

The Politics of Economic Reform in New Zealand

Daniel L. Nielson

University of California, San Diego

In 1983 New Zealand possessed one of the most economically interventionist and protectionist regimes in the developed world. The government tightly controlled foreign exchange, keeping the New Zealand dollar overvalued. Foreign companies faced high trade barriers and a hostile environment to direct investment. Adding to New Zealand's already extensive welfare state, major new spending and public works programs had thrown the budget into deep deficit. The government produced numerous products and services and pervaded many economic sectors.

In the decade that followed, New Zealand economic policy experienced a virtual about-face. By 1993, the country had passed from its interventionist status to become one of the most open, non-interventionist economies in the Organization of Economic Cooperation and Development (OECD). The changes in New Zealand have been so vast that some analysts, with only slight exaggeration, have likened the transformation to reforms occurring now in countries of the former Soviet bloc.

In addition to the speed and scope of economic adjustment, other facts make the New Zealand reforms even more remarkable. The Labour Party had traditionally championed economic interventionism. Yet it was a Labour government that initiated the reforms in 1984, fighting long-held party traditions. Labour even deepened the adjustments after its re-election in 1987. The changes spawned a vast public outcry at the subsequent economic dislocation and at the six-year recession that the new policies had exacerbated. Voter backlash against the reforms finally helped to propel the National Party—Labour's principal opposition—into office in 1990. Yet, despite public opinion, the National Party followed the course pioneered by their Labour opponents. The following case discussion puts these and other puzzles into their political context.

NEW ZEALAND POLITICAL INSTITUTIONS

The Structure of Government

Like most other former British colonies, New Zealand's political institutions are fashioned on the Westminster model. In fact, New Zealand's political organization is more prototypical of a pure Westminster system than that of Britain itself (Lijphart 1984). New Zealand is a parliamentary system with only two large parties, one of which almost always constitutes the government without need for coalition partners. The parliament is unicameral (there is only one house in the legislature). Unlike Britain, there is no vestigial House of Lords. Local governments have no real control over municipal affairs; provinces were abolished in 1876. Representatives, or members of parliament, are selected by plurality vote—a "first-past-the-post" system, as it is

called in New Zealand—in roughly 100 single-member districts in elections held approximately every three years. In New Zealand, voters can only express a preference for the prime minister and cabinet by voting for their preferred party's candidate in individual districts. Following the almost universal pattern in similar democracies, this system of single-member district plurality voting has resulted in a two-party system. Currently the National Party and the Labour Party dominate the New Zealand polity (Nagel 1994, Gold 1985).

Single-member district plurality voting often lends itself to disproportional representation because the winner in each district takes that district's only seat, regardless of the vote margin. That is, the system often "manufactures" majorities of *seats* in parliament even when no party wins a majority of *votes* due to the small vote shares won by third parties (Taagepera and Shugart 1989). Sometimes the party that takes second place in the popular vote wins a majority of seats and thus wins control of government. For example, in both 1978 and 1981, the Labour Party won a majority in the popular vote, but was denied a majority in the legislature. Labour's votes were highly concentrated in the urban centers, rather than dispersed throughout the country's suburban and rural districts (Bollard 1994). In both elections, Labour won huge vote majorities in urban districts but lost rural seats by slight margins, allowing National to hold onto control of government.

New Zealand does not have a written constitution. Instead, its rules of government encompass a large set of important laws that stretches back to the 1688 British Bill of Rights and the 1297 Magna Carta (Harris 1985). For all practical purposes, the New Zealand parliament is sovereign over constitutional and policy matters. Virtually all legislative actions—from the Human Rights Commission Act of 1977 to the Margarine Act of 1908—have precisely the same status: each can be overturned by fifty percent of the legislature, plus one (Harris 1985). There exists no second house to pass on laws, no executive veto, and no judicial review (Nagel 1994, Bollard 1994, Harris 1985).

