



3 December November 2018

Hon Grant Robertson
Minister of Finance

Dear Minister,

Triannual Report – 1 July to 31 October 2018

I am pleased to submit the Commission's first triannual report for the 2018/19 year. While intended to cover the reporting period 1 July 2017 to 31 October 2018, this report also comments on matters outside of the reporting timeframe where relevant.

The Commission delivered the *State sector productivity* final reports on 1 August 2018, and they were publicly released on 17 August 2018 with the evaluation completed in September 2018. We also delivered the *Low-emissions economy* final report on 29 August 2018, and it was publicly released on 4 September 2018 with the evaluation currently being completed.

Work has commenced on a new inquiry into *Local government funding and financing*. We published an issues paper on 6 November 2018 to aid public participation and our engagement process is underway. We are working in conjunction with LGNZ's zone and sector meetings to meet with a range of councils and other interested parties. We have also set up an official's forum to meet periodically with government agencies to get updates on various workstreams and to sound-out findings and recommendations as they evolve.

The Commission's research outside of our inquiries continues and we leveraged our strong connections in editing a special edition of a journal for New Zealand policymakers (*Policy Quarterly*), with eight articles on productivity issues. The articles illustrate how our understanding of New Zealand's productivity performance has improved over recent years and where key gaps remain.

We are working on the joint research project with the Australian Productivity Commission into *Growing the digital economy in Australia and New Zealand: maximising opportunities for SMEs*. and are on track to deliver the research report to the requesting Ministers on 31 January 2019.

Regarding financial and administrative matters, the Commission tracked \$28k under budget for the reporting period and is forecasting to be in budget balance at the end of the financial year. Our 2017/18 Annual Report was presented to the House on 15 November 2018 and we will attend the Economic Development, Science and Innovation Committee on 29 November.

We look forward to final confirmation of the terms of reference for the *Technological Change, Disruption and the Future of Work* inquiry and moving forward with our new work programme in 2018/19.

We would be pleased to meet with you to discuss the Commission's performance to date, and we remain open to any feedback to assist us to improve the value of our reporting to you.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'Murray Sherwin', with a long horizontal line extending to the right.

Murray Sherwin
Chair

Triannual Report: 1 July to 31 October 2018

Report structure

- Operational delivery
- Financial performance
- Capability
- Priorities and issues ahead

Operational delivery

This table is a high-level summary of our operational delivery. Green indicates progress according to schedule; orange indicates delays or other issues.

	Status	Comment
Inquiries		<p>On 1 August 2018, the Commission delivered its final reports for the State sector productivity inquiry (published on 17 August). Publications included:</p> <ul style="list-style-type: none"> • Two final inquiry reports: Improving state sector productivity, which contains advice and recommendations for Ministers and agency leaders, and Measuring state sector productivity, which contains guidance for state sector officials who are tasked with measuring productivity. • Performance management research looking at the history of efficiency measurement in the health sector. • Measurement case studies, including case studies of the Police, the Courts, Early Childhood Education, and MSD. • Innovation research looking at innovation in primary health care and at the example of the Health Care Homes service model. • Staff and leader perspectives, including: a summary of interviews with senior public sector leaders; and, analysis from a survey of PSA members. <p>In September, the Commission published an evaluation of the State sector productivity inquiry, which consisted of three separate pieces of work: an expert review by Dr Murray Horn and reports on participants perspectives via a focus group and participant survey.</p> <p>On 29 August 2018, the Commission delivered its final report for the Low-emissions economy inquiry. We also released modelling reports, summary documents, and a 2-minute video explaining the inquiry's findings.</p> <p>On 16 July 2018, we received the terms of reference for a new inquiry into Local government funding and financing and published an issues paper on 6 November 2018 to aid public engagement.</p>
Research		<p>The Commission leveraged its strong connections in editing and contributing to the August 2018 edition of <i>Policy Quarterly</i>, a journal for New Zealand policymakers, containing eight articles on productivity.</p> <p>The Commission's work on spatial economics (regional development) is proceeding and enhancing our understanding of the growth process across New</p>

		<p>Zealand cities and regions. The aim of this work is to build an evidence base for regional development policy.</p> <p>We started work on a joint research project with the Australian Productivity Commission into growing the digital economy in Australia and New Zealand. We will deliver our research report to the referring Ministers by 31 January 2019.</p>
Promoting understanding		<p>The Commission continues to promote understanding of productivity related matters, including with presentations based on our narrative (<i>Can the Kiwi fly? Achieving productivity lift-off in New Zealand</i>) and Productivity Hub events on topics such as the labour market effects of technical change. Planning for the next biennial Productivity Hub Symposium in December 2019 has begun and Philip McCann (University of Sheffield) has been confirmed as the keynote speaker.</p>

Inquiry: Measuring and improving state sector productivity

	Status	Comment
Right focus		<p>The evaluation found that 74% of survey respondents “agreed” or “strongly agreed” that the final reports focused on the issues most significant to the topic. The independent expert review conducted by Dr Murray Horn found that:</p> <p>“The reports give relevant and material advice on most aspects of the four areas identified in the Terms. Where the inquiry falls short, it does so because the Terms created a dilemma for the inquiry: the best measures for meeting the three objectives in the four identified sectors are not the narrowly defined technical efficiency measures the Terms require.” (p. 1)</p>
Good process management		<p>The terms of reference required a draft report, and then a final report by 30 August 2018. The final reports were delivered on 1 August 2018.</p> <p>During the inquiry, the Commission sought submissions and held engagement meetings on the issues paper and draft report to ensure the inquiry was well-informed and relevant. We commissioned 11 research papers (including a number of case studies), engaged in two roundtables and four conferences and seminars, and referenced about ninety published papers.</p> <p>In the evaluation, 67% of inquiry participants surveyed “agreed” or “strongly agreed” that overall they were satisfied with the Commission’s inquiry processes.</p>
High-quality work		<p>The survey of inquiry participants found that 55% of respondents agreed (20% disagreed, 25% didn’t know) that the inquiry overall had helped set or lift the standard in New Zealand for high quality analysis and advice on measuring and improving state sector productivity.</p> <p>The stakeholder focus group agreed that the reports met the terms of reference, left nothing out, and could be applied by those working in the public sector. However, some felt the Commission’s recommendations were familiar and didn’t break any new ground and there were several suggestions for improvements.</p>

		The quality of this inquiry was commended by Professor Patrick Dunleavy of the London School of Economics, who is one of the few scholars investigating how to measure the productivity of UK public services.
Effective engagement		<p>The Commission interviewed multiple current and former senior state sector leaders to inform this inquiry. We carried out 46 engagement meetings, attended 7 conferences/roundtables and received 31 submissions from individuals/organisations.</p> <p>The inquiry found that there was scepticism about the value of productivity measurement and concerns about any deviation from a focus on outcomes in Ministries, but a real appetite for assistance and advice on measurement in more operationally focused departments and agencies.</p>
Clear delivery of message		<p>The Commission produced two slim final reports for this inquiry. This was partly in response to feedback about the inaccessibility of longer reports, but also to develop targeted advice for two different audiences:</p> <ul style="list-style-type: none"> • The Improving state sector productivity report provided advice for Ministers and departmental leaders about productivity performance and setting expectations for improvement. • The Measuring state sector productivity report provided guidance for officials on how to develop productivity metrics. It could be read independently or in conjunction with the other report. It could also be used to commission or evaluate productivity studies, or to understand productivity measures created by others. The Commission is now working on an online interactive guide to further improve accessibility and expand the reach of this work. <p>The survey of inquiry participants found that 95% of respondents “agreed” or “strongly agreed” that the findings and recommendations were clear.</p>

Inquiry: *Transitioning to a low-emissions economy*

	Status	Comment
Right focus		<p>This inquiry attracted an unprecedented level of quality submissions on our issues paper and draft report (403 submissions). Together with our engagement process, this allowed us to appropriately focus our inquiry: our research workstreams, findings and recommendations.</p> <p>The survey of inquiry participants showed that 73% of respondents “agreed” or “strongly agreed” that we focused on the issues most significant to transitioning to a low-emissions economy. Also, 72% of respondents “agreed” or “strongly agreed” that we went into sufficient depth on the issues we covered.</p> <p>Feedback from the focus group was that we asked the right questions and focused on the right issues. That said, some thought there were analytical gaps in areas such as non-financial drivers of behaviour and the role of behavioural sciences in developing non-market solutions in transitioning to a low-emissions economy.</p>

Good process management		<p>83% of survey respondents were “satisfied” or “very satisfied” with the Commission’s process for running the inquiry. Likewise, the focus group commented that the process used to produce the final report was “...excellent: open, inclusive, and robust”.</p> <p>The high level of interest generated by this inquiry, its comprehensive engagement process, and critical modelling work created time pressures. Despite allocating additional resource, it meant a delivery of our final report to referring Ministers on 29 August 2018, instead of the requested delivery of 30 June 2018.</p>
High-quality work		<p>Substantial modelling work was commissioned by a consortium of <i>Vivid Economics, Concept Consulting</i> and <i>Motu Economic and Public Policy Research</i> on different transition pathways to a low-emissions economy, examining different scenarios of the future and respective impacts and outcomes. The modelling provided high-quality data and analysis to inform our policy recommendations.</p> <p>85% of survey respondents rated the analysis of information as acceptable or better. 79% of respondents rated the “overall quality” of the inquiry as acceptable or better.</p> <p>The stakeholder focus group was very positive about the quality of the inquiry and made some valuable suggestions for improving the process and quality of future inquiries. We look forward to learning more from the independent expert evaluation that is currently being undertaken by Dr Gwenneth (Wendy) Craik, a leading Australian-based consultant and advisor in public policy and natural resource management.</p>
Effective engagement		<p>The team carried out over 130 engagement meetings, attended 34 conferences/seminars and 403 submissions were received from a diverse range of interested groups and individuals.</p> <p>Our terms of reference indicated that we should engage closely with the Climate Change Iwi Leadership Group in understanding this inquiry. In the event, this proved difficult for the Iwi Leadership Group to accommodate. However, we received excellent engagement and submissions from Te Rūnanga o Ngāi Tahu. The team also met regularly with the Ministry for the Environment’s Climate Change Transition Hub.</p> <p>83% of survey respondents said they “agreed” or “strongly agreed” that the Commission provided ample opportunity to participate; 80% “agreed” or “strongly agreed” that the Commission was approachable; and, 90% “agreed” or “strongly agreed” that the Commission communicated its views clearly.</p> <p>Overall, engagement with stakeholders was described positively by the focus group with some noting that opportunities had been missed early in the inquiry process for the Commission to go further, faster “...had they talked to the right people and accessed the most relevant research earlier.”</p>
Clear delivery of message		<p>95% of survey respondents “agreed” or “strongly agreed” the style of writing and language used were assessible and clear. 93% “agreed” or “strongly agreed” that the findings and recommendations were clear, whereas the focus group was interested in the Commission’s role after the report was released in areas such as coordination, oversight and communicating with stakeholders.</p>

Inquiry: Local government funding and financing

	Status	Comment
Right focus		The Commission published an issues paper on 6 November 2018 to aid public engagement in the inquiry. It seeks views and information on 49 questions about current pressure points and ways that councils can manage cost pressures.
Good process management		The team have reviewed the evaluation feedback from our latest inquiries to understand how we can better plan, engage and communicate in our inquiry work. The work programme is on track with the issues paper published on 6 November 2018 and engagement meetings are underway.
High-quality work		We have received positive feedback on the issues paper with stakeholders noting its "thoroughness" and coverage of key issues,
Effective engagement		<p>We are working with LGNZ to engage with councils on the questions in the issues paper through its zone and sector meetings. Following initial engagement with local authorities, a series of roundtables will be organised to discuss specific issues with experts. In addition, we will be meeting with other interested parties in the regions: business organisations, academics, iwi and other Māori organisations, developers, ratepayer organisations and other community groups and government agencies.</p> <p>We have also established an official's forum (convened by DIA) to meet periodically with government agencies (DIA, MBIE, MfE, Treasury, Tax Working Group; Infrastructure Unit) to get updates on various workstreams related to the inquiry that are being progressed across government. The first meeting was held in October and another is planned for February 2019.</p>
Clear delivery of message		In our draft report, we will take care to convey our evidence and messages in clear and accessible language, acknowledging the wide range of viewpoints. All chapters will be reviewed by an external editor, in addition to our internal editing process to ensure clarity and accessibility.

Previous inquiries

The evaluation of the *State sector productivity* inquiry is included in our *2017/18 Annual Report* and available on the Commission's website at www.productivity.govt.nz/statesectorprod. The evaluation of the *Low-emissions economy* inquiry is underway. The focus group and survey have been completed and the expert review is underway.

We note also that formal government responses to the following inquiries are yet to be received: *Low-emissions economy*; *State sector productivity*; *Better urban planning*; and, *Boosting services sector productivity*.

Research

The Commission was pleased to be invited to be the editor of the August 2018 edition of *Policy Quarterly*, a journal for New Zealand policymakers. This edition had eight articles on productivity issues with contributions from the OECD, the Australian Productivity Commission, the Ministry of Business, Innovation and Employment, Victoria University of Wellington, and the Commission itself. As the editorial overview noted, lifting productivity is the answer to many of New Zealand's hardest problems but for many years the

drivers of this productivity performance were not well understood. The articles illustrate how our understanding of this performance has improved over recent years and where key remaining gaps are. The articles were:

- *Moving on from New Zealand's productivity paradox* by Patrick Nolan, Huon Fraser and Paul Conway of the New Zealand Productivity Commission
- *The future of productivity – what contribution can digital transformation make?* By Dirk Pilat and Chiara Crisuolo of the OECD
- *Meeting the challenge of a low-emissions economy* by Steven Bailey and Geoff Lewis of the New Zealand Productivity Commission
- *Quakes and aftershocks: organisational restructuring in the New Zealand state sector, 1960-2017* by Masashi Yui and Robert Gregory of Victoria University of Wellington
- *Shifting the dial: improving Australia's productivity performance* by Ralph Lattimore of the Australian Productivity Commission
- *Measuring productivity in the health sector* by Patrick Nolan of the New Zealand Productivity Commission
- *Quality adjusting education sector productivity* by Patrick Nolan of the New Zealand Productivity Commission, Norman Gemmell of Victoria University and Grant Scobie of Everest Consulting
- *Productivity measurement in the digital age* by Sharon Pells of the Ministry of Business, Innovation and Employment.

Spatial productivity (Regional development)

Our work on spatial productivity (regional development) is progressing and we expect to release a paper for discussion in early 2019. This paper will explore how and why patterns of industry employment change have differed across cities and outline industries that have managed growth in regional cities. By better understanding the process of growth and development across New Zealand's cities, we hope to use this work to build a strong evidence base for regional development policy.

Growing the digital economy: joint project with the Australian Productivity Commission

At their annual leaders' meeting in March 2018, the Prime Ministers of Australia and New Zealand committed to a review on *growing the digital economy and maximising opportunities for small and medium enterprises* (SMEs). We, along with the Australian Productivity Commission, received the scope of research from the Minister of Finance for this review in August 2018 and started a joint project in September.

Reflecting the scope of research, the project explores how institutional and regulatory settings in the two countries can support the use of digital technology and how SMEs can maximise the opportunities from digital transformation.

It was unrealistic to follow our typical inquiry processes given the short timeframe and we have not produced an issues paper or draft report. Nor have we sought written submissions. We have, however, held 33 meetings with interested parties to inform the research, and attended conferences in Adelaide, Wellington, Auckland and London. We will deliver a research report to the requesting Ministers by 31 January 2019.

The Productivity Hub

During the reporting period, the Productivity Hub's work on competition progressed. This work is aimed at building the data infrastructure necessary to measure competition in different parts of the economy and assess the impact of competition and market size on firm performance. This project has involved updating our firm-level productivity numbers, which were previously only available from 2000 to 2012.

The Hub continues to run a successful events programme, with roundtables on topics such as the labour market effects of technical change. Planning for the next biennial Productivity Hub Symposium in December 2019 has begun and Philip McCann (University of Sheffield) is already confirmed as the keynote speaker.

Promoting understanding

Our work through the Hub increases the profile and understanding of productivity issues. We have also been promoting understanding of productivity issues through an extensive presentation programme to a wide range of audiences, across both our inquiry and non-inquiry work:

- The *Low-emissions economy* inquiry attracted a number of invitations to present. Staff gave presentations to Auckland's CEO Forum, Red Meat Sector Conference, Fonterra Climate Change Breakfast, New Zealand Institute of Economic Research Annual Dinner Event, Electricity Authority Board's Strategy Day, EIANZ Symposium, Financial Services Federation AGM, and EECA Business Large Energy Users Forum. Murray Sherwin was also interviewed by the Forest Owners Association on how to achieve carbon neutrality by 2050 for Forest Call, a television series on Face TV.
- Our Economics & Research team presented on New Zealand's productivity story and the potential for change to Auckland Tourism Events & Economic Development, Xero and the Ministry of Business, Innovation and Employment.

Financial performance

Overall the Commission tracked \$28k under budget for the reporting period. Variances are insignificant with Personnel being the largest under-spend at \$8k. The Commission is forecasting to be in budget balance at the end of the financial year. The tables below provide a summary of financial performance across the Commission, and in output areas, for the reporting period:

All financial activity

Financial Performance (\$000's)	4 months to October 2018		2018/19 year
	Actual	Variance to budget	Forecast
Income	1,705	-	5,142
Expenditure	1,620	28	5,142
Net surplus	84	28	-
Total equity			

Output cost breakdown

Output performance (000's)	Actual (4 months to end- October 18)	Variance to budget (4 months to end- October 18)	Allocation remaining (full year)
Inquiries	1,420	9	3,127 (69%)
Research	201	19	394 (66%)

Capability

We had the benefit of the following secondments to assist with our research and inquiries:

- Sandra Moore, Principal Adviser with the Ministry of Social Development was seconded to the *State sector productivity* team and is undertaking research for the proposed *Future of work* inquiry until the end of 2018.
- The Productivity Commission and the Chair in Public Finance at Victoria University of Wellington have jointly provided a scholarship for Huon Fraser, an undergraduate student, to undertake research on health sector productivity. His work contributed to the *State sector productivity* inquiry and the Commission's work on understanding New Zealand's productivity performance.

Two senior staff members have temporarily departed the Commission: Amelia Sharman, a Principal Advisor, was seconded to the Secretariat to the Interim Climate Change Committee from September 2018; and; Paul Conway, Director of Economics & Research, is taking a six-month unpaid sabbatical and is due back in April 2019. Dr Patrick Nolan is leading our economics work programme in his absence.

To ensure we have sufficient resource for our inquiry work programme we recently concluded a recruitment round and made three new appointments:

- Jo Smith, Principal Advisor - Jo joins us after working the last eight years at Sapere Research Group. Jo also has expertise in applied economic research and analysis, and has considerable experience conducting stakeholder engagement activities and programme & service evaluation.
- Hamed Shafiee, Senior Advisor - Hamed worked the last three years at Hutt City Council as a Senior Policy Advisor/Economist providing economic analysis and advice to support the Council's policy functions, inputs into financial strategies, and economic development planning.
- Sally Garden, Principal Advisor - Sally has worked the last four years in the Office of the Parliamentary Commissioner for the Environment where she led a number of inquiry-related workstreams and will bring considerable stakeholder engagement expertise to our inquiry work.

Priorities and issues ahead

On the horizon for the next triannual period (November 2018 – January 2019) and beyond:

- The *Growing the digital economy in Australia and New Zealand* joint report will be delivered by 31 January 2019.
- Submissions are due on 15 February 2019 for the *Local government funding and financing* issues paper and the draft report will be released in June 2019.
- We look forward to receiving the signed Terms of Reference for the *Technological Change, Disruption and the Future of Work* inquiry and expect to begin the inquiry in February 2019.
- The Commission will be submitting a bid for improved resourcing of the Productivity Commission's independent research function in line with recommendations from David Skilling's recent review of the Commission's work. This would help connect productivity-related research and policy development, allow independent and regular reporting and analysis on productivity, including how to best respond to changing technologies and markets, and maximise the value of Productivity Commission (NZPC) inquiries.
- We are also refreshing the Forward-Looking Agenda for Productivity Research (FLARE) with our Productivity Hub colleagues (the Ministry of Business, Innovation and Employment, Statistics New Zealand, and the Treasury). The goal is to aid the coordination and collaboration of research on understanding and improving New Zealand's productivity performance and to better connect productivity research with policy practice.