the new zealand institute

DISCUSSION PAPER 2004 / 2

It's not just about the money:

The benefits of asset ownership

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The New Zealand Institute

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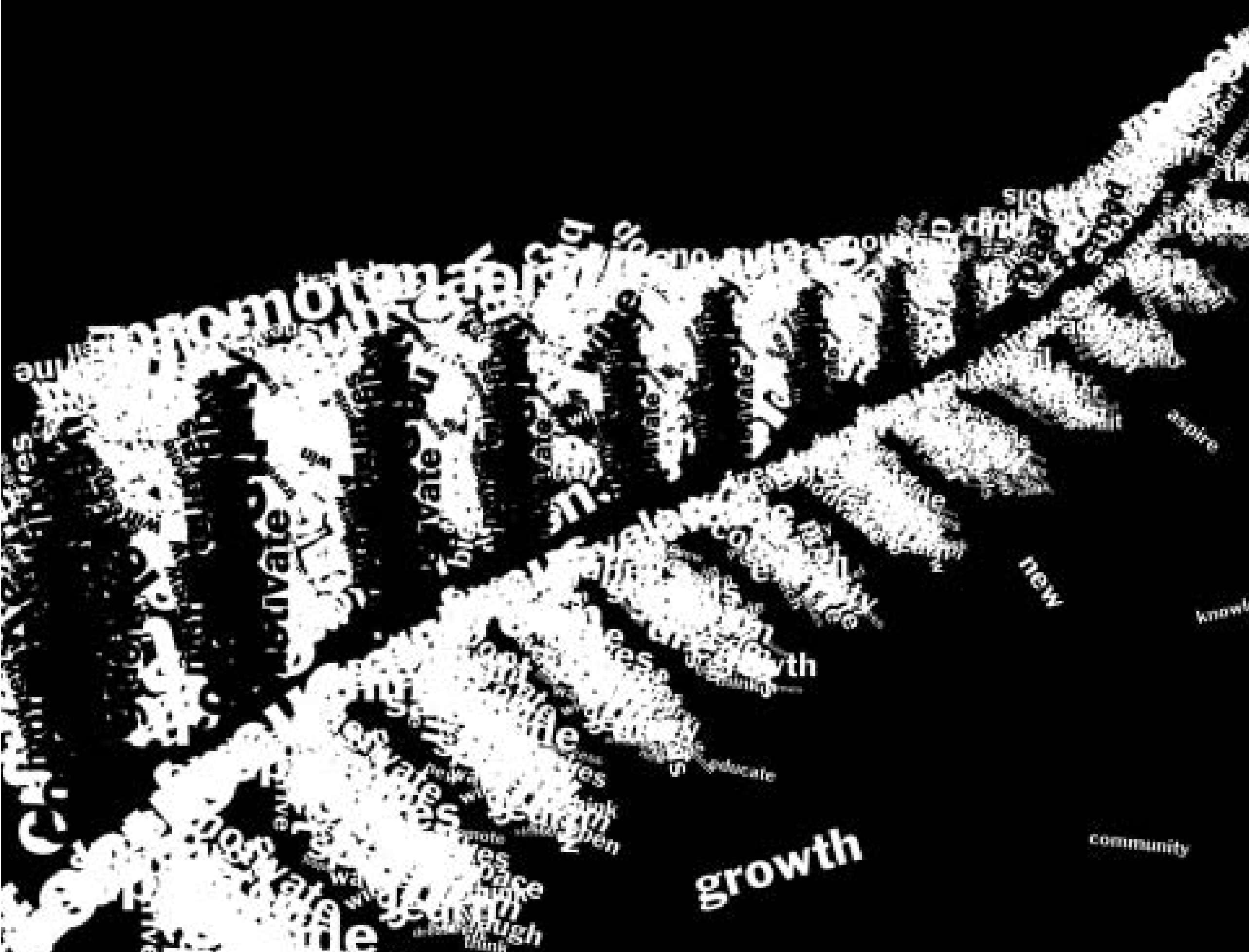
‘It’s Not Just About The Money’ is the second paper in a series that forms part of the New Zealand Institute’s initial research program on Creating an Ownership Society. This paper follows on from our first paper – ‘The Wealth of a Nation’ – which was released in July.



FOREWORD: CREATING AN OWNERSHIP SOCIETY

Asset ownership is increasingly important for meaningful participation in society and the economy. Ownership enhances the ability of people to access opportunities and to invest in the future – by buying a house, financing education, and so on – and allows people to cope with shocks. Assets provide greater security, control, and independence. A broad distribution of ownership also generates enhanced social cohesion at a national level, and ensures that more New Zealanders obtain the benefits of economic growth. So helping all New Zealanders acquire assets will make a significant contribution to New Zealand's economic and social future.

In recognition of the increasing importance of asset ownership, many countries are introducing and expanding 'asset based policies' that assist and encourage people to accumulate wealth. Creating an ownership society, in which ownership of assets is broadly distributed through the population and in which all people are able to accumulate wealth over their lifetimes, is a policy priority across many countries. And such policies are advocated by governments and political parties from across the political spectrum; it is not a policy solely of the left or of the right.

However, many New Zealanders do not have any real wealth holdings. And many New Zealanders – particularly young New Zealanders – are finding it increasingly difficult to advance financially and build an ownership stake; rising house prices and declining home ownership rates, student loan debt, and an emerging debt culture, all make wealth accumulation harder. Further, New Zealand's overall level of household wealth is substantially lower than in most other countries, and this is likely to constrain domestic investment, productivity and growth.

Although New Zealand has historically had policies that assisted people to accumulate wealth – like assisted home ownership – these policies have been removed over the past two decades, and there are currently no deliberate policies that assist New Zealanders to build an ownership stake. This sets New Zealand apart from the international policy mainstream, and increasingly so as countries pursue asset based policies to encourage ownership.

We have chosen 'Creating an Ownership Society' as our initial work program because increasing the number of New Zealanders with an ownership stake – and increasing the overall level of asset ownership in New Zealand - will have a profound effect on New Zealand's economic and social future. We also believe that New Zealand policy settings in this area are increasingly out of date and we want to contribute new and creative thinking to the New Zealand debate, drawing on developments in international policy and thinking. Our focus is on identifying ways in which New Zealanders can be assisted to acquire assets over their lifetime.

So over the next several months, we will be releasing a series of papers examining different aspects of this issue, discussing these issues with New Zealanders, and developing recommendations as to how government, business and community organisations can assist many more New Zealanders to build an ownership stake.

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EXECUTIVE SUMMARY

Many New Zealanders are currently without an ownership stake, and find it difficult to build wealth over their lifetime. The median household wealth in New Zealand is just $68,300, with 800,000 New Zealanders owning less than $20,000. And 16% of New Zealand households have negative wealth, where their liabilities exceed their assets.

It is also likely that the difficulties that New Zealanders face with respect to accumulating wealth will become more pronounced. In particular, young New Zealanders face new pressures, like student loan debt and declining home affordability, which constrain their ability to accumulate wealth. This means that there may be an increasing number of New Zealanders without an ownership stake in the economy.

Asset ownership – or the lack of asset ownership – has profound effects on life outcomes for individuals and for the well-being of communities

The international and New Zealand evidence on the economic and social importance of asset ownership to individuals and communities strongly suggests that this situation is cause for serious concern. Asset ownership has a significant effect on the economic and social outcomes for individuals and for communities.

For individuals, asset ownership provides direct financial benefits in terms of the returns generated. As a result, those who own assets are in a much better position to get ahead financially than those who do not own assets. In this sense, wealth inequality is frequently self-perpetuating. Further, the benefits from economic growth are often capitalised into asset values, so that asset owners benefit disproportionately from growth. Those who own assets – like real estate – get ahead while those without assets may get priced out of the market.

And accessing these return opportunities often requires some initial asset ownership. For example, a deposit is required to buy a home, and initial equity capital is generally required to start a new business. It takes money to make money.

Assets also provide a buffer, which allows people to better manage risks. The insurance provided by asset ownership is becoming increasingly important as the risks that people face become more diverse and the extent of social insurance provided by the government reduces.

The ability to access opportunity and get ahead, and to better manage risks, also generates powerful social and psychological benefits. Asset ownership gives people a sense of control and independence, allows them to focus on the future to a much greater extent, and is an increasingly important determinant of meaningful participation in society. Asset ownership has been strongly linked to better health and employment outcomes, quality of life, marital stability, and educational outcomes for children. Encouraging asset ownership seems an important way in which to build a genuinely inclusive economy.

Widespread asset ownership also has significant community-wide benefits in terms of generating social cohesion and a feeling that everyone has an opportunity to get ahead and build a future. To the extent that people own a house, a business, or financial assets, they are better able to participate meaningfully in society. Indeed, the evidence shows that people who own assets tend to be more involved in their communities. Conversely, communities in which many people do have an ownership stake – and where people feel marginalised – tend to experience worse outcomes.

Many of these benefits have long been understood and have motivated policies across the world, including in post-war New Zealand. But the strength of the evidence, and the importance of asset ownership, seems to be increasing. The implication is that creating an ownership society in New Zealand – ensuring that many more New Zealanders have an ownership stake – will have significant effects on the ability of New Zealanders to participate meaningfully in society.