The Decision-Making Process

The party in New Zealand with a majority of seats forms the government by selecting out of its ranks a prime minister and a cabinet. The party caucus (the membership of the party in parliament) chooses the prime minister directly. The cabinet consists of roughly 20 ministers who propose and direct legislation pertaining to their respective ministries. Cabinet policy committees, which include a smaller number of key ministers, decide most legislative matters (Bollard 1994). They are advised by bureaucratic department secretaries, who are career civil servants appointed by fellow high-ranking bureaucrats.

Because party leaders control the nomination of parliamentary candidates, they exercise virtually iron-clad party discipline. If a member votes against the party, especially on matters of priority, then that member can be removed as a candidate in the next election. To advance in the party and eventually join the cabinet, individual members of parliament understand that they must vote the party line without deviation. Thus, once the cabinet decides on a matter of legislation, the governing party's back-benchers almost always pass it without opposition when it comes to a

general vote in the chamber. This pattern holds except for those very rare instances where a cabinet decision is so controversial that it provokes a back-bench rebellion.

Because of the New Zealand doctrine of collective responsibility, cabinet members are compelled to support each cabinet decision publicly, even if they disagreed with it in cabinet or policy-committee meetings. If they cannot support a given decision, “they should resign or expect to be dismissed” (Nagel 1994: 21). New Zealand’s rules and practices mean that core government decisions are made by a relatively small group of politicians in the cabinet. These decisions are prone to instability. If the balance within a cabinet changes, even by a few votes, the new dominant cabinet majority can reverse policy. The same holds for the delicate equilibrium between different camps within parties, and between the two largest parties themselves.

In fact, radical policy changes have often characterized New Zealand policy making. At times when the Labour Party has taken office after a period of National Party government, its cabinet’s first acts have entailed overturning core elements of the National policy program. And vice versa. However, two institutional features prevent this instability from cycling into chaotic policy swings. First, as in most two-party systems, both dominant parties are centrist. While each party has its core supporters—workers for Labour, farmers and manufacturers for National—both also compete for the swing voter, who can be swayed to switch parties from one election to the next. For most of the last half century, party leaders in both major parties have pitched their platforms to traditional New Zealand middle class concerns of economic stability, full employment and generous spending on social services and infrastructure.

Second, New Zealand possesses a well-trained and meritocratic civil service. Politicians in the cabinet do not appoint bureaucrats nor do they dismiss them when the party in power changes. This meritocratic norm extends all the way to the level of department head. While the role of the civil service is only advisory, bureaucrats’ training, policy expertise and control over government information often gives them leverage in dealing with politicians. Bureaucrats often draft the initial version of government measures and can affect the legislative agenda. Thus, the civil service’s permanence and influence dampens somewhat the potential for wanton legislative flip-flopping.

THE BACKGROUND OF REFORM

With only 3.3 million people in an area roughly the size of the United Kingdom, and roughly six times more sheep than people, agricultural production clearly dominates New Zealand’s economy. Since the establishment of New Zealand as part of the British empire, the country’s agricultural products had found profitable markets in the mother country. Between 60 and 70 percent of New Zealand’s primary products were sold in the British market with minimal processing, largely because New Zealand enjoyed preferential trade access to the U.K. market (Bollard 1994: 73). The government also lavished subsidies on farmers to keep them internationally competitive. But beyond agriculture, the country’s production profile includes a significant urban manufacturing component. Before 1984, government policies nurtured industry behind significant trade barriers and restrictions on foreign investment. In many respects, New Zealand’s economy resembled the import-substitution industrialization economies of the developing world. The system of

manufacturing protection and agricultural subsidies worked well for New Zealand; profitable agricultural trade coupled with the government's generous program of social services and transfer payments made the population one of the most prosperous and egalitarian in the world.

