sup>5</sup> *Ibid.*, p. 4.

<sup>6</sup> For example, W. Kasper et al.: *Australia at the Crossroads*, Harcourt Brace Jovanovich Sydney-New York 1980; W. Kasper: *The Destruction and Creation of Jobs*, Australian Institute of Public Policy, Perth 1985; P. Brook: *Freedom at Work: The Case for Reforming Labour Law in New Zealand*, Oxford University Press, Auckland 1990; R. Epstein: *Liberating Labour – The Case for Freedom of Contract in Labour Relations*, Centre for Independent Studies, Sydney 1991.

☐ The negotiating parties were given the freedom to use agents of their choice, with agency having to be fully contestable.

☐ It facilitated bargaining at the individual workplace level, rather than bargaining for big, anonymous groups at industrial or occupational levels covering multiple work sites, as had been the case before.

☐ However, it restricted the freedom to work by giving all workers and staff asymmetric rights under comprehensive provision for arbitration in cases of personal grievances through Employment Tribunals and an Employment Court, raising the transaction costs of dismissal.

The ECA liberated employers as well as workers to a greater extent than what is, for example, currently customary in the United States. New Zealand workers are now free to contract their labour, subject to very few constraints, such as a minimum wage.<sup>7</sup> New Zealanders are now able to negotiate singly or in groups through appointed agents, such as elected worker representatives, hired specialist agencies, or trade unions. The agents require explicit, written authority for each negotiation round. Contracts are generally subject to the common law on contracting. For example, work has to be delivered during the contract period. Only after the end of the contract period are strikes and lock-outs permitted – exit options that exist in other contracts as well. Unions certainly no longer have a monopoly in representing workers, as had been the norm before the ECA.

Government now does not interfere in what consenting adults wish to do with regard to wage rates, periods of notice, severance pay, work periods, conditions for shift work, holiday arrangements or job-specific health and safety conditions (other than those fixed by legislation). Employment contracts have to spell out how employees will proceed in conflicts with

employers (there is a non-obligatory standard clause which can be altered by mutual agreement).

Where contract conditions are violated, specialist labour courts may be appealed to by employees, either the lower-level Employment Tribunals or the Employment Court.<sup>8</sup> Appeals against the verdicts of specialist courts can be lodged in the general courts of the land (and have then been frequently overturned). In the final phase of legislation, a general personal grievance provision for employees had been written into the ECA. In practice, this considerably raised the obstacles to firing. Privileges were extended to workers which employers do not have, from previously 400,000 to 1.7 million people.<sup>9</sup> In the hands of the long-serving judges of the Employment Court, who were imbued with the principles of the traditional, power-based industrial-relations system, this became a considerable new limitation of the freedom to hire and fire.

It is central to understanding the effects of the ECA that it was an integral part of a comprehensive liberalisation strategy in which there have so far been very few reversals. As the reforms progressed, the sub-orders governing product, capital and labour markets were eventually made mutually consistent again, so that the new rule system – what one might call the new economic constitution of New Zealand – is now stable and effective.<sup>10</sup>

### The Opponents' Predictions were Wrong

The Employment Contracts Bill had been controversial during the election campaign of 1990,

<sup>7</sup> Adults have to be paid a minimum of 40% of the average wage, youths between 15 and 19 years 60% of the adult minimum. In March 1997, the new conservatively-led coalition government mandated a higher adult minimum wage of NZ \$ 7.00 per hour, not much below the US minimum wage, where average real incomes are 50% higher. The youth wage has been raised to NZ \$ 4.20 per hour; see D. M. Bradford: What Happens Now? – Keynote Address to the Annual Industrial Relations Conference, Wellington, 3 March 1997, mimeo. It has been argued that the minimum wage for youth hampers job creation and the entry of inexperienced youngsters into the best training scheme available, namely being part of a work team; ACIL Economics and Policy: What Future for New Zealand's Minimum Wage Law?, Canberra 1994, mimeo; J. Sloan: Towards Full Employment in New Zealand, New Zealand Business Roundtable, Wellington 1994. Other constraints of the freedom of contract are the stipulation of a minimum of three weeks' leave and eleven paid public holidays per annum, paid sick leave, equal pay for women and men, a right to unpaid maternity leave, job protection for defence-force volunteers and special protection against illegal deductions from wages.