There is a clear role for deliberate action to create an ownership society

The outcomes that are affected by asset ownership – or the absence of asset ownership – are those in which all New Zealanders have a clear interest. Governments, businesses, and community organisations all have an interest in ensuring that individuals have the opportunity to participate meaningfully in modern society. On this basis, creating an ownership society, and helping all New Zealanders to get ahead financially, ought to be a clear policy priority for government, as well as for business and community organisations.

The creation of an ownership society, in which many more New Zealanders are accumulating assets and building wealth, will require policy assistance and encouragement. This is a clear lesson from the New Zealand experience over the past decade, where successive governments have pursued a hands-off approach to wealth accumulation and relied on individual decision-making. This approach has contributed to a situation in which many New Zealanders are struggling to accumulate wealth, home ownership rates and household financial wealth are declining, and household savings are low, despite the strong economic growth over the past decade.

There are three primary reasons that a hands-off approach to policy is inadequate.

First, the evidence is clear that savings and wealth accumulation is an area in which people do not make fully rational decisions. Many people find savings hard, and so policies and institutions that make the savings decision easier – for example, through default enrolment into savings schemes – generate much improved outcomes. Although helpful, relying on income growth, tax cuts, or financial education in isolation will be insufficient to increase savings significantly – as the New Zealand experience over the past decade has shown. Rather policies that deliberately allow for income growth to be converted into wealth are required.

Second, some New Zealanders lack the income to be able to save and accumulate wealth. Assisting low income New Zealanders to accumulate assets is likely to require policy assistance. The standard way in which New Zealand governments have achieved redistributive objectives is through

income transfers. But to an increasing extent, meaningful participation requires asset ownership and cannot be achieved simply through income transfers. This is why asset building initiatives in low income communities have been implemented or are under consideration in many developed countries.

And third, people do not consider the community-wide benefits to asset ownership when they are making individual decisions. As a result, encouraging asset ownership may improve overall community well-being.

The importance of deliberately encouraging asset ownership is recognised in all other Anglo countries – and most other OECD countries – where a wide range of policies exist to enable people to build an ownership stake.

In sum, asset ownership matters profoundly for both individuals and communities – and improving these outcomes is something that ought to be a key priority for the private and public sectors. And there is a strong case for the government to prioritise the creation of an ownership society and implement policies to encourage wealth accumulation – as indeed New Zealand governments have done in the past.

1 INTRODUCTION

Many New Zealanders are currently without an ownership stake, and find it difficult to build wealth over their lifetime. The median household wealth in New Zealand is just $68,300, with 800,000 New Zealanders owning less than $20,000. And 16% of New Zealand households have negative wealth, where their liabilities exceed their assets.

It is also likely that the difficulties that New Zealanders face with respect to accumulating wealth will become more pronounced. In particular, young New Zealanders face new pressures, like student loan debt and declining home ownership rates, which act to constrain their ability to accumulate wealth. This means that there is likely to be an increasing number of New Zealanders without an ownership stake in the economy.[1]

But should the ownership situation of New Zealand households be seen as a source of particular concern, and should improving these outcomes be a top policy priority for the government? There are many competing demands for policy attention. And is there a case for the government to deliberately improve this situation by introducing policies that assist and encourage asset ownership, or is this something that should be taken care of by individuals?

The first part of this paper reviews the New Zealand and international evidence on the economic and social effects of asset ownership on individuals and communities.[2] There is a large and growing body of evidence that documents the profound importance of asset ownership for people and the communities they live in, and also some suggestion that asset ownership is becoming more important over time.

This evidence suggests that New Zealand's current position is cause for significant concern – and also that improving the ownership position of New Zealanders and creating an ownership society is something that is likely to generate substantial benefits.

The second part of the paper examines whether the creation of an ownership society ought to be a key policy priority for New Zealand governments. Should the government be deliberately focused on ensuring that many more New Zealanders are able to accumulate assets – as governments in all other Anglo countries do – or is this something that will happen naturally as incomes rise?

The key arguments for a deliberate focus on encouraging asset ownership are examined. For example, in terms of assisting low income people to get ahead, is encouraging and assisting asset ownership an important complement to the traditional focus on income transfers? And the paper draws on behavioural economics to examine whether individuals tend to make appropriate savings decisions. Taken together, these arguments – and the evidence on the effectiveness of policies that encourage wealth accumulation – provide a serious challenge to New Zealand's current hands-off approach to wealth accumulation.

[1] These data are described and discussed in detail in Skilling & Waldegrave (2004).
[2] A future paper will outline the importance of household saving and wealth accumulation for investment, productivity, and economic growth.

2 PRIVATE BENEFITS FROM ASSET OWNERSHIP

INTRODUCTION

This section examines the benefits that individuals and households receive from asset ownership in terms of both direct financial benefits as well as in terms of broader well-being.

One important reason for saving and accumulating assets is to provide retirement income. There has been considerable debate in New Zealand as to whether New Zealanders are saving sufficiently to enable them to maintain their standard of living after they retire. Although there are no obvious problems currently among the retired population, it is not clear that future cohorts of elderly people will be in such a position. Home ownership rates are declining, savings rates are low, and uncertainty remains over the level of national superannuation in the future. So it is not obvious that we should be relaxed about the level of retirement savings by New Zealanders.

However, although saving for retirement is an important motivation for asset accumulation, this paper focuses on the increasingly important role that asset ownership plays during an individual's life.

The idea that assets are accumulated for reasons in addition to saving for retirement has long been recognised. In 1936 John Maynard Keynes noted that in addition to saving for retirement, people save in order to build "a reserve against unforeseen contingencies" and "to enjoy a sense of independence and the power to do things, though without a clear idea or definite intention of specific action". And many people save for to finance a bequest or for a down-payment or a deposit on a home, car and so on.

This is why life cycle approaches to saving can only explain about half of people's saving behaviour – there are many other motivations for saving. So even if there were a very generous public pension, this does not mean that the optimal level of household saving is zero.

Broadly speaking, assets generate benefits in terms of their ability to:

- provide individuals with an ability to access opportunity and make investments that yield a return in an independent manner
- provide a buffer that allows people to deal with risk.

These benefits have a direct financial effect. But at least as importantly, the ability of assets to allow people to access opportunity and manage risk provides people with a far greater degree of control over their lives, and this generates powerful social and psychological benefits. The benefits of asset ownership extend far beyond the financial outcomes. This section begins by describing the role that asset ownership plays, and then surveys the evidence on the social and psychological effects of asset ownership.

ACCESSING OPPORTUNITY

The first way in which asset ownership matters is that, in general, assets generate a rate of return. Those who own assets obtain a benefit in terms of interest and often capital gains. Asset ownership, then, can be self-perpetuating just as debt accumulation can be self-perpetuating.

Investing in home ownership, for example, has been the traditional method of wealth accumulation in New Zealand. Generations of New Zealanders have benefited from home ownership, paying off the mortgage and benefiting from the capital gain over this period. And over the past few decades, homes have generated good returns for many. Those who have had a housing asset have generally done well, whereas non-home owners haven't been able to get ahead to the same extent and many are finding it more difficult to get into the housing market. Indeed, home ownership rates have declined sharply over the past decade particularly among the young.

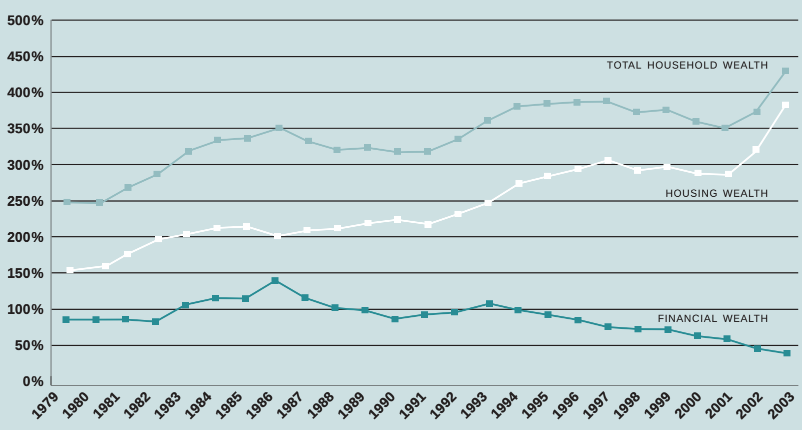
Indeed, as Figure 1 shows, a large component of the increase in household wealth over the 1990s was driven by increases in the value of real estate rather than saving out of wage income – and particularly over the past few years.

The financial advantages of asset ownership generalise beyond home ownership. Asset owners in New Zealand have been able to access returns and to get ahead financially in a way that non-asset owners have not. Returns to asset ownership – interest bearing deposits, returns to equities, appreciation in house prices – have consistently exceeded wage growth over the past twenty years. Of course, this is not the case for everyone. In some areas, housing prices have declined and many shares lost significant value as a result of the 1987 Sharemarket Crash. But it is generally true.