Then came the oil shocks. The worldwide recession threw New Zealand's economy into deep crisis. Britain's 1973 entry into the European community and participation in the common agricultural agreements constituted a second shock, as the British market became increasingly closed to New Zealand farm exports. The government could have responded to the recession with a downsizing of state-owned industry, an easing of the regulatory environment, or a reorientation of trade relations. It did none of these. Instead, under the direction of National Party Prime Minister Robert Muldoon, the government launched an enormously subsidized public works project called "Think Big." The new program aimed to improve infrastructure in the country, end the balance of payments problems through further import substitution, and reduce the country's oil dependence. It expanded and built petrochemical refineries, steel mills, synthetic-fuel plants, and methanol-production facilities (Nagel 1994: 14). But its real purpose was maintaining full employment in the face of external shocks. "Think Big" amounted to a large-scale jobs program. The fiscal deficit ballooned as a result, with the public debt growing sevenfold between 1975 and 1984, from NZ\$4 billion to NZ\$28 billion. Inflation soared into the high teens until Muldoon's government instituted a wage and price freeze in 1982. The gross domestic product (GDP) grew at merely 0.2 percent per year between 1974 and 1984, compared with the OECD average of 1.8 percent (Nagel 1994: 4; Bollard 1994).

Table 1
AVERAGE ANNUAL GROWTH RATES IN GDP PER CAPITA

Period	New Zealand	OECD Average
1955-60	1.8	2.1
1960-65	2.8	3.9
1965-70	1.6	3.6
1970-73	2.6	4.2
1974-84	0.2	1.8

SOURCE: OECD, *Economic Surveys: New Zealand, 1975, 1988-89*.

Throughout the late 1970s and early 1980s, internal and external pressure continued to mount on the government to adjust the economy to the changing international environment, and to deal with the fiscal and stabilization crises. The National government under Muldoon had initially taken modest steps toward reform, but, after the oil shocks and the closure of British markets, policy innovation that threatened the middle classes no longer proved palatable to the prime minister. Muldoon, who had dominated New Zealand politics as Prime Minister for nearly a decade, stubbornly refused to scale back the welfare state, open the closed economy, or temper his public works projects.

This recalcitrance had political roots. Unlike many of his patrician or business-class co-partisans, Muldoon came from a working-class background. He strongly

identified with what he called the “ordinary bloke,” and drew much of his core support from the middle and lower-middle classes. He was master at mobilizing the older, less educated citizens by playing off their anger at the “extremist left” that had protested the Vietnam war, advocated Maori rights, and mobilized against apartheid in South Africa. Muldoon’s ardent supporters, which he dubbed “Rob’s Mob,” vocally opposed economic reform. A rift grew between Muldoon and reformist factions in his party. He dealt with party revolt by sacking the ring-leaders in the cabinet and forcing others out of the party completely.

As the 1984 election approached, a formerly staunch National Party supporter and benefactor named Bob Jones launched a third party, called the New Zealand Party, with the express purpose of bringing down Muldoon and his National Party cronies. Jones’ political views smacked of libertarianism, and he advocated an unorthodox mix of emphasis on education, law and order (but decriminalization of marijuana use), environmental conservation, and dismantling of the New Zealand armed forces. However, as its *raison d’être* and central program, the New Zealand Party called for a turn toward free-market economics (Nagel 1994: 15).

The new party drew as much as 20 percent support in pre-election polls, and polled 12 percent of the popular vote in the 1984 election—a strikingly high figure for a third party in New Zealand. But more important than the popular vote, the party’s effect in the swing districts in urban and suburban areas proved crucial to the electoral outcome. Supporters of economic adjustment—those most pinched by high inflation, stagnant growth and closed markets abroad—defected from the National Party’s ranks and cast their vote for the new reformist party. These defections propelled the Labour Party into power after having spent most of the previous thirty years in opposition.

