Bernard Hickey: How the foreign profit and interest drain has made us poorer

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The foreign profit and interest share of NZ's economy has risen from 1 per cent of GDP in 1972 to over 7 per cent in 2009. Photo / Thinkstock

Ever wondered why it seems New Zealanders can't ever seem to get ahead despite apparent growth in Gross Domestic Product?

The simple answer is that any growth we saw in the last six or seven years was being gobbled up by either population growth or the ever-growing drain on our economy from profits sent offshore to foreign owners of assets here or interest payments to foreign creditors.

An analysis of the national accounts since the early 1970s shows that the share of GDP accruing to foreigners has risen from around 1 per cent to as high as 7 per cent in 2008.

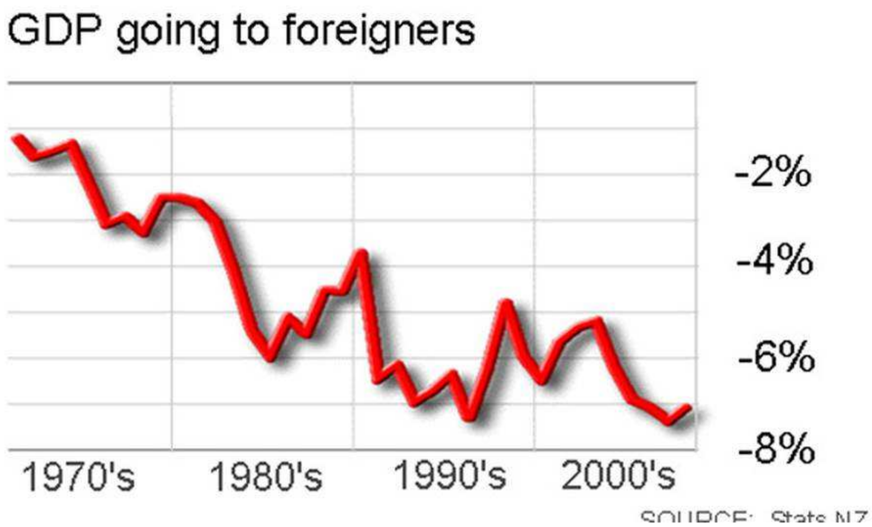
A combination of asset sales to foreigners and increased foreign debt has seen the net investment deficit (it has always been a deficit) rise from NZ$79 million or 1.2 per cent of GDP in 1972 to a record high NZ$13.34 billion or 7.4 per cent of GDP in 2008.

This is referring to dividends sent back overseas to foreign owners or rising values of assets owned by foreigners or rising interest payments on debts owed to foreigners.

This has meant that while New Zealand's total Gross Domestic Product (GDP) has been rising through this period, our Gross National Income (GNI) per capita (which subtracts the earnings sent offshore and accounts for population growth) has been flat to falling since the June quarter of 2005.

After a substantial slump through the 2008/09 recession, GNI per capita is still below where it was the September quarter of 2003.

Chart one shows how the foreign share of New Zealand's income has grown since the 1970s.



The acceleration started in the early 1980s in the final years of the Muldoon government. It reversed itself slightly in the late 1980s before heading lower again through early 1990s as state asset sales and foreign borrowing by banks and others took their toll.

It widened again after the mid 2000s as bank borrowing offshore associated with the property boom worsened the situation.

Those foreign asset sales and the foreign borrowing through the 1980s, 1990s and 2000s are now expressing themselves in a continual leeching of dividends and interest payments that have essentially stalled per capita growth in income domestically.

Essentially, any GDP growth since 2003 has been gobbled up by interest payments and dividends. We are essentially now borrowing to pay the interest on previous debt and the rent on foreign-owned assets. We have passed the point of no return.

Chart two shows how GDP (total national output) has diverged from GNI per capita since the early 1990s. This is partly due to population growth without the associated GDP growth to go with it (due to flat or falling productivity growth), or because of the growing drain from dividends and interest payments.