Given that New Zealand's home ownership rates declined sharply between 1991 and 2001 (from 74% to 68%), the increase in housing wealth has benefited a declining share of the New Zealand population. And the returns to financial assets have benefited the 20% of New Zealand households who own financial assets. The compounding nature of asset ownership means that New Zealand's wealth inequality is likely to have risen substantially over the past decade – as indeed it has in most other Anglo countries.

Moreover, asset owners are likely to benefit from economic growth to a greater extent than non-asset owners. Many of the benefits from higher rates of economic growth are capitalised into asset values. For example, Grimes et

FIGURE 1: HOUSEHOLD WEALTH AS A % OF DISPOSABLE INCOME



Source: Reserve Bank of New Zealand

"[My partner bought a house in] Kaikoura [under the rent-to-buy scheme] – just to have an asset – something to leave the kids in the future. The way the market is at the moment, I think it was a pretty good idea."

MALE, 35, CHRISTCHURCH, DE FACTO
2 CHILDREN, HOMEOWNER, $30,000 - $50,000

"What saved us was that I joined the superannuation scheme before I turned 30. I paid 1/5th of my wages in superannuation every week – it was a battle sometimes. It's that that has made our life the way it is – travel, our house – it would have been a different type of lifestyle otherwise. Others in the super fund pulled out and I know what state they're in and they wish they hadn't."

MALE, 81, PALMERSTON NORTH

al. (2003) find that real economic growth in a particular New Zealand region has an approximately proportionate effect on regional house prices; a 1% increase in real income leads to about a 1% increase in house prices. This empirical regularity is also observed in many other countries, and has been long documented in the US.

This means that the benefits from economic growth are unlikely to be evenly spread. Indeed economic growth can disadvantage those who don't have a large asset ownership position as it becomes more difficult to buy assets, like a house. Although economic growth should also lead to wage growth, for most New Zealanders these gains haven't come close to the returns on asset ownership. So, there are real financial advantages to asset ownership. Benefits accrue to those who have assets, and to this extent wealth inequality is likely to be self-perpetuating.

But not everyone has equal access to these return possibilities. Often it takes money to make money. For example, to get into home ownership requires a deposit and starting a small business frequently requires some initial equity capital. Some people can't afford to become asset owners. This is particularly evident in the housing market, where many people – particularly young people – are unable to assemble the required deposit to get into the housing market and so are unable to access the returns generated by home ownership.

In terms of starting a small business, there is New Zealand evidence that home ownership is an important source of collateral for financing small business. Thorp & Ung (2000) note estimates that between 10% and 20% of housing loans are used to finance small business. This means that the declining rates of home ownership in New Zealand, particularly among young New Zealanders, may constrain the ability of a growing number of people to finance the establishment or expansion of small businesses.

Similarly, international studies commonly find that the level of asset ownership matters for starting a new business and becoming an entrepreneur. Blanchflower (2004) describes consistent international empirical evidence that wealth does matter significantly in terms of the probability of starting a business.

To an increasing extent, then, asset ownership has a profound effect on the opportunities open to people and affects the ability of people to participate meaningfully in society and the economy. For example, people without assets are much more limited in their ability to invest in the future – by buying a house, for example, or financing long-term investments like education – because they cannot access sufficient funds for the initial investment.

Although the deregulation of credit markets has reduced the need for down-payments and has reduced the size of the deposit on a house, for many people affordability remains a problem and asset ownership remains important. Some deposits are still required for many investments, some people cannot access credit – or can only do so at very high rates of interest.

As a result, asset ownership is a key factor in economic advancement, because people need command over a certain amount of assets in order to make positive investments. Indeed, asset ownership is particularly important for those on low incomes as a way of getting ahead.

This is why generational transfers of wealth have a significant effect on life outcomes – they affect the opportunities open to people. Asset ownership allows people to transfer wealth across generations and provide an advantage to the next generation. Michael Sherraden notes that "asset accumulation enables the next generation to begin their lives with resources and therefore opportunities. This is important because social development is something which occurs across generations, not only within them" (2003, p. 29). Conversely, the absence of inherited wealth can act as a source of disadvantage.

"I think trying to get into the house market these days is hard and the longer you are not in it, the harder it is to get in."

FEMALE, 31, AUCKLAND, RENTER

"...it is hard for people to get the deposit together to break into the housing market."

FEMALE, 26, WELLINGTON, HOMEOWNER

"I am frustrated that I can only rent as it is dead money but I have no other choice ...I don't have the money for the deposit anyway. It is a really depressing situation..."

MALE, 23, AUCKLAND, UNEMPLOYED

"...it's extremely difficult for people to make the commitment without sufficient funds for a deposit. There are lots of people out there with the financial position to pay the weekly mortgage but don't have the deposit."

MALE, 38, AUCKLAND, MARRIED

"...it's not difficult – it's just getting the deposit that's difficult. The rent we're paying at the moment will cover any mortgage"

MALE, 41, AUCKLAND, MARRIED

"I don't know when I will ever be able to own a home... I will be looking at the price of houses, the [student] loan factor, it's going to be such a long time before I can get a deposit."

FEMALE, 25, WELLINGTON, $25,000 STUDENT LOAN

PRECAUTIONARY SAVING

A second major benefit of asset ownership is an enhanced ability to manage risks and meet the costs associated with negative events. For example, losing employment income, having to repair your car or fridge, or having a sickness in the family, may all impose unexpected financial costs. Asset ownership enables people to finance these costs and to manage risks in a more flexible, controlled manner.

"When we got married people gave us cheques and after our honeymoon, £30 was left over. My husband gave it to me to do whatever I liked ...Where we lived ...there was only a general store and post office, so I put it in the post office. That turned out to have been one of the best things I ever did ...The post office savings bank account followed me all my life."
FEMALE, 79, PALMERSTON NORTH

"My mum received an inheritance that was enough for a house deposit, so we decided to buy a house when I was 22."
FEMALE, 26, WELLINGTON

Without a pool of assets, such events may impose real hardship on people. For example, if you don't have liquid assets to pay to fix your car when it breaks down, you may be unable to continue working – or to take a job in the first place – on the other side of town because you can no longer get there. And the only responses open to people may be expensive – for example, using a taxi or paying high rates of interest to obtain unsecured personal finance.

An inability to respond efficiently to shocks may make it very difficult to get ahead. People without assets are far less resilient to shocks; every time a negative event occurs they get knocked back and it may be difficult to recover. Asset ownership provides a buffer that allow for income to be stabilised and reduce the chances that a shock will throw people into income poverty or into debt.

Of course, private asset ownership is not the only means of managing risk. One of the major roles of the government – in New Zealand, as in other developed countries – has been to provide social insurance through income transfers (e.g. unemployment benefit, sickness benefit, retirement income) and the public provision of health care. Indeed, the welfare state in New Zealand and overseas has expanded over the past century in response the demand for insurance against new risks (James (1992), Rodrik (1998)).

However, the extent of the insurance provided by the government is very partial for many. For example, the unemployment benefit represents a low proportion of many people's current income and is inadequate to allow many to maintain their consumption levels. And internationally, as in New Zealand, fiscal pressures have led to reduced generosity of social insurance. More generally, the insurance provided through the welfare system does not cover many of the increasingly pervasive and diverse risks that people face today. These changes mean that individuals are effectively bearing more risk. It is difficult for any welfare system to adapt itself to the different circumstances of a diverse population. So although social insurance will continue to play an important role in shielding people from risk, it is increasingly insufficient to cover all of the major risks that people face.

Another way of managing risks is through private insurance. Indeed, many New Zealanders have private health insurance and income protection insurance – as well as insurance for vehicles, house and contents. This is partly a response to the reducing coverage of social insurance.

But this private insurance is often far from perfect, and people will generally continue to absorb a portion of any loss. Moreover, in many cases, markets do not exist to allow people to offload important risks through insurance or other means. For example, human capital – the value of a person's lifetime earnings potential – is the most important asset that most people have and yet comprehensive private markets do not exist to insure against negative earnings shocks and so on. And for many smaller risks, such as a car or a fridge breaking down, there are no real insurance products available, and people have to bear these costs out of pocket.

In such an environment, asset ownership can provide a powerful insurance function. Indeed, precautionary savings is an important motivation for saving, although exact estimates of the magnitude vary significantly.

And the case for building an asset buffer is increasing. At the same time as the generosity of social insurance coverage is reducing, the risks that people face are increasing and becoming more diverse. As examples of this, consider changes in family structure and the nature of work.

The possibility of changes to family structure (e.g. through divorce or death) is a source of substantial risk and uncertainty. Variation in family structure is an influential determinant of poverty and income inequality; for example, 67% of children in single parent households live in poverty compared to 19% of children in two parent households (Ministry of Social Development (2003)). Further, there is less insurance within households headed by a single person as there is no other source of earnings to fall back on. This makes these households less resilient to shocks. This is a particular problem for New Zealand, which has one of the highest rates of single parent households in the OECD (OECD (2002)).

Moreover, although New Zealand's recent economic performance has been strong and stable, with low unemployment, New Zealanders continue to face economic risks. New Zealand has very high rates of employment and firm turnover (Carroll et al. (2002), Simmons (2002)), and there are high rates of 'precarious employment' (Department

THE TRANSFER OF HEALTH CARE FINANCING

The private share of health spending in New Zealand has increased significantly over the past two decades. In 2002, 23% of health costs were financed privately, up from 18% in 1991 and 12% in 1980. Between 1990 and 2001, overall health spending increased by about 60% in real terms. Over this period, private health spending grew by 111% in real terms, with much slower growth in public spending.