<sup>8</sup> The Employment Court, staffed with the special-case judges of the old industrial-relations era have often tried to go against the spirit of the ECA, for example in making dismissals harder. This has led to the most severe criticisms of the new-era labour-market constitution. C. Howard: Interpretation of the Employment Contracts Act 1991, New Zealand Business Roundtable, Wellington 1995; B. Robertson: The Status and Jurisdiction of the New Zealand Employment Court, New Zealand Business Roundtable, Wellington 1996; C. W. Baird: The Employment Contracts Act and Unjustifiable Dismissal, New Zealand Business Roundtable, Wellington 1996; C. W. Baird: The ECA: Almost a Model for the World, 19 March 1996, mimeo; W. Kasper: Free to Work: The Liberalisation of New Zealand's Labour Market, in: The Fraser Institute: Right-to-Work Laws: The Global Evidence of their Impact on Reducing Unemployment, Vancouver 1997.

<sup>9</sup> D. M. Bradford, op. cit., p. 8.

<sup>10</sup> Since the Fraser Institute has just published my more detailed analysis of the ECA and its consequences, I can confine myself here to a fairly short summary of its provisions. See W. Kasper: Free to Work, op. cit. Before proceeding, however, I wish to assert that none of the other recently published analyses have changed my original major assessments in: W. Kasper: Free to Work – The Liberalisation of New Zealand Labour Markets, Centre of Independent Studies, Sydney-Wellington 1996; and W. Kasper: Responsibility and Reform – a Conversation with Ruth Richardson, in: Policy, Vol. 12, No. 3, pp. 25-31.

but this did not prevent a landslide win for the Nationals who had campaigned with it when most prop-ups for regulated labour markets had either already been done away with or were about to fall.

The Employment Contracts Bill was even more controversial after the election. Unions, churchmen, academics, industrial relations experts, and welfare lobbyists agitated publicly against the Bill, combining this with vocal opposition to the concurrent social-welfare reforms. Leading figures (including a few business representatives) put their names to a number of dire predictions: real wages would fall; new jobs would be of low quality and part-time to suit employers; anarchy, strikes and confrontation would break out; "gangster unionism" would spread; unemployment would rise, especially among women and young people; work place democracy would be suppressed; employers would be unable to calculate their costs beforehand, and discontinuities would disrupt business. The Council of Trade Unions feared widespread abuses by employers and set up an emergency telephone "sweatline" for aggrieved workers.

Without exception, these predictions turned out to

be wrong.<sup>11</sup> The "sweatline" soon lapsed for lack of demand. Most definitely, New Zealand did not return to (what some depicted as) the 19th century workplace – on the contrary:

□ Average real wages, though hard to measure, have on average risen slowly. Admittedly, 10% of individual wages were initially reduced, but numerous pay packets were increased to reflect productivity deals. After many years of "judicial levelling of wages", the wage structure has become more diversified and now reflects rewards for higher skill levels. This has committed many workers to skill acquisition.<sup>12</sup>

□ Strike activity dropped to near zero. Most new wage contracts are now settled with a minimum of fuss and transaction cost. Wage structures have been simplified. After the highly politicised posturing by union and employer apparatchiks during the centralised wage-fixing rounds before 1991, work disputes and industrial relations have faded from the headlines and the political agenda.<sup>13</sup>

□ Employment has risen by about 240,000 (i.e. by nearly 20% or 4½% p.a.) since 1991. Medium-term forecasts are for continued solid rises. It is probably futile to attribute these job increases to single factors at a time of system-wide institutional reform, but Maloney<sup>14</sup> made a valiant econometric attempt to allot job creation to various proximate causes such as the ECA and the drop in unionisation which it facilitates.

□ Unemployment in New Zealand during the strong cyclical upturn from mid-1991 to early 1996 fell overall from nearly 11% to below 6%, much faster and by

<sup>11</sup> See W. Kasper: *Free to Work ...*, 1997, op. cit.

<sup>12</sup> Ibid.

<sup>13</sup> R. Kerr: *Obstacles to Employment and Productivity Growth in New Zealand's Labour Market*, Institute for International Research, 11th Annual Industrial Relations Conference, Auckland 1997, mimeo.

<sup>14</sup> T. Maloney: *Does the Adult Minimum Wage Affect Employment and Unemployment in New Zealand?*, Auckland Working Papers in Economics, No. 137, 1994, Department of Economics, University of Auckland, mimeo.