Not only did Muldoon’s dogged defense of economic interventionism put him at odds with factions in his own party and result in electoral defeat, it also had become completely out of step with the policy advice offered by the bureaucracy. The Treasury Department, whose responsibilities and expertise encompass all aspects of the New Zealand economy, had begun calling for a major shift in economic policy in the late 1970s. Throughout the 1970s, Treasury’s ranks became increasingly dominated by free-market economists, particularly those with expertise in micro-economics. Many officials had received postgraduate training at U.S. institutions, including Harvard’s John F. Kennedy School of Government, Harvard Business School and the economics department at the University of Rochester. Treasury also employed consultants from the U.S. (Bollard 1994).

Treasury economists became convinced that the country’s problems were structural in origin. They received encouragement in the form of reports and statements by the IMF, the World Bank and the OECD. Treasury thus prepared a comprehensive document detailing the steps of reform. It called for a reversal of the values that had previously guided New Zealand economic policy making. Analysts have argued that the report heralded “efficiency over equity, growth over stability, competition over security, monetarism over Keynesianism, and private over public ownership” (Nagel 1994: 4-5).

This proposal grew in importance due to the near monopoly Treasury holds on economic policy advice in the country. It is as if one super-agency in the U.S. combined all the resources and expertise of the “Office of Management and Budget, the Council of Economic Advisors, the Department of the Treasury, the Congressional Budget Office, the General Accounting Office, and most of the economists and policy analysts who work for executive agencies and congressional committees” (Nagel 1994: 19). The

reform advocated by the Treasury Department included proposals to remove all currency controls and eventually to allow the New Zealand dollar to float freely in relation to other currency. Utilizing its information monopoly, Treasury called for aggressive trade liberalization; corporatization and privatization of state enterprises; and full liberalization of rules governing foreign investment. It also advised reform of industrial relations, with individual contracts coming to replace union-negotiated collective contracts. And, it pushed for the reform of welfare services, health care and education. It advocated the institution of a user-pays principle and the tightening of requirements for receipt of government services.

LABOUR LAUNCHES REFORMS

The Reform Plan

The Labour Party had also undergone significant change in its own ranks during its long exile from the cabinet. A group of middle- and upper-class professionals had risen in the ranks of the party leadership, and brought a very different perspective to matters of policy than the traditional union-centered membership. Where in 1972 only 40 percent of the Labour Party MPs were professionals or semiprofessionals, by 1984 that number had risen to 73 percent. Roger Douglas typified the ascent of the new Labour elite. An accountant and disciple of neoliberal economics, he had served during the last few years of Muldoon's administration as Labour's shadow minister of finance. Douglas had written a book, called *There Has to be a Better Way*, that outlined a vastly new, market-oriented strategy for New Zealand's economy. He served both as the chief economic spokesperson for Labour during the campaign, and as chief critic of Muldoon's economic practices. Despite Douglas' clear neoliberal views, during the campaign Labour avoided overtly signaling that drastic changes in economic strategy would follow the party's electoral victory.

When Douglas became Labour's new Finance Minister and began his series of startling reforms by devaluing and floating the currency only days after taking office, many New Zealanders were shocked, and charged that the electorate had been duped by Labour. Others, such as Jones and his New Zealand Party, applauded Labour's efforts and endorsed the neoliberal reforms. Labour forged forward with Douglas' reform plans, soon named "Rogernomics."

The government lifted currency controls entirely, and almost fully deregulated the financial sector—it removed restrictions on entry into the banking sector and freed interest rates. The Reserve Bank was made more autonomous, given a board of directors, and charged formally with keeping the inflation rate between zero and two percent. Before, the central bank had been subject to political criteria in its performance. In 1989 the change in the bank meant that it had been reestablished as an independent agency, with a formal contract to provide a service to government: a low inflation rate. New directives removed controls on foreign investment in New Zealand and on New Zealanders seeking to invest externally. This deregulation applied to any form of investment, both direct and portfolio. New legislation also removed restrictions on the establishment of foreign-owned companies in New Zealand and on the repatriation of earnings and capital (Bollard 1994: 80).