Between a third and a half of the adult population have some private health insurance coverage. However, of the 23% of health spending that is private, only 6% is covered by private health insurance – the remainder is 'out of pocket' expenses.

Sources: OECD (2003b), Ministry of Health (2003)

"At least with assets you have something for a rainy day."
MALE, 54, PALMERSTON NORTH

"I think it's a good idea to save and I want to have a buffer all the time rather than live from week to week like I have before. I want financial security and independence so I am saving for the sake of saving rather than for a specific goal as in the past."
FEMALE, 24, WELLINGTON

"I always ensure that I have [a certain amount] in my saving account; it is my safety net. If I go below (for example when I bought my car), I will save until I am back to my minimum ...It's a degree of protection, degree of peace of mind, I feel I am not at the mercy of my employers or of any drastic economic changes."
MALE, 40, AUCKLAND

"My job's finishing at the end of this year – so, I need savings for living costs while I am job hunting..."
FEMALE, 24, CHRISTCHURCH
SINGLE, RENTER, $30,000 - $50,000

of Labour (2002)). This means that many New Zealanders face a high probability of a negative employment income shock.

The increase in the incidence of household risk is an international trend, and has been widely remarked upon (Hacker (2004)). Mandel (1996) argues that economic insecurity has become a fact of life for countries, companies, and individuals. This phenomenon is not restricted to those at the bottom of the income distribution; it is pervasive, and even well educated, high income individuals are subject to risk and uncertainty. In many ways, this increased risk is the result of creating an efficient, dynamic economy that responds rapidly to changing circumstances.

So overall incomes are rising, but the distribution of possible outcomes for each individual has also risen. Individuals are more likely to experience an unexpected reduction in living standards; for example, due to unemployment or a new job with reduced pay and conditions. As a result, the security that assets provide will become more important and asset ownership will become an increasingly important determinant of how well New Zealanders can provide for themselves.

Further, the confidence instilled by having an asset buffer to fall back on should increase people's propensity to take risks, because bad outcomes can be managed. People who have an ownership stake will be more inclined to start a business, change careers, and so on if they have some protection against things not working out. This dynamic, risk-taking behaviour is important for both individual and national economic success.

THE IMPACT OF ASSET OWNERSHIP ON HOUSEHOLD WELL-BEING

The ability to access opportunity and manage risks that is generated by asset ownership leads to powerful social and psychological benefits for individuals and households. These social and psychological benefits are at least as important as the direct financial benefits that are generated by asset ownership.

There is a substantial body of international evidence that asset ownership, by allowing people to access

> *"In fact, we generally have excellent reasons for wanting more income or wealth. This is not because income or wealth are desirable for their own sake, but because, typically, they are admirable general purpose means for having more freedom to lead the kind of lives we have reason to value. The usefulness of wealth lies in the things that it allows us to do – the substantive freedoms it helps us to achieve."*
>
> AMARTYA SEN, 1999

opportunity and manage risks, matters profoundly in terms of giving people a much greater sense of independence, control and security over their lives and also a much greater sense of being able to plan for the future (OECD (2003a)). Indeed, asset ownership is an important part of ensuring that people can participate meaningfully in society.

Asset ownership is strongly linked with improved life outcomes for individuals and households, as well as with a range of psychological benefits in terms of things like greater security and a sense of control.

US academic Michael Sherraden notes that "To mention only a few examples from research, there is convincing evidence that, controlling for other factors, homeownership is associated with residential stability, maintenance and upkeep of the home, and social and political involvement at the local level. There is convincing evidence that, controlling for other factors, home ownership and financial assets are associated with marital stability and reduced domestic violence. There is convincing evidence that, controlling for other factors, homeownership and financial assets are associated with higher educational attainment in children" (2001).

Scanlon & Page-Adams (2001) provide a comprehensive survey of the international evidence on the impact of asset ownership on a range of outcomes. They find that asset ownership:

- Reduces the probability of marital dissolution
- Is associated with mental and physical health of family members
- Is associated with the economic stability of families
- Leads to improved educational outcomes for children (particularly due to home ownership)
- Leads to a reduction in intergenerational poverty

In a recent UK longitudinal study, John Bynner (2001) analysed the effect of assets on life outcomes. The study provided information on asset holdings at age 23 and Bynner used this information to test the effects of these assets on outcomes at age 33, controlling for a battery of other personal characteristics that might also affect these outcomes. Bynner found that asset ownership was robustly linked to:

- Fewer years in unemployment
- Reduced probability of marital breakdown
- Good health and absence of depression
- Political interest, trust in the political system, and work ethic

Drawing in part on this work, HM Treasury (2001) note that "Research shows that young people without assets are more likely to have lower earnings, higher unemployment and poorer life chances overall. Conversely,

"I am not looking ahead because all I can see is my debts... It would be difficult to put aside an extra amount. At this moment, we have to manage on $100-$150 per week – so, you can't really save on that!"
FEMALE, 33, AUCKLAND, 3 CHILDREN

"I can't get ahead in life – it's a real struggle. A property gains significant value, savings mean you have more opportunities and choices in life."
MALE, 32, AUCKLAND

"I would like not to be worrying about making ends meet all the time or living pay-cheque to pay-cheque."
FEMALE, 28, AUCKLAND

"We decided to buy a home as we were renting. In five years, we rented six houses. We realised it was a stupid situation, especially with a young child. Owning a house provides financial security and stability for now and for the children's future."
PROFESSIONAL FEMALE, 40, AUCKLAND
MARRIED, 3 CHILDREN

"I now own my house (mortgage free)… I feel more secure, I know my children will inherit my assets, it is good to know…"
FEMALE, 66, AUCKLAND

those with assets have improved prospects in life – not just because savings provide both a financial buffer against rainy-day needs and a source of financial independence and opportunity, but perhaps also because the very act of saving encourages greater self-reliance, forward-planning and an increased willingness to make personal investments".

And asset ownership is also strongly associated with changes in people's attitudes, world-view, and the ways in which they engage and interact with the world around them. Sherraden (2001) observes that the evidence demonstrates that "when people begin to accumulate assets, their thinking and behaviour changes as well. Accumulating assets leads to important psychological and social effects that are not achieved in the same degree by receiving and spending an equivalent amount of regular income. These behavioural effects of asset accumulation are important for household well being. They are likely to include more long range planning, better care of property, increased learning about financial affairs, and increased social and political participation".

Page Adams & Sherraden (1996) summarise findings from 25 academic studies addressing the personal and social effects of asset holding. They note that these studies consistently document a link between asset ownership and outcomes such as life satisfaction, a sense of independence, greater economic security, a greater focus on the future, and reduced depression and problematic alcohol use. Asset ownership has also been linked to reduced stress, and greater marital stability. Further, they note that "some of the strongest and most consistent empirical evidence for the positive effects of assets come from studies involving outcomes for children", in particular in terms of outcomes like improved self-esteem and educational outcomes.

Recent Australian research examines the link between wealth holdings and self-reported measures of 'well-being' and 'ill-being' (Headey & Wooden (2004)). This study found that wealth exerts a much stronger effect than income on reported well-being – and a particularly strong effect in terms of improving the score on reported ill-being. Accumulated wealth seems to be valued more highly than a high income. The authors attribute this stronger relationship to the heightened feeling of economic security afforded by asset ownership.

Asset ownership also provides people with a much greater sense of control and independence, and "fundamentally allows people to take control over many aspects of their lives" (Allen Consulting Group (2003)). Consistent survey evidence suggests that asset ownership enables people to look beyond the immediate and make longer term plans for the future, which has both economic and social benefits. Sherraden (1991) contends that "assets create an orientation towards the future" as distinct from "present-oriented survival strategies".

For example, the commencement of savings and becoming an asset owner often lead to changes in habits and behaviours. For example, participants in programs that encourage asset ownership among people who haven't previously engaged in savings or asset accumulation often become regular savers with a view to achieving future goals (Kempson et al. (2003)).

The social benefits associated with home ownership are particularly well documented (Scanlon and Page-Adams (2001)). Beneficial outcomes of home ownership include higher rates of self-reported life satisfaction and enhanced social status, behavioural changes to protect investments, and residential stability (which contributes to improved educational outcomes for children).

Conversely, a lack of asset ownership can generate negative outcomes. Williams & O'Brien (2003), for example, document the negative outcomes associated with being in debt, particularly in terms of the negative effects on emotional well-being. Debt is often associated with increased stress, depression, and feelings of low status and self esteem.