Bernhard Duijm

## Die Wettbewerbspolitik der EG gegenüber vertikalen Vertriebsvereinbarungen

This book analyzes the policies of the European Commission concerning vertical distribution agreements from an economic point of view.

1997, 219 pp., hardback., 64,- DM, 467,- öS, 58,- sFr, ISBN 3-7890-4672-8

(Integration Europas und Ordnung der Weltwirtschaft, Vol. 15)



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more than during the comparable upturn in Australia<sup>15</sup> and much more than in previous New Zealand upturns.<sup>16</sup> In the 1996-97 cyclical "growth pause", New Zealand unemployment did not rise again (different from Australia with its more regulated labour markets).

☐ Three quarters of the new jobs are full-time.

☐ Far from being to the detriment of certain classes of people who are sometimes designated as "socially disadvantaged", the new labour law led to disproportionately large falls in the (high) specific unemployment rates of Maori and immigrants from the Pacific Islands, of long-term unemployed, and young people. Many of the young now manage to get into the best job-training scheme yet invented: being part of a functioning work team. The long-term unemployed, who made up half the total in 1992, now account for only a quarter of the number of those without a job. These effects happened early, i.e. before the first labour shortages came about in high-activity centres such as Auckland. They owe much to the ECA, but also much to less generous public welfare.<sup>17</sup> Analyses by the NZ Treasury confirm that the most effective escape from poverty is a job, even if the initial wage is low. About one quarter of the most poorly paid 20% of workers moved to a higher income bracket within a year, and there is evidence that workers on low wages have achieved wage increases by larger percentages than better-paid workers.<sup>18</sup>

☐ The predicted disruption of business and the unpredictability of wage contracts failed to materialise. On the contrary, business managers now had to speak more directly to their workers, and managers (and workers) became better informed about the ongoing evolution of their businesses. People felt a sense of empowerment when uniform dictates handed down in distant places gave way to direct negotiations. The climate in many workplaces improved, and many productivity reserves were mobilised in exchange for corresponding wage premia. This is not only documented by case studies,<sup>19</sup> but also by opinion surveys. Whereas the ECA had initially been opposed by a 2:1 margin in some opinion surveys conducted during 1991 and

1992, the majority of New Zealanders now approves of the new workplace freedom. A representative opinion survey five years after the ECA came into force showed that 41% of 1000 surveyed New Zealanders approved, or strongly approved, of the ECA and only 24% disapproved. Similar percentages saw positive effects on the general economy.<sup>20</sup> The approval of the ECA in general had thus grown, but was nevertheless still mixed. However, great majorities of employees found that the ECA had affected them personally in more positive ways: over 3/4 of respondents were satisfied or very satisfied with their own terms and conditions, their own job security and their own bosses. 85% said that they now feel high or very high job satisfaction. It seems that long-held general beliefs colour general responses more than recent personal experiences and that many still consider the benefits of liberalisation a matter of personal good fortune, not of general, systematic improvement.

☐ More than 3/4 of surveyed New Zealanders now want direct employment and wage negotiations with their employer. Only 21% favour negotiations between unions or through other intermediaries whom workers cannot control directly.<sup>21</sup> In practice, groups of workers normally elect spokesmen to negotiate on their behalf or engage agents, at times former unionists who had lost their jobs. This reduces information and other transaction costs. The essential difference to the old union system is that the workers now determine the negotiation strategy. Control has moved from union officials to the workers who can hire and fire their agents. The empowerment workers feel under the ECA becomes apparent in much casual evidence.

☐ In the 1996 general election, some political parties (Alliance, Labour) campaigned, amongst other things, with the promise to repeal the ECA. They lost the election, as 60% of the electorate voted for parties

<sup>17</sup> The New Zealand Treasury has estimated that the increase in the differentials between household incomes from employment and incomes from social welfare since 1991 has raised labour-force participation by 2%; increased total employment numbers by 2.5%; reduced unemployment by 0.7 of a percentage point; and induced more young adults to participate in education and training; see R. Kerr, *op. cit.*, p. 4.

<sup>18</sup> *Ibid.*, p. 5.

<sup>19</sup> W. Kasper: *Free to Work ...*, 1997, *op. cit.*

<sup>20</sup> National Business Review: New Zealanders Back Labour Reforms, 16 Feb. 1996, pp. 1 and 22-23. (Press report about an MRL Research Group opinion survey), here p. 23.