As one of its first moves, Labour sharply reduced agricultural subsidies in 1984-85, and had fully eliminated them by 1989. This move outraged farmers, who then demanded either that the policy be reversed, or that other economic sectors immediately be exposed to the same unsoftened international market pressures. In contrast, the government phased in liberalization of trade in manufacturing over a longer time period. Also, the government phased out import licensing over a period of four years. This move exposed a high nominal tariff structure, which officials have since rationalized by decreasing the highest tariffs by the highest percentage. By June 1993, nominal tariffs rates had declined to an average of 10 percent, and were scheduled to be reduced by one third again by 1996 (Bollard 1994: 80).

While Douglas did not privatize the bloated state sector very aggressively, he did institute a series of measures aimed at making state-owned enterprises more efficient. Aided by Treasury's expertise, he "corporatized" many companies under the State-Owned Enterprises Act of 1987, making their leaderships responsible to boards of directors and subject to market incentives. Their staffs were reduced in size and their management structures were completely reorganized, and an enterprise-specific investment schedule was established for each. The government also introduced a "user pays" principle for many public services.

Although the government did not extend the welfare state, it did prove generous in maintaining the programs that had already been established. In education, the government reduced class sizes by hiring 2,000 more teachers in the country. It also gave pay increases to nurses and other health-care professionals. While a consumption tax and a flattened income-tax code helped alleviate the fiscal deficit, the government attempted to carefully structure its new, flattened tax policy so as not to burden the lowest income groups.

Still, the free market reforms proved radical and far-reaching. As with all such adjustments, the costs soon became apparent. While the central bank brought inflation under control, the new market pressures forced significant dislocation in the private and public sectors. Unemployment grew, approaching double digits. GDP growth, while sluggish during most of the '70s and early '80s, declined even further, even to real negative rates in some years. An income gap appeared and widened rapidly in the formerly egalitarian society. See Table 2.

Table 2
NEW ZEALAND SELECTED ECONOMIC INDICATORS, 1983-91

Indicator	1983	1985	1987	1989	1991
Inflation	15.4	8.6	14.6	5.2	5.5
Unemployment	5.4	3.8	4.1	7.4	9.9
Interest Rate	13.8	21.0	27.4	13.5	12.1
Effective Rate of Assistance					
Manufacturing	39.0	37.0	26.0	19.0	14.0
Agriculture	49.0	34.0	19.0	-1.0	-6.0

SOURCE: Bollard 1994: 76.

The 1987 Electoral Battle

Two major issues dominated the election campaign of 1987: economic reform and the ban on nuclear warships in New Zealand harbors. On the nuclear issue, the Labour government had pursued the ban even though it led to the withdrawal of New Zealand from the ANZUS security pact with Australia and the U.S. This issue had broad appeal among the growing class of “postmaterialist” voters in the country, who supported environmentalism, feminism and other relatively new social issues. The National Party continued its opposition to economic reform and decried the withdrawal of the country from ANZUS. Supporters of the economic reform and supporters of the nuclear ban did not exactly overlap as an electoral group, but there was sufficient congruence in voter support for the issues to form a set of swing voters in several marginal districts.

In the 1987 election, Labour actually lost significant shares of the vote in districts that had provided “safe” seats for the party in previous elections. Its overall margin over National slipped from 7 percent to 4 percent in the popular vote (Nagel 1994: 23). Many working-class voters, suffering from the economic downturn, had grown disaffected and had abstained from voting altogether—although abstention typically did not result in Labour’s losing a seat in any given district. The party, however, picked up swing voters in marginal districts, and retained its legislative majority. By 1987, the upstart New Zealand Party had virtually disappeared as a campaign vehicle. See Table 3.

Table 3
NEW ZEALAND ELECTORAL STATISTICS, 1978-1993

Party		1978	1981	1984	1987	1990	1993
Labour	Vote %	40.4	39.0	43.0	48.0	35.1	34.7
	Seat %	43.5	46.7	60.0	58.8	29.9	45.5
National	Vote %	39.8	38.8	35.9	44.0	47.8	35.0
	Seat %	55.4	51.1	37.9	41.2	69.1	50.5
Social Credit	Vote %	16.1	20.7	7.6	-	-	-
	Seat %	1.1	2.2	2.1	-	-	-
NZ Party	Vote %	-	-	12.3	0.3	-	-
	Seat %	-	-	0.0	0.0	-	-
*Alliance	Vote %	-	-	-	-	14.3	18.2
	Seat %	-	-	-	-	1.0	2.0
NZ First	Vote %	-	-	-	-	-	8.4
	Seat %	-	-	-	-	-	0.0

*The Alliance consists of several minor third parties, including Green, New Labour, Democrat and Mana Motuhake (a Maori-rights party).

SOURCES: Thomas Mackie and Richard Rose, *The International Almanac of Electoral History* (Washington, D.C.: Congressional Quarterly, Inc., 1991); and Stephen Levine and Nigel Roberts, “The New Zealand Electoral Referendum and General Election of 1993,” *Electoral Studies* 13, 1 (September 1994): 247.

Leadership Struggle

In Labour's second term, although reform initially continued apace under Douglas' leadership, the anticipated positive effects of adjustment failed to materialize. The stock market crash of late 1987 exacerbated this problem. Because of the government's previous financial reforms, New Zealand's sharemarket had been caught up in a speculative bubble, and when the crash hit, it fell farther than any other market in the developed world (Nagel 1994: 24). New Zealand's shares have yet to recover the value they lost in the crash.

The effects of the deepened economic crunch splintered the governing party, and rifts manifested themselves in the cabinet. Prime Minister David Lange (pronounced *long-ee*) favored halting the reform process in an attempt to avoid inflicting further pain on the electorate. Finance Minister Douglas favored moving forward, arguing that prosperity would not return until markets could function fully unfettered. He advocated a flat-rate income tax and the privatization of state-owned enterprises. These policies would signal an essential roll-back of the country's well-developed welfare state (Nagel 1994: 24).

Douglas publicly announced his intentions to move forward with this program. Lange was outraged. The two leaders' differences became bitter and public. After a prolonged political battle, Lange forced the resignation of Douglas from the cabinet. In retaliation, Douglas led a back-bench revolt that restored Douglas to the cabinet and ousted Lange from his position as prime minister. Deputy Prime Minister Geoffrey Palmer stepped in to fill the breach as prime minister, but his leadership proved ineffective. Finally, Mike Moore assumed the leadership post. He declared that while he would not roll back the party's economic reform attempts, he would halt them where they stood. With three prime ministers in a period of 14 months, the Labour Party conveyed an image of disorganization and ineffectiveness to an already unsettled electorate for the 1990 elections.

THE 1990 ELECTION AND NATIONAL'S REFORM PROGRAM

In contrast, the National Party organized a credible opposition campaign. National had overcome its internal struggle shortly after the 1987 election; Muldoon was ousted and neoliberal reformers subsequently assumed party leadership posts. Just before the 1990 election, National spokespeople announced a reversal in the party's nuclear position, supporting the country's withdrawal from ANZUS. This defused the nuclear question as a campaign issue. However, similar to Labour's 1984 strategy, National soft-pedaled the party's interest in further economic reform. National leaders signaled that they favored the reforms that had already occurred, but had limited interest in pressing them further, except in a few key areas.

In the 1990 election, once the nuclear issue had been defused, the Liberal Party lost a sizable group of left-wing voters. Constituents that had previously voted with Labour because of the party's leftist social and foreign policies jumped ship and joined minor third parties, such as the Greens or the breakoff NewLabour Party. Labour faced further defections in many key districts. The electoral pendulum swung back to favor National, which formed the executive with 67 seats to Labour's 29. Labour had lost 28 seats and fell 13 percent in the popular vote (Nagel 1994: 24). See Table 3.

The “few key areas” on National’s economic reform agenda turned into major efforts to gut policies that had favored the Labour Party’s primary constituents. Under the direction of the new Minister of Finance and free-market purist Ruth Richardson, the government began to dismantle the elaborate system of welfare transfer payments and social services that had long served as hallmarks of the country’s egalitarian public policy. National restored voluntary unionism and restructured labor-industry bargaining rules. In the Employment Contracts Act of 1991, individual contracts, rather than union membership contracts, were mandated, and the government withdrew the legal recognition of unions to bargain collectively (Nagel 1994: 34). In these efforts, National received substantial encouragement and administrative support from the Treasury Department.

Also, the state-owned Housing Corporation began to charge tenants at market-level rates and sold off its subsidized mortgages. Richardson’s new budget substantially tightened eligibility requirements for welfare recipients, and cut back cash benefits sharply (Nagel 1994). The National government also moved forward with privatization plans. Between 1988 and 1992, “22 enterprises were sold for a total of NZ\$12 billion,” with little distinction made among buyers, be they foreign or domestic (Bollard 1994: 79-80). Proceeds from the sales went to alleviate public debt.

With the capstones of New Zealand’s economic reforms put in place by National in the early 1990s, the economic policy turnaround was virtually complete. However, economists and other policy analysts have been baffled at the sequencing of the country’s reforms. Generally, economists argue that governments should stabilize the economy before initiating structural adjustment. This ensures “balance in the government sector” (Bollard 1994: 97). And, they should deregulate product markets and labor markets before deregulating the financial sector. That way, flows in commodities and not flows in capital will determine the real exchange rate. Finally, governments should “deregulate domestic markets before external ones, to allow local interests to absorb any economic rents and to retain internal balance before liberalization” (Bollard 1994: 97-98). Analysts have noted that New Zealand violated virtually all of the established principles for ordering economic-adjustment policies. At least partly as a result of the misordering of reform policies, the country’s economy was slow to see the positive results that such adjustments are supposed to foster.

Finally, in 1993, the country passed through its first year of high economic growth in nearly a decade. GDP grew at 5.2 percent for the year (Nagel 1994: 5). However, unemployment remained high at 9 percent. The income gap continued to widen with disposable incomes falling sharply for the lower-income segments of the populace, for some by as much as 30 percent (Nagel 1994: 34). Unemployment crested at 11 percent in 1992 (Nagel 1994: 5). By deregulating financial markets, causing unemployment, restructuring taxes regressively, and cutting social services, government policy had contributed to growing inequality (Nagel 1994: 22). Many New Zealanders found themselves excluded from the benefits of the reforms. Public outcry against the pace of the economic reforms intensified. Again, a rift in the governing party developed, and Richardson was sacked by Prime Minister Jim Bolger as a result of the in-fighting. The government then halted further economic reforms, but held steady on the deep adjustments that had already been implemented.

VOTER OUTRAGE AND ELECTORAL REFORM

With both major parties now appearing responsible for the dislocating economic policies, but also claiming credit for the returned economic growth, voters faced a difficult choice for the 1993 election. The election resulted in one of the closest races in New Zealand political history. The National Party finally formed a sustainable government more than a week after the election, but with a margin of only a single seat.

For many voters, the choice between National and Labour proved ultimately unpalatable. Disgust with the manner in which policy decisions were made by government had risen to extreme heights. Confidence in politicians had slipped from 33 percent in a 1975 poll, to merely 4 percent in 1992; voter turnout had dropped from 86 percent in 1984 to 76 percent in 1990.

Concurrent with the 1993 election, voters were allowed to choose not only between parties for government, but also between types of electoral systems that would decide future elections. In a referendum, voters could opt to retain single-member districts, or could choose to shift to a mixed-member proportional representation system (MMP). They chose to toss out the old system and change to MMP by a 54 to 46 margin. Analysts have interpreted the result to indicate widespread voter dissatisfaction with the two major parties and with the political system that produced them. Observers have also understood the referendum result to signal voter disaffection with the manner in which economic reform was implemented.

Modeled on the German electoral system, MMP means that seats are awarded proportional to votes cast for party lists. Under MMP single-member districts remain. But nearly half the seats in the expanded 120-member House will be awarded by proportional representation such that each party's share of the total 120 seats conforms closely to its nationwide party-list vote. (The exact number of seats in single-seat districts and in the national PR district will vary from election to election.) The electoral law provides a threshold of five percent of the national party-list vote for a party to obtain seats; however, any party that wins at least one "electorate seat" (i.e. a single-seat district) is entitled to its full proportional share of seats, even if its list vote was less than five percent. The practical effect of proportional representation, determined in multiple studies and forming one of the most robust findings in the study of politics, is to increase the number of parties represented in the legislature (Taagepera and Shugart 1989). The multi-party system means the formation of coalition governments—members from two or more parties dividing the ministerial portfolios among themselves—or minority cabinets in which the party (or parties) that control the cabinet are short of a majority in parliament.

POSTSCRIPT: The First Three MMP Elections

New Zealand held its first election under the new system on October 12 1996. Subsequent elections were held in 1999 and 2002.

Party	1996				1999				2002			
	% list votes	single-seat districts	list seats	total seats	% list votes	single-seat districts	list seats	total seats	% list votes	single-seat districts	list seats	total seats
National	33.8	30	14	44	30.5	22	17	39	20.9	21	6	27
Labour	28.2	26	11	37	38.7	41	8	49	41.3	45	7	52
NZ First	13.4	6	11	17	4.3	1	4	5	10.4	1	12	13
Alliance	10.1	1	12	13	7.7	1	9	10	1.3	0	0	0
ACT	6.1	1	7	8	7.0	0	9	9	7.1	0	9	9
United Future	0.9	1	0	1	0.5	1	0	1	6.7	1	7	8
Green	--	--	--	--	5.2	1	6	7	7.0	0	9	9
Progressive	--	--	--	--	--	--	--	--	1.7	1	1	2
Others	7.5	0	0	0	6.1	0	0	0	3.6	0	0	0
Total	100.0	65	55	120	100.0	67	53	120	100.0	69	51	120

Supplementary Notes:

- NZ First is a conservative nationalist party that broke away from National and is headed by a former National minister, Winston Peters.
- Alliance is a leftist party that broke away from Labour and is headed by Jim Anderton, a former Labour minister and leader of the country's trade union movement.
- ACT is a strongly free-market party that broke away from Labour and is sponsored by former Labour minister, Roger Douglas.
- Progressive is a coalition founded by former Alliance leader Jim Anderton. Its full name is Jim Anderton's Progressive Coalition.
- Results shown for United Future in 1996 are for a party then known as United and headed by Peter Dunne. This party subsequently merged with a Christian-right party, Future New Zealand and ran as United NZ in 1999.

REFERENCES

- Bollard, Alan. 1994. "New Zealand." In John Williamson, ed. *The Political Economy of Policy Reform*. Washington, D.C.: Institute for International Economics.
- Harris, B.V. 1985. "The Constitutional Base." In Hyam Gold, ed. *New Zealand Politics in Perspective*. Auckland, NZ: Longman Paul Limited.
- Lijphart, Arend. 1984. *Democracies: Patterns of Majoritarian and Consensus Government in Twenty-One Countries*. New Haven, CT: Yale University Press.
- Nagel, Jack H. 1994. "Market Liberalization in New Zealand: The Interaction of Economic Reform and Political Institutions in a Pluralitarian Democracy." Paper presented at the September 1994 Annual Meeting of the American Political Science Association, New York City.
- Taagepera, Rein and Matthew Shugart. 1989. *Seats and Votes*. New Haven, CT: Yale University Press.