"The disadvantage of having no assets is real deep insecurity of tenure, which is quite stressful. Another significant thing is my perceived low social status. So, the big advantages of assets in my opinion are secure tenure and status."
MALE, 42, AUCKLAND, UNEMPLOYED

"Lack of financial security obviously, and lack of flexibility should a family member or myself fall sick."
FEMALE, 23, MELBOURNE, STUDENT

"Well I can't earn money off any assets that I do not hold, so it really comes to not having added security which these assets would provide."
FEMALE, 27, LIVING OVERSEAS

"If I get into any money trouble I have nothing to fall back on."
MALE, 21, CHRISTCHURCH, STUDENT

"My family and I simply have nothing solid, no place to go back to... I have no security."
FEMALE, 39, AUCKLAND
SINGLE PARENT OF 5 CHILDREN

"It is very frustrating, we have no asset to fall back on, nothing to sell if we need money."
FEMALE, 35, AUCKLAND, MARRIED, ONE CHILD

AMERICAN DREAM DEMONSTRATION PROGRAM OUTCOMES

The American Dream Demonstration program opened 'individual development accounts' (IDA's) for over 2000 people in 13 US cities between 1997 and 2001. This is a matched savings programs, where savings were matched by the sponsoring organisations with the funds being used for home purchase or repair, microfinance or post-secondary education. Participants often had no background of saving prior to participation. The average participant in the program accumulated about $700 a year, including the matched component.

REPORTED EFFECTS OF IDA PARTICIPATION BY SURVEY RESPONDENTS

- Economic effects: 59% of respondents strongly agree or agree that they are more likely to work or stay employed; 41% work more hours; and 73% buy or renovate a home.
- Education: 60% strongly agree or agree that they are more likely to make educational plans for their children; and 59%, educational plans for themselves.
- Psychological effects: 93% of respondents strongly agree or agree that they are more confident about the future; 84% are more economically secure; and 85% are more in control of their lives.

COMMON THEMES IN EXTENDED INTERVIEWS WITH IDA PARTICIPANTS

- The IDA program "creates goals and purpose"
- Participants can "see more clearly" and "visualise a future"
- The IDA program also provides a "road map" and a "way to reach goals"
- In sum, respondents identify the IDA program structure as changing both outlook and behaviour related to saving and reaching life goals.

Sources: Schreiner et al. (2002), Sherraden (2002), McBride et al. (2003).

In interpreting this international evidence, it is important to consider the possibility that the causality might run in the other direction. That is, it may be that, say, more optimistic people are more likely to accumulate assets – and so asset ownership may not produce these characteristics as much as be the product of them.

However, considerable care has been taken in the above studies to control for these characteristics and to identify causality properly. So, it seems likely that the causal relationship runs much more strongly from assets to positive outcomes, than in the other direction. Further, the consistency of the results across countries, contexts, and multiple independent studies gives greater confidence in the robustness of the results. And the results accord with intuition.

SUMMARY

In sum, asset ownership generates powerful economic and social benefits to individuals and households. In an economic sense, assets position people to access opportunity and enable people to get ahead. Indeed, differences in wealth holdings have a tendency to become self-perpetuating and have inter-generational effects. For example, over the past few decades, New Zealand home owners have been able to get ahead financially to a greater extent that those who have not been in a position to own a home. Asset ownership is also becoming increasingly important in managing risks as public provision reduces in generosity and as people are exposed to an increasing range of risks.

And asset ownership has profound effects on the life outcomes experienced by individuals. The international evidence consistently links asset ownership to improved health, employment, psychological, and educational outcomes, as well as to enhanced quality of life and greater sense of control and independence. This contributes to a greater focus on investing in the future.

So whereas standard economic theory treats asset ownership simply as deferred consumption, there is increasing evidence that asset ownership generates substantial additional benefits. To the extent that many New Zealanders are unable to accumulate assets over their lifetime, their ability to exert control over their lives is reduced – with implications for a range of life outcomes and the well-being of individuals and households.

This evidence shows clearly that we ought to be concerned that many New Zealanders do not have an ownership stake, and struggle to accumulate wealth over their lifetimes. The appropriate response is to investigate how many more New Zealanders can best be assisted and encouraged to build an asset ownership stake.

3 BENEFITS TO THE COMMUNITY

INTRODUCTION

The previous section has described the profound effect that asset ownership has on social and economic outcomes for individuals and households. But in addition to these benefits, there are economic and social benefits that accrue at a community and national level from broadly distributed asset ownership. In other words, there are powerful positive externalities associated with asset ownership.

The basic idea is that because asset ownership affects the ability of people to participate meaningfully in society, broadly distributed asset ownership can have a positive effect on social cohesion and stability. Conversely, a situation in which many people do not have an ownership stake may create problems and tensions to the extent that non-asset owners feel less able to participate and less a part of society. Indeed, political philosophers from Aristotle to Alexis de Tocqueville to John Rawls have identified asset ownership as an important element for economic and social participation by individuals and for the functioning of communities.

This section explores two broad, and related, effects that asset ownership has on the functioning of society. The first is that a population in which most people have an ownership stake is likely to be more cohesive, as people are able to participate on more of an equal basis. The second benefit is that where more people have an ownership stake, there are more people with a direct interest in the success of the community and who are more likely to invest in the community.

> *"Where the middle class is large, there are least likely to be factions and dissension."*
> ARISTOTLE, 306 BC

> *"But the most common and durable source of factions has been the various and unequal distribution of property."*
> JAMES MADISON, 1787, FEDERALIST PAPERS NO.10

SOCIAL COHESION AND STABILITY

Asset ownership generates a series of benefits to individuals, which enhances their ability to participate in society in a meaningful way. That is, asset ownership provides people with a sense that they can operate in much the same way as other people in society.

The insight that broadly distributed asset ownership and a property owning middle class is an important element of a cohesive and functioning society is not new. Over 200 years ago, de Tocqueville noted "the general equality of conditions" in early American society – as compared to European society at the time – and linked this to more active civic participation and engagement because people had a greater incentive and more resources to engage in the political process. Indeed, economic democracy is often seen as an important complement to political democracy.

Similarly, political philosopher John Rawls, in the preface to the revised edition of A Theory of Justice, draws a sharp distinction between a property owning democracy and a welfare state. Whereas a welfare system focuses on "redistributing income", a property owning

democracy focuses on "ensuring the widespread ownership of productive assets and human capital" and thereby putting "all citizens in a position to manage their own affairs and to take part in social cooperation on a footing of mutual respect under appropriately equal conditions" (1999). Indeed, the idea that asset ownership generates increased social influence and greater peer recognition has been widely noted (Sherraden (1991), Saunders (1990)).

Where people have an ownership stake in the country, political stability and better overall outcomes are likely. Conversely, a situation in which many people don't have a stake may generate social tension and pressures, as people don't feel that they can participate in society on the same basis as other people.

This idea has motivated policy settings across a range of countries. In the US, for example, Lind (2004) observes that successive governments have deliberately created and supported a property-owning middle class through encouraging widespread asset ownership over the past couple of centuries. Ray Boshara (2003) describes some of these asset building programs; "The Homestead Act of 1862, for example, offered 160 acres of land to every American – rich or poor – who was willing to occupy and cultivate it for five years. And the GI Bill of 1944 helped millions of Americans get a college education or

THE DARK SIDE OF HOME OWNERSHIP?

There are obvious benefits to social capital associated with home ownership, but there may be some negative effects as well. For example, some have argued that home ownership is linked to higher rates of unemployment, because home ownership may lock people into particular locations even if the jobs have moved elsewhere (Oswald (1996, 1997)).

However, more recent work casts doubt on the strength of this claim. Glaeser & Shapiro (2002) find little US evidence to support the Oswald claim, and tend to believe the opposite to be true with home owners having lower rates of unemployment than non-home owners. And Flatau et al. (2003), using Australian micro-data, find that home owners have lower unemployment rates and are quicker to exit unemployment than are renters (partly perhaps because of the financial pressure to continue to pay the mortgage).

buy a first home. These programs greatly equalised the distribution of wealth in America – not by punishing the rich but by expanding opportunities and the ownership of assets".

The argument that asset ownership has community-wide benefits has had particular application in the context of home ownership. In addition to home ownership being a powerful vehicle for wealth accumulation, it significantly affects other types of behaviours and has a profound impact on the functioning of neighbourhoods and communities. In particular, the evidence suggests that home owners feel much more anchored in the community and make more of a contribution to that community.

As Alan Greenspan recently noted "The choice to buy a home is a decision to plant a family's roots in a community with all the implicit incentives to make that community thrive. Where home ownership flourishes, it is no surprise to find increased neighbourhood stability, more civic-minded residents, better school systems, and reduced crime rates" (2002). There are obvious benefits to social capital associated with home ownership; people who expect to live in an area for a while are more likely to invest in developing relationships in the community than those who only expect to stay for a few months.

Indeed, home ownership has been strongly and consistently linked to greater community involvement in terms of things like participation in voluntary organisations and local political activity. After controlling for income, education and other personal characteristics, homeowners are more likely than renters to participate in voluntary neighbourhood organisations and to engage in local political activity. Glaeser & Shapiro (2002) cite evidence that homeowners are more likely to vote locally and also note that areas with high rates of home ownership are likely to have more spending on schools. This is consistent with the prediction that home owners will support long-term investments that will have a positive impact on property values. And Glaeser & Sacerdote (2000) provide strong empirical evidence that home owners are much more likely to vote in local

"My wife wanted [the house] as a symbol – [buying a house] is something you do here – there's a level of participation and belonging that comes with a house – once you're in, you're in – you can play the game."