<sup>21</sup> *Ibid.*

<sup>22</sup> *Ibid.*

<sup>15</sup> W. Kasper: *Free to Work ...*, 1997, *op. cit.*

<sup>16</sup> V. Hall: Economic Growth, in: B. Silverstone, A. Bolland and R. Lattimore (eds.): *A Study of Economic Reform: The Case of New Zealand*, North Holland, Amsterdam 1996; J. Yeabsley and J. Savage: What do We Know about the Economic Impacts of the Employment Contracts Act?, address to the Moving Forward Conference Auckland, 15 May 1996, mimeo.

that promised to retain the current system. Under the new electoral system it is unlikely that a coalition will ever be formed that can repeal the ECA.<sup>23</sup>

Have there been any losers? The most noted losses from the new freedoms to work and associate have occurred in union membership, which has gone from fairly high rates due to closed-shop legislation and compulsory union membership in many occupations to US levels, maybe 30% of the workforce. Many union officials lost their jobs and influence. Nonetheless, some unions rose to the competitive challenge and have become service organisations that do their members' bidding, help their members to compete, and even sell services (such as training) to employers. Likewise, the Employers' Federation had to reinvent itself to become an information and service provider to its members, having before been a monopoly negotiator in central wage cases. Other casualties of the liberation of labour have been the industrial relations departments at various universities and the contributions from the union wing of the labour movement to its political wing.

### System-Wide Benefits

The more general effects of the sea change in the New Zealand economic constitution have been that the climate in the work sphere has improved, that raising productivity and the quality of output have become an ongoing game and that New Zealand workplaces have become internationally highly competitive:

□ The 1996 Global Competitiveness Report<sup>24</sup> rates New Zealand as the third most competitive economy out of 44 countries overall (Canada ranks in 8th place). As to the "quality of labour", the Report rates New Zealand second, with top rankings on such criteria as "willingness to accept change", labour costs, labour force restructuring, and ability to avoid the social costs of employment.<sup>25</sup> However, the Global Competitiveness Report also documents residual labour weaknesses in New Zealand, such as limitations to the supply of skilled labour, alcohol abuse, and minimum wage regulations.

□ The Fraser Institute's index of economic freedoms

rates New Zealand as the country with the second highest level of economic freedoms in 1993-95<sup>26</sup> and among the ten countries with the biggest improvement in economic freedom ratings.<sup>27</sup> "New Zealand comes out clearly the leading reformer of the 23 (OECD) countries in both absolute and relative terms", wrote David Henderson, former Head of the OECD's Economics Department, recently.<sup>28</sup>

□ Overall productivity increases (measured at the level of national accounts) became a major point of criticism by the defenders of labour-market dirigisme, once they were no longer able to predict wage reductions and job destruction. Overall labour productivity has risen by 2 per cent per annum during the 1991-96 upswing, and total factor productivity rose by 2.3 per cent (as against 1.3% in previous upturns in the demand cycle<sup>29</sup>). Such relatively slow aggregate productivity increases after reforms are not amazing in an economy that emerges from massive unemployment: New Zealanders have, on the whole, translated the upswing in demand into more employment and modest wage increases, as individually less productive workers were "sucked" into jobs. This (probably welcome) effect of course dilutes average productivity increases. As the economy approaches high employment and as growth moves from a job-extensive to a productivity-intensive mode, average productivity can be expected to increase more rapidly.

□ At the micro level, great productivity advances are being reported, and the business people directly involved attribute much to the ECA (although the other reforms are also crucial). Thus, at a conference of the Australia-New Zealand Business Council in Auckland (22-23 September 1996), one CEO after the other reported great strides in productivity:<sup>30</sup> for example, the privatised railroad now operates with one quarter of the staff before privatisation and has more than doubled its output volume (productivity up 9 times from an admittedly appalling base). The State-owned, but corporatised electricity industry has improved its management of production and distribution capacities to such an extent that the plans

<sup>23</sup> R. Kerr, *op. cit.*, p. 1.

<sup>24</sup> World Economic Forum: Global Competitiveness Report 1996, WEF, Geneva 1996.

<sup>25</sup> *Ibid.*, pp. 106-107. Canada tends to rate between 7th and 30-40th place on labour-market criteria.

<sup>26</sup> J. Gwartney, R. Lawson and W. Block: *Economic Freedom of the World: 1975-1995*, The Fraser Institute, Vancouver 1996, p.xx.

<sup>27</sup> *Ibid.*, p. xxviii.

<sup>28</sup> D. Henderson: *New Zealand in an International Perspective*, New Zealand Business Roundtable, Wellington 1996.

<sup>29</sup> V. Hall, *op. cit.*; J. Savage: *What Do We Know about the Government Impacts of the ECA?*, NZ Institute of Economic Research Working Paper No. 96-9, May 1996.

<sup>30</sup> The conference results were not fully recorded and there is no edited set of the papers presented. I took careful notes and cite from my personal record.

for the construction of one large power plant could be trashed. Since the privatisation of the old telephone monopoly and its exposure to completely open competition in 1990, each employee of NZ Telecom looks after three times as many phone lines as before. As many new entrants in the "lightly regulated" telecom market of New Zealand are learning how to compete properly, telephone costs have fallen by 50% in real terms. The stock prices of NZ Telecom nevertheless keep rising. New Zealand's privatised and competing ports now deal with a standardised basket of loading activities at only 30% of the costs of the same operations in Australian ports (which government-owned, unionised NZ ports surpassed in inefficiency not so long ago). Freighters are turned around on average in 18½ hours, compared to 3½ days in 1988. No wonder that New Zealand is attracting "management pilgrims" from around the world who are interested in efficiency.

□ An important consequence of the new right to work at conditions that you can influence personally is a palpable improvement in satisfaction with the work experience, as documented for example in the surveys cited above. A new commitment to quality and productivity has replaced notorious attitudes to performance that prevailed when distant authorities fixed wages and one was essentially rewarded for simply being at work. Now, the wage is comprehended as a reward for effort, skill and attention to quality. Complicated wage premia for weekend work or shift work have disappeared, but wage premia for human capital have become widespread. This – in combination with cuts in indiscriminate public-welfare provision – has given rise to great increases in training and education demand: people invest in their human capital to succeed in the labour market. One should not underestimate the importance of satisfaction from the work experience, which after all dominates many people's lives, although this does not show up in econometric studies.

### Residual Limitations of the Right to Work

American economist Charles Baird, after studying the ECA, called it "almost a model for the world"<sup>31</sup> – "almost" since the freedom to work is still subject to some artificial regulatory limitations.

The freedom to work and employ is reduced most severely by the provision that workers can claim

personal grievance before a tribunal, which the hold-over Employment Court has interpreted in ways that give asymmetric powers to employees, including for the first time employees in high management positions. In this respect, unemployment contracts differ from the symmetric provisions of other contracts. The grievance privilege has played an important part in dismissals and has raised the transaction costs of dismissal to employers.

Baird<sup>32</sup> found on the basis of US patterns of behaviour that the "unjustifiable dismissal clause" had the effect of a tax on employment that reduces the effectiveness of labour resources, hinders enterprise and business growth, lowers real wages and makes income distribution less equal. He estimated that the lowest quintile of household incomes has been reduced by 18% on average, that real wages are depressed by 7%, and that between 19,000 and 47,000 jobs have failed to materialise.

The statutory obstacles to dismissal were inserted by activist legislators and hardened by activist judges on the Employment Court – which NZ observers sometimes call the Unemployment Court – out of fears that liberalised labour markets might disadvantage (powerless) employees when confronted with (powerful) bosses.

This seems to be based on a complete misunderstanding of the competitive process. Rather, it is based on the model of a power relationship between suppliers and buyers that may apply in monopolistic or highly regulated markets but that is totally misplaced when the freedom of contract and competition reign. At the risk of dwelling on fundamental economic theory, let me state what competition in the labour market – or any free market – is:

□ Each buyer of labour rivals with other buyers, and each seller rivals with other sellers. Workers therefore might need protection from other workers, not the employers! Competitors on both sides of the market incur costs to gain a position which they expect to make themselves attractive contract partners for someone on the other side of the market (for example, sellers of labour incur the costs of investing in their skills to gain a position ahead of other sellers).

□ In competitive labour markets, employers have to incur information and other transaction costs to find the most appropriate contract partner within the bounds of the costs they are prepared to incur. Employers have to make efforts to obtain the workers

<sup>31</sup> C. W. Baird: *The ECA: Almost a Model ...*, op. cit.

<sup>32</sup> C. W. Baird: *The Employment Contracts Act ...*, op. cit.



who offer the skills they can use best, at the most advantageous contract conditions.

The processes of rivalry amongst sellers and buyers and of contracting between buyers and sellers occur concurrently in a dynamic discovery process that we call competition (and that few economic textbooks explain).<sup>33</sup> The sellers of labour under the ECA therefore rival with other sellers, as the new flourishing of skill acquiring demonstrates. They do not rival with "powerful" bosses. As long as there is high unemployment, workers also rival with unemployed people. However, the approach to high employment enhances each worker's competitive position (whereas the labour re-regulation and job destruction under Labour 1984-90 had done the opposite). As high employment levels are reached, the employers have to rival with other employers for the workers that are best suited to their specific purposes. Their power in the market is controlled by the rivalry with other employers. They have to offer attractive, flexible conditions to the workers they want and have to incur information costs to find out what the other side of the labour market really wants. These normal competitive efforts explain the now high personal satisfaction of New Zealand workers with their bosses and work conditions.

Market competition gives both sides the "exit option", the right to hand in a notice or to dismiss. If that option is blocked or hindered asymmetrically on one side of the market, competition can become dysfunctional as a discovery procedure, and the efficiency- and freedom-creating capacity of the free market is abridged. Experience in numerous countries and periods has shown that obstacles to dismissal are not only obstacles to hiring, but also obstacles to the intensive search for the best use of scarce labour resources.

The ECA and related institutional reforms have now proven the job-creation capacity of competitive markets. There are now moves afoot to delete the "unfair dismissal clause",<sup>34</sup> which jars with the general competition rules of the legislation and stems from a

differing mental model of the work relationship. The coalition agreement of the new government spoke critically of "judicial activism" and hinted at terminating the specialist Employment Court.<sup>35</sup> This would move employment contracts fully into the common law of contracts, and apply the simple rules of ownership, contract and tort. The transaction costs of employing people would be reduced and the rules would be more readily understood by everyone (lower compliance and information costs).

Another limitation of the right to work in New Zealand is the minimum wage, which was recently increased (as mentioned). This can be expected to disadvantage low-productivity people, such as inexperienced youths, and to erect barriers to the entry of low-skill people into working life. It is needless to say that minimum prices frequently turn outsiders into disadvantaged groups. Prescriptive populism by ignorant politicians and bureaucrats is, however, alien to New Zealand's current economic constitution. The raising of the minimum wage constitutes a – so far – rare element of backsliding in the reform strategy.

### Conclusion

These residual impediments to an unabridged right to work are only remarkable in the context of the freest, most trust-inspiring economic constitution that the citizens of any OECD country are able to enjoy. They are minor in comparison to New Zealand's past or other OECD countries. However, New Zealander workers and producers are not competing with their past, nor for that matter all that much with other OECD countries. They compete as the inhabitants of one of the "front-line states" with the new industrial countries in East Asia. Workers and job creators there enjoy even greater freedom to work and are less distracted by public-welfare activism. East Asian workers in many places now not only enjoy rapid productivity and wage increases, as their economies reach high employment, but also surprisingly even income-distribution outcomes.<sup>36</sup> Thus, the benchmark for New Zealanders is no longer what may be done in sclerotic labour markets in Europe, but the reality of the not-so-new industrial countries of Asia.

The realisation has indeed spread in New Zealand that Kiwi jobs are competing with jobs in Kuala Lumpur, Shanghai and Seoul – and that jobs in places like Auckland are increasingly successful thanks, on the whole, to the simple, non-discriminatory, and enterprise-and-trust-inspiring institutions which are now governing working life in New Zealand.

<sup>33</sup> For more on this see the article on "German Market Process Theory" and "Competition" in P. J. Boettke: *The Elgar Comparison to Austrian Economics*, E. Elgar, Aldershot 1994, pp. 500-507 and 96-102 respectively.

<sup>34</sup> D. Bradford, *op. cit.*

<sup>35</sup> R. Epstein: *Employment Law, Courts and Contracts*, New Zealand Business Roundtable, Wellington 1996.

<sup>36</sup> J. Riedel: *Economic Development in East Asia: During What Comes Naturally*, in: H. Hughes (ed.): *Achieving Industrialisation in East Asia*, Cambridge University Press, Cambridge 1988, pp. 1-38, here pp. 18-21.