

What is very big, diverse and full of promise - but underperforming?



No, we're not referring to the Auckland Blues. Rather, it is New Zealand's services sector – representing around 70% of New Zealand's GDP, deeply intertwined with our primary and manufacturing industries and, like the Blues, full of individual stars, but collectively off the pace in terms of meeting its performance potential.

The Productivity Commission has just released its final report on boosting productivity in the services sector. The report shines a spotlight on the critical role that the sector plays in the New Zealand economy and includes a raft of recommendations to lift its performance. Implementing these recommendations would sharpen competition in the sector and help firms in the services sector to more effectively harness information and communications technology (ICT). The Commission believes that these recommendations can make a significant contribution to lifting the sector's productivity, and to New Zealand's overall economic performance.

The services sector now accounts for around 70% of GDP and this share is continuing to grow. Despite this, the sector has traditionally received less attention than the primary and manufacturing sectors. "A thorough examination of the services sector was long overdue", says Commission Chair Murray Sherwin.

"What surprised us most about the services sector was its deep and extensive linkages with the rest of the economy. Firms on average spend around 40% more on services than they do on wages and salaries. And services now account for over 50% of the value of New Zealand's exports when you include the value of services, such as transport and finance, that are embedded in goods exports.

"Given the centrality of services to our economy, a high-productivity services sector is a must. But unfortunately the productivity performance of New Zealand's services sector lags behind that of other developed countries and shows little sign of catching up. On the plus side, the scope for improvement is significant.

"A healthy level of competition is an important pre-requisite for lifting productivity. It drives innovation and gives consumers more choice, better products and lower prices. But in some parts of the sector competition is subdued – in part a consequence of New Zealand's small market size and geographic isolation.

"The Commission recommends helping consumers drive competition, enabling the Commerce Commission to make greater use of market studies of competition issues in service markets, and reducing barriers to overseas firms supplying services in New Zealand. We also need to be at the top of our game when it comes to competition law and resolve the long-standing debate around section 36 of the Commerce Act.

"ICT is the modern-day equivalent of earlier revolutionary technologies like steam engines and electricity. Embracing ICT and the opportunities it creates is particularly important for New Zealand's service firms. But firms will struggle to make effective use of ICT if they are unable to access the right mix of business and technical skills. There is scope to improve the supply of ICT skills, for example by enhancing links between business and tertiary education providers.

"Getting the most out of ICT will require flexibility and changes to the way that we do business. New Zealand needs to be open to these changes and embrace the opportunities that they present. Cloud computing is a good example of the productivity benefits that ICT can create. The Commission has made a number of recommendations on regulatory issues that, if left unaddressed, are likely to slow the uptake of cloud computing in New Zealand."

Background

In March 2013, the Productivity Commission was asked to assess the role of services in the New Zealand economy and provide policy options to lift productivity in the services sector. A 1st interim report (July 2013) provided an overview of the services sector in New Zealand, concluding that services are a central component of the economy and that there is significant scope to improve the productivity performance of the sector.

Drawing on submissions received on the 1st interim report, two topics related to services-sector productivity were chosen for in-depth analysis: competition and ICT. A 2nd interim report on these two topics was published in January 2014. The final report brings together the key insights from both interim reports. It contains 81 findings and 31 recommendations. The Commission's research and analysis was supplemented by 56 submissions, 3 roundtables, over 60 engagement meetings and a survey of 1 526 businesses.

Three research papers have also been published that contributed to this inquiry:

- Conway, P., & Zheng, G. (2014). Trade over distance for New Zealand firms: measurement and implications. New Zealand Productivity Commission Working Paper 2014/5.
- Meehan, L. (2014). Structural change and New Zealand's productivity performance. New Zealand Productivity Commission Working Paper 2014/4.
- Meehan, L. (2014). New Zealand's international trade in services: A background note. Productivity Commission Research Note 2014/1.

About the New Zealand Productivity Commission

The Commission – an independent Crown entity – was established in April 2011 and completes in-depth inquiry reports on topics selected by the Government, carries out productivity-related research, and promotes understanding of productivity issues.

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