MALE, 43, CHRISTCHURCH, MARRIED
3 CHILDREN, HOMEOWNER, $75,001 - $100,000

"The advantages [of having assets] are participation and being able to contribute to whanau things like tangis – spread it around a bit."

MALE, 43, CHRISTCHURCH, MARRIED
3 CHILDREN, HOMEOWNER, $75,001 - $100,000

elections, to work to solve local problems, and to maintain their property.

Overall Glaeser & Shapiro (2002) find that there is some evidence "that homeownership creates positive spillovers for near neighbours. Homeowners do appear to be more active citizens. They vote more. They take better care of their homes. Houses that are surrounded by homeowners are worth a little more than houses that are surrounded by renters."

Conversely, an absence of home ownership can lead to a sense of alienation from the surrounding community. Robinson (2004), in a survey of Salvation Army staff across New Zealand, notes the common observation that "for some clients this [the lack of home ownership] can bring with it a sense of disenfranchisement from the community. Clients feel no sense of ownership or belonging. They have no stake in the area in which they live and know it is likely that they will soon be moving" (p. 8).

Indeed, policies to encourage home ownership have been implemented by many countries with a view to create a property owning democracy and to give people a stake in society and the economy. For example, assisted first home ownership in Australia and the sale of public housing to tenants in the UK under Margaret Thatcher in order to broaden ownership (Saunders (1990)).

Similarly, New Zealand has a history of encouraging home ownership. And with considerable success; New Zealand's home ownership rates were among the highest in the developed world. These policies were motivated by a sense that high rates of home ownership lead to social stability as well as generating benefits for the individuals concerned (DTZ (2004)). The New Zealand government's 1950 White Paper on Housing stated that the government considered that home ownership "develops initiative, self-reliance and thrift and other good qualities which go to make up the moral strength of the nation…above all, home ownership permits responsible citizenship".

However, the community benefits of asset ownership are not just restricted to home ownership. Other forms of asset ownership – such as a small business or financial assets – are also important determinants of participation in society, because increasingly they affect the ability of people to access opportunity and to get ahead. Ensuring that there is general equality of opportunity is an important element of fostering social cohesion. For this reason, there is renewed policy interest across the world in ensuring that there is widespread ownership of financial assets.

For example, Australian Labor Party leader Mark Latham argues that a key policy objective "should be to give people a tangible stake in the success of the new economy" (2001) and ensure that all have an opportunity for economic participation because they have an ownership stake.

STAKEHOLDER IN SUCCESS

Broadly distributed asset ownership allows most citizens to benefit from progress, rather than having a situation where non-asset owners watch those with assets get ahead. As Ray Boshara notes "It doesn't take an army of economists to know that society as a whole reaps huge rewards when we have more owners, savers, taxpayers and entrepreneurs – and fewer people depending on the state, their communities and others for their livelihoods and well-being" (2003).

Communities in which most people have an ownership stake in the society and in the economy, tend to be more successful. This is because people who have a stake in the performance of the community and the economy are more likely to engage and to make a contribution because the outcomes will have an impact on them personally. As was noted above, home owners tend to take better care of their properties and are also more involved in local politics because these decisions will affect the value of their investment.

To take another example, where employees have an equity stake in their company, they have a more direct stake in the success of the organisation, and the evidence shows that better outcomes are likely. Academic studies systematically find that firms in which employees have an equity ownership stake generate higher rates of productivity and higher rates of job satisfaction.

Kruse (2002) surveys the findings from 31 studies on employee attitudes and behaviour under employee ownership and notes that "most studies find higher organisational commitment and identification under employee ownership, while studies are mixed between favourable and neutral findings on job satisfaction, motivation, and other behavioural measures". Kruse (2002) also notes that overall, the evidence clearly suggests a significantly positive effect of employee ownership on firm performance. The average estimate is the firm productivity rises by about 4-5% in the year in which employee ownership is introduced, and that this higher level of productivity is maintained. Further, Kruse (2002) notes the empirical consensus that employee ownership is associated with greater employment stability and higher rates of firm survival.

This argument has broader application. Societies in which most people have an ownership stake – and who therefore can expect to benefit from economic progress – are much more likely to favour investment in the future of the country. Just as the evidence suggests that asset owners have a longer-term view at a personal level, we can also expect that asset owners will also favour policies that have longer-term benefits at the national level (Alesina & Rodrik (1994), Persson & Tabellini (1994)).

An ownership society – in which asset ownership is broadly distributed within the population – is likely to lead to the benefits of higher rates of economic growth being more broadly shared. In turn, this is likely to increase the support base for policies and actions that will generate higher rates of economic growth.

Achieving broad support for economic growth is likely to be an important part of achieving better growth outcomes. One of the recurring themes in economic growth success stories over the past couple of decades is the existence of social consensus around economic growth. Successful countries like Ireland, Finland, Singapore and Australia have each had a sense of shared purpose about priorities and direction, although they each faced different challenges and responded in different ways. This doesn't mean there was universal agreement on every policy detail, but there was broad agreement on the strategic direction. This consensus enabled these countries to make the required changes and sustain economic policy over long periods of time, and is recognised to have played an

> *"The only problem with capitalism is that there are not enough capitalists."*
>
> RUSSELL LONG
> DEMOCRATIC SENATOR FROM LOUISIANA

important role in the economic success of these countries.

In a New Zealand context, a drive to improve economic performance is more likely to be sustained over the long term – and will probably work more effectively – if New Zealanders are committed to the goal and feel the policies are consistent with New Zealand culture and values. So the challenge is to create an environment in which pro-growth policies command widespread support by ensuring that economic policy is consistent with New Zealand's social environment.

Unfortunately, however, there is little evidence of broad public or political agreement in New Zealand on the relative importance of growth and the appropriate policy direction. For example, the recent Growth & Innovation Advisory Board (GIAB) survey of New Zealander's attitudes to growth suggested that New Zealanders have a generally positive attitude to growth, but that this support is 'lukewarm'. Indeed, about 40% of respondents were neutral or negative about the likelihood of getting tangible benefits from growth, like better pay or a better health system. There seems to be a general ambivalence about growth.

Given the importance of raising New Zealand's economic performance, a key challenge is to generate a sense of shared purpose around both the importance of economic growth and the broad direction of policy.

The GIAB survey results provide some guidance as to how to do this. The results seem to say that New Zealanders support growth in a conditional sense. That is, they will support the pursuit of growth if the policies are 'fair', in the sense that most people have a reasonable opportunity to share in the benefits of higher growth. Providing all New Zealanders with genuine opportunity to participate in economic success and to share the benefits is likely to be important in terms of creating broad-based support for economic growth.

Asset ownership provides a way in which people can benefit from growth, in addition to wage growth, because asset values will generally increase in a growing economy. Indeed, as was noted earlier, many of the benefits to growth accrue in the form of capital gains as income growth gets capitalised into asset values. For most New Zealanders the rise in property prices will have outstripped their wage growth over the past decade. This benefits those who own assets, but likely disadvantages those who do not.

Creating an ownership society in which many more New Zealanders own assets is likely to make a significant contribution towards the perception that growth policy is fair, as widespread asset ownership means more New Zealanders will benefit individually from growth. And if the gains from growth are widely shared, there is more likely to be broad support for future growth - ensuring that economic policy is much more likely to be sustainable and effective.

SUMMARY

The evidence described in this section shows that societies in which most people have an ownership stake can be expected to function and perform better. For one thing, people who own assets – be it a home, a small business, or financial assets – tend to feel that they can participate in society on a more equal basis, and this has a positive effect on social cohesion. People tend to engage in community and political activities, and tend to make more of an investment in the long-term future of the community.

One reason for these improved outcomes is that asset ownership generates a more direct link between the success of the community and good outcomes for the individual. As such, people are more likely to invest to a greater degree in the long-term prosperity of the community.

Conversely, a society in which many people have no ownership stake – or any likely means of generating an ownership stake – is not one in which people are able to participate. In such a situation, support for basic social and political institutions is likely to erode. This is likely to have a negative impact on economic and social outcomes.

This suggests that broadening the current distribution of household wealth in New Zealand, and increasing the number of New Zealanders who have a meaningful ownership position, ought to generate significant benefit to the community at large. This provides further motivation for considering possible deliberate policy action to improve New Zealand's household wealth outcomes.

4 THE NEED FOR ACTION

INTRODUCTION

The previous sections have described the profound impact of asset ownership on both individuals and the broader community. Asset ownership enhances the ability of people to participate meaningfully in society, by better allowing people to get ahead by accessing opportunity and managing risks. And a broad distribution of asset ownership enhances social cohesion and the functioning and performance of communities. Although some of the benefits to asset ownership have been understood for decades, if not centuries, the strength of the evidence base – and probably the importance of asset ownership itself – has increased over the past decade or so.

Governments in many countries have responded to the evidence of these benefits by introducing and expanding policies that assist and encourage people in terms of wealth accumulation, from various savings policies, to home ownership policies, to asset building initiatives in low income communities. This focus reflects a recognition that increasing the level and broadening the distribution of asset ownership is a key policy priority.