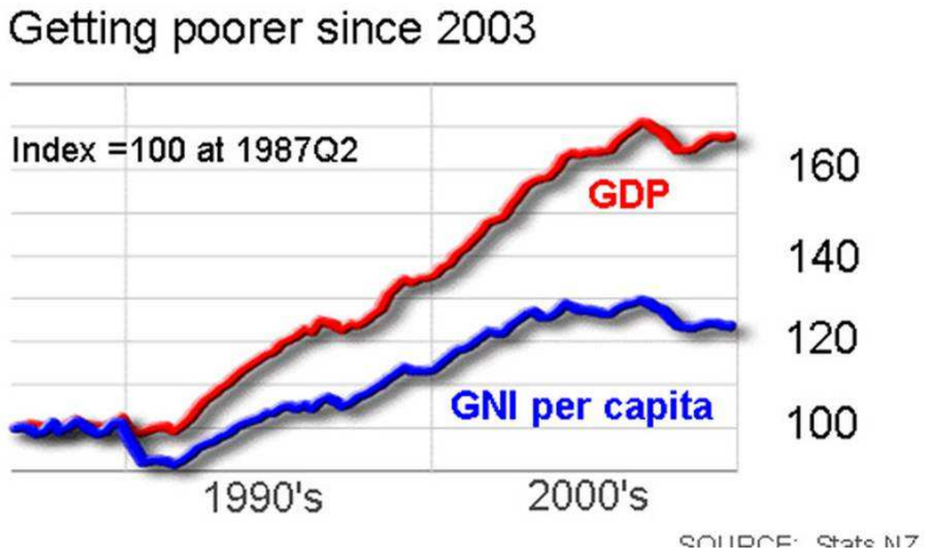
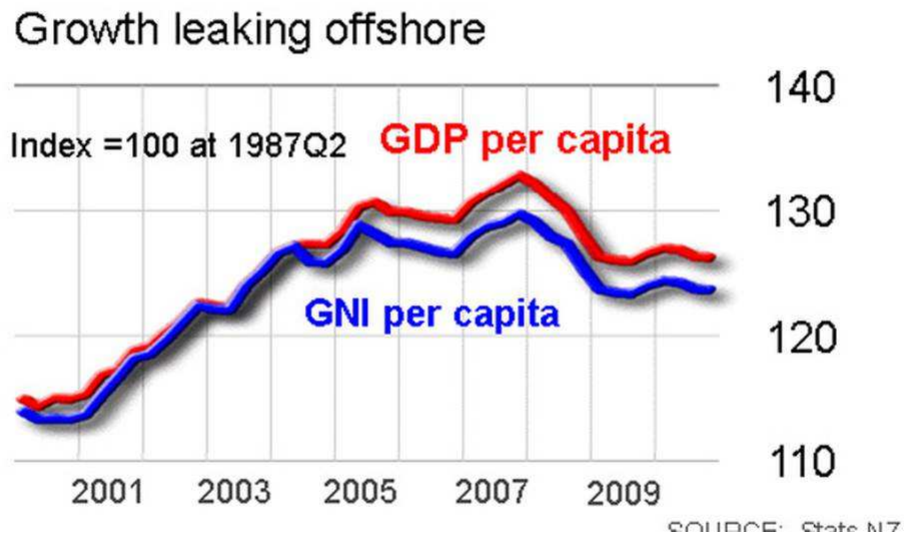


Chart three shows GDP per capita and GNI per capita.



This essentially abstracts out the population growth issue.

It shows a widending gap since 2003.

So what?

So what does this mean for economic policy? What should voters and politicians do with this information?

It shows clearly that New Zealanders have been living beyond their means since at least 2003 and probably earlier. It's clear now that any growth we produce is going offshore to service debts and pay the rent. We are already tenants in our own land.

Since the early 2000s we have been kidding ourselves that we are worth higher incomes and we did it by borrowing even more offshore, firstly through our banks and now through our government.

We withdrew from our housing ATMs from 2003 to 2008 and increasingly since 2005 we have withdrawn from our government ATM in the form of Working for Families payments, interest free student loans and other increases in spending.

So what can and should we do?

Firstly, we have to stop borrowing more. That means turning around the budget deficit much more quickly than the government is planning.

Here's 5 ways in which we could turn around that debt:

- We should also do everything we can to stop selling more assets.

This is difficult because it essentially means either forcibly stopping asset sales or (more sustainably) making sure we generate our own capital surplus.

- That could and I think should involve formal bans on large sales of assets to foreigners.

- We should be very careful during any part privatisation of state assets to ensure they are sold to New Zealanders.

- We should be obsessive about increasing our exports and reducing imports. In the long run this slow slide to penury is a result of consuming beyond our means in a national sense.

If that means venturing beyond the orthodoxy of free floating exchange rates and completely free movements of capital we should do it. Virtually no other central bank or government in the world runs such a laissez faire monetary policy or trade policy.

Thinking the unthinkable

Now for something a little more controversial.

- One solution for getting rid of debts you can't afford to pay is printing money.

This a last resort, but it is not unprecedented and it's something that the leader of the western world (America) is doing right now.

The Reserve Bank could buy these bonds currently being issued by the government and essentially inflate the debt away. That punishes both local savers and foreign creditors (who hold our debt in New Zealand dollars) but it does fix the problem of indebtedness. It would also immediately cause a slump in our currency.

This would have been unthinkable a few years ago.

But when it's good enough for America, maybe it could be good enough for us too.

I welcome your thoughts.