So what are the implications for New Zealand? As was described in detail in a previous paper, New Zealand is far from an ownership society (Skilling & Waldegrave (2004)). Many New Zealanders do not have any meaningful ownership stake in New Zealand, and many New Zealanders struggle to accumulate wealth over their lifetime. Further, there are many emerging pressures on wealth accumulation like student loan debt, declining home ownership rates, and the emergence of a debt culture.

The absence of an ownership stake for many New Zealanders can be expected to have negative effects on both the individuals and households concerned, but also on the broader community. And improving these wealth outcomes – and creating an ownership society in New Zealand – is likely to generate substantial upside for both individuals and the broader community.

However, at the moment New Zealand is unique among Anglo countries – and very unusual among developed countries – in having no policies that deliberately assist and encourage wealth accumulation. Whereas all other Anglo countries have savings policies (tax concessions, matched savings, compulsory savings) for a variety of purposes (retirement, education), and home ownership assistance policies, New Zealand stands out as having a hands-off approach to asset accumulation.

New Zealand's hands-off approach is based on the assumption that in general people will make rational savings and asset accumulation decisions that are appropriate to their circumstances and preferences. In this view, to the extent that many New Zealanders do not accumulate assets – for example, because they consume rather than save – this simply reflects their preferences and is not cause for deliberate government action.

However, it seems unlikely that the current hands-off approach will lead to significant improvements in either the level or the distribution of household wealth. Indeed New Zealand's savings and household wealth record over the past decade or so suggests the opposite. And the international policy mainstream also suggests that other governments believe more deliberate action is required. This section will examine the key arguments for government involvement in encouraging and assisting asset ownership, with a view to determining whether this ought to be a policy priority in New Zealand.

Broadly speaking, there are three key arguments for why a voluntary approach to asset accumulation is unlikely to be sufficient to achieve an ownership society. These are:

- Behavioural issues: many people do not make fully rational decisions with respect to savings and wealth accumulation
- Redistribution: some people lack the income to save and to accumulate assets in a way that will enable them to participate meaningfully in society
- Positive externalities: the positive side-effects associated with a broadly distributed ownership structure.

BEHAVIOURAL ISSUES

In traditional economic models of saving, people calculate the optimal path of savings and consumption and then act to accumulate assets in a way that will maximise their welfare. In reality, however, most people do not act like this. 'Behavioural economics', which integrates psychology into economic models, does a much better job in explaining real world behaviour. A key intuition in behavioural economics is that "economic rationality is systematically violated and that decision-making errors are both widespread and predictable" (Laibson & Zeckhauser (1998, p. 5)). Indeed, departures from full rationality are particularly likely with respect to saving and wealth accumulation.

For one thing, there are few chances for learning; the consequences of inappropriate savings decisions may not become apparent for many years, by which time it may be difficult to remedy any previous under-saving. And the informational demands associated with savings decisions are high; many people are not sure how much they ought to be saving for future needs.

Moreover, many people are not sufficiently far-sighted to save for future needs. Empirical estimates suggest that many people have short time horizons, of about 3 years or so, with discount rates frequently in excess of 30% (Loewenstein & Thaler (1992)). One of the implications of this is that income is consumed rather than saved for future consumption because the future is not heavily weighted.

But perhaps the most powerful determinant of savings behaviour relates to the costs of self control. Many people – indeed, probably most people – understand that it is in their long-term interest to save and to accumulate wealth, but they also have short-term preferences for consumption that may over-ride their long-term preferences. Laibson et al. (2001) provide a good example of this, finding that many US households simultaneously have interest-bearing credit card debt – at very high rates of interest – and are saving for retirement, earning much lower rates of interest. It is very hard to understand this behaviour using standard economic theory, but

> *"Deferred gratification isn't worth it for most people – you can spend $200 on a cell phone now and use it or save $200 for use later. But $200 is peanuts compared to what you need for a house or university – you need more like $20,000. So, you give up and spend it now."*
>
> MALE, 36, WELLINGTON

much easier once the costs of self control are incorporated.

Savings then can be seen as a process of exercising self-control. As Nobel Laureate George Akerlof (1991) notes, savings is a classic area in which procrastination is likely to occur – there are short-term costs, long-term benefits, and lots of future opportunities to start saving. And for many people, the procrastination is repeated – savings is something that will always happen 'next year'. Laibson (1997) demonstrates that models of saving behaviour that incorporate these features can explain real world behaviour well.

This explanation fits with the consistent results from surveys in many countries that show that people are aware of the importance of saving, but consider that they save too little (Laibson et al. (1998)). That is, people report that they have difficulties in taking the actions they would like to. And repeated New Zealand survey evidence documents that many people report that they are under-saving relative to their aspirations.

In this view, people who find it easier to exert self control will save more than those who do not. Thus, whereas standard economic models of saving assume "that individuals solve for the optimal consumption plan, and then execute it with will of steel" (Thaler (1992, p. 109)), in reality people find it hard to exercise self control and may not achieve the outcomes they want.

In response to the recognition that self-control is valuable but costly, households frequently "take steps to constrain their future behaviour" (Thaler (1992, p. 109)) so as to reduce the costs of self-control. For example, households can develop rules of thumb to guide savings behaviour, such as a rule that they will not consume out of future income, or they can commit to irreversible actions, like automatic contributions into an illiquid investment vehicle with early withdrawal penalties. This is why financial advisors routinely advise people to cut up credit cards. By deliberately constraining liquidity, households aim to increase their saving rate and improve their welfare.

Habit formation is also important – forming a savings habit is another way of reducing the costs of self control. This is why changing habits and behaviours is an explicit focus of many savings schemes. Indeed, the evidence shows that once people start savings, they are likely to continue to save (Thaler (1994), Kempson et al. (2003)).

Where the costs of exercising self control to save are reduced, we expect to see increased savings. For example, introducing illiquid investment vehicles, or imposing penalties for early withdrawal, reduces the costs of self-control with respect to saving and can be expected to increase saving. By assisting people to follow their long-term preferences, these institutions are likely to enhance individual welfare. As George Akerlof notes, "individuals may be made better off if their options are limited and their choices constrained" (1991, p. 2).

One way of reducing the costs of self control is to remove the choice by making saving compulsory. And the evidence shows clearly that compulsory savings schemes do substantially increase saving, even though models of fully rational behaviour predict a considerable offset. Recent Australian evidence suggests that about two thirds of the compulsory savings in the Australian superannuation scheme represents new savings (Connolly & Kohler (2004)). This is consistent with estimates from the US and the UK (Bernheim (1999), Feldstein & Liebman (2001)). Indeed some studies have found that compulsory savings 'crowds in' new savings, where people begin to save additional amounts because they have formed a savings habit.

However, compulsion is not the only way to reduce the costs of self control. The evidence on savings behaviour in voluntary work-based retirement savings schemes in the US (mainly 401(k) plans) demonstrates the importance of institutions that reduce the costs of self control. The evidence demonstrates persuasively that people respond to specific institutional characteristics of these programs when making savings decisions.

Choi et al. (2001a,b) and Madrian & Shea (2000) show that the institutional context is very important in determining participation and the contribution rate. Employees seem to be passive decision-makers and take the 'path of least resistance' in making savings decisions. For example, participation rates are substantially higher when people are automatically enrolled in the scheme and need to deliberately opt out if they do not want to participate. Madrian & Shea (2000) document close to a 50% increase in participation among new employees after automatic enrolment was introduced compared to a situation where employees needed to make a decision to join the scheme. The increase in participation is particularly high for young and low-income employees.[3] Interestingly, only a small proportion of employees who are automatically enrolled choose to exit the scheme subsequently.

Another way of increasing participation rates is to specify that employees need to make a decision with respect to their participation by a particular date. This process has also been shown to increase participation rates significantly (Choi et al. (2003)).

The scheme default options are also very important in terms of affecting decision-making; for example, automatic enrolment, the type of investment vehicle and so on. Employees tend to stick with the default contribution rate and the default investment fund. Few employees increase their contribution rates, even when they report that they would like to do so, unless they are given a low-cost way of doing so. This

[3] *When employees are required to deliberately sign up to participate, many do not do so despite the tax advantages and the frequent matching contribution from employers. In a rational model, we would expect the participation rate to be close to 100%, and the puzzle is why so many employees do not sign up unless strongly prompted.*

is an example of the status quo bias (Samuelson & Zeckhauser (1988)).

In a New Zealand context, there is evidence that participation rates in employer based superannuation schemes are considerably higher than in the population at large (Scobie & Le (2004)). This is likely to be at least partly due to the relative ease of participating, which reduces the cost of self control associated with savings.

However, the deregulation of credit markets, and the ease with which credit can now be accessed, has significantly reduced liquidity constraints and has made the exercise of self-control more difficult. Because the enhanced access to credit reduces the commitment value of illiquid assets, and makes self control more costly, household savings rates can be expected to fall. Indeed, the expansion of access to easy credit coincides with a significant decline in savings rates in Anglo countries. And in general, households in countries with more deregulated capital markets save less than those in countries with a more regulated environment, where it is more difficult to accumulate debt. For example, household savings rates in Continental European countries are frequently in excess of 15% of disposable income, compared with household savings rates of below 5% for most Anglo countries.

Similarly, the decline in New Zealand's savings rates correlates well with the deregulation of New Zealand's credit markets, which made it easier for households to access mortgage finance and personal credit. Household borrowing has risen sharply over this period, as it has in other Anglo countries. However, New Zealand's savings rates and financial wealth are considerably worse than in other Anglo countries. This is attributable in significant measure to the absence of policies and institutions that assist and encourage savings (there is an extended discussion of these trends in Skilling & Waldegrave (2004)).

Indeed, New Zealand policy has made it easier to accumulate debt over the past 15 years or so (e.g. consumer credit, student loans) but has not done anything deliberate to help people accumulate assets. This is an unbalanced approach, and the outcomes are as expected – low and declining financial wealth, with sharply increasing household borrowing and low and declining household savings. This contrasts with the situation in other Anglo countries, where there are policies to assist and encourage asset accumulation and where household financial asset holdings have risen by more than the increase in household debt over the past decade.

The policy implication is that deliberate action to encourage and assist savings and asset accumulation is an important thing to do in New Zealand. Providing a policy and institutional framework that reduces the cost of self control is necessary to ensure that New Zealanders can get ahead financially. At its core, this is a very simple proposition; where the savings decision is made easier for people, people respond by saving more. The international and New Zealand evidence is clear that policies that make saving and asset accumulation easier lead to significantly improved household saving and wealth outcomes.

And the evidence suggests that relying on financial education and income growth is unlikely to be sufficient to achieve these improved outcomes.

The evidence is clear that financial education within the workplace and in secondary schools leads to higher levels of saving (Bayer, Bernheim, & Scholz (1996), Bernheim & Garrett (1996), Bernheim, Garrett & Maki (1997)). However, although important, financial education is unlikely to be sufficient to overcome the self-control problem. People need something more immediate, tangible, and enduring in order to make appropriate savings decisions. Choi et al. (2001a) report that less than one third of those surveyed report that they changed their actions in line with their intentions after financial education. Financial education that is linked to some specific savings program is more likely to be successful.

Taken together, this evidence suggests that many people want to save but that they face real self-control problems in terms of making this choice. If the savings decision is made automatic or easier,

the costs of exerting willpower diminish, and increased saving becomes more likely. This is why savings policies and institutions have a good track record of success internationally.

Income growth can also make an important contribution to household wealth accumulation. Obviously, as household income increases, there is more money that can be saved. But income growth cannot be relied on in isolation to increase household saving. Indeed, New Zealand has generated strong economic growth over the past decade but savings have been low and declining. Instead, people have chosen to increase consumption spending – indeed, private consumption growth has consistently been much stronger than income growth. For example, retail spending has grown by an average of about 6-7% p.a. since 2000, considerably in excess of economic growth rates. And the experience of the personal tax rate cuts in New Zealand in the 1990s was that they were consumed rather than saved, suggesting again that the answer is not simply increasing household's disposable income.

Rather, income growth needs to be coupled with policies and institutions that make it easier to convert this income growth into wealth. Otherwise, the New Zealand and international evidence suggests that it will be consumed and will not generate long term benefits for individuals and for communities. Deliberate action to convert income growth into wealth accumulation is required, from the government and also from employers and community groups.

REDISTRIBUTION

However, for some New Zealanders, the primary barrier to wealth accumulation is not self control as much as a lack of sufficient income to enable saving. The New Zealand evidence shows that wealth accumulation in New Zealand is strongly linked to income and in particular that New Zealanders who earn below the median income do not hold significant amounts of wealth. So the incomes generated by many New Zealanders do seem to make it difficult for them to save substantially.

This concern should not be over-stated. The international evidence suggests that providing easy and efficient ways of saving does stimulate savings behaviour even among those on low incomes. And the rapid growth in New Zealand's consumption spending noted above, suggests that there is disposable income available that could be saved rather than consumed.

However, a policy approach to wealth accumulation that relies entirely on individual decision-making is likely to mean that many low income people will not be able to accumulate significant amounts of assets because they are on insufficient income (even if they are disciplined savers).

The challenge in creating an ownership society is to ensure that many more New Zealanders – and particularly low income New Zealanders – are able to accumulate assets. The benefits to asset ownership discussed above apply to all the population, and perhaps generate particular benefits for those who currently have no ownership stake at all.

Asset ownership is an important part of economic advancement. As Sherraden (2003) observes, "for the vast majority of households, the pathway out of poverty is not through income and consumption but through saving and investing in education, enterprise, and property" (p. 28). In addition to increasing labour force participation, access to financial asset ownership and education are critical to economic success.

As discussed above, asset ownership generates powerful economic and social benefits for individuals and households as well as for communities. Indeed, ensuring that people have at least some asset ownership stake is an increasingly important way in which to achieve the key policy objective articulated in the 1972 Royal Commission on Social Security – to ensure that "everyone is able to enjoy a standard of living much like the rest of the community, and thus able to feel a sense of participation in and belonging to the community".

Achieving these outcomes necessarily requires some deliberate action as those on modest incomes are less well placed to achieve them by themselves. Indeed, the evidence on the importance of asset ownership, and particularly for those on low incomes, has motivated a series of policy initiatives and proposals in several Anglo countries to extend savings and asset accumulation policies to those on low and middle incomes. Traditionally, many savings policies have advantaged middle and high income earners disproportionately because the tax concessions on savings went to those who had the most to save. In response to this, there have been numerous proposals initiatives aimed at promoting asset building programs for low income households (OECD (2003a), Regan & Paxton (2001), Allen Consulting Group (2003)).

The matched savings programs like the Savings Gateway in the UK and the American Dream Demonstration in the US are examples of this approach. The evidence from these, and other, programs has been very positive; people on low incomes want to save and are able to do so in come measure, particularly when assisted by matched savings and other forms of support (access to banking, financial education and so on).

The benefits of asset ownership to individuals and communities are sufficient to make this a policy priority. Both public and private organisations ought to be looking at ways to assist and encourage low and middle income New Zealanders to build an ownership stake; for example, assisting people to save for a first home, to finance education, and so on.

Historically, policy in New Zealand has been designed to assist people to move ahead through free public education and training, full employment policies, assisted home ownership programs, and the provision of social insurance in the form of income transfers. And New Zealand welfare policy continues to focus on income transfers and the provision of a social safety net, with wealth accumulation being seen as a private activity. In this sense, the current welfare system in New Zealand is fundamentally similar to the welfare system three decades ago. There have been few attempts to encourage asset ownership through the welfare system.

However, although income transfers help in terms of alleviating poverty, such an approach is of less use in getting ahead. Boshara (2003) draws a distinction between getting by with the assistance of income transfers and getting ahead through asset ownership. So whereas the traditional focus in the delivery of welfare policy has been income transfers and public provision, there is increased interest in asset building programs as a powerful way to assist people to get ahead (Sherraden (2003)).

Similarly in New Zealand, governments should view asset accumulation as an important part of achieving distributive outcomes, and helping people get ahead, in addition to the historical reliance on income transfers.

POSITIVE EXTERNALITIES

Asset ownership generates benefits to both individuals and to communities. A society in which most people have a meaningful asset ownership stake is likely to function better and deliver superior community outcomes. The benefits that are generated by the existence of an ownership society flow to everyone in society irrespective of whether they are an asset owner or not. For example, the evidence suggests that people are better off living in a street with high rates of home ownership, because of higher rates of neighbourhood participation, better home maintenance and so on, irrespective of whether they themselves rent or own. Similarly, to the extent that broadly distributed asset ownership creates a larger support base for growth, this benefits everyone.

This means that there are benefits external to those captured by the individual asset owner. In the jargon, these are called 'externalities'. Individual decisions with respect to asset ownership may not fully reflect these broader benefits, and so people may not prioritise asset ownership in a way that generates optimal social outcomes.

However, the government has an interest in obtaining the community-wide benefits of an ownership society – cohesive, functioning communities – and in addressing the negative outcomes associated with communities in which many people do not have an ownership stake. And governments often step in to ensure that these broader outcomes are achieved. Indeed, this motivation is commonly invoked by governments around the world. For example, the goal of creating a 'property owning democracy' has been an explicit aim of governments from the US and the UK, to Australia and post-war New Zealand. Governments believed that the community-wide externalities generated by such outcomes warranted policy action. And as noted above, these policies have frequently been successful.

Given New Zealand's current household wealth outcomes, and in particular the number of New Zealanders without an ownership stake, and the strength of the empirical evidence on the benefits from having an ownership society, encouraging and assisting more widespread asset ownership ought to be an urgent policy priority.

CONCLUSION

Creating an ownership society in New Zealand will require deliberate action on the part of government and the private sector to assist and encourage wealth accumulation. The existing approach to savings and wealth accumulation, which relies on individual decision-making with no government involvement, will very likely be inadequate to achieve significantly improved ownership outcomes. Indeed, this lesson is apparent from the past decade of New Zealand's experience.

The current hands-off approach does not adequately recognise the insights of behavioural economics, does not recognise the importance of asset building in achieving redistributive objectives, and does not consider the positive externalities that are generated by broadly distributed asset ownership.

Rather, the approach observed in other Anglo countries – and most other OECD countries – where governments deliberately and actively encourage wealth accumulation is needed in New Zealand. These policies and institutions enable people to convert income into wealth, and generate better outcomes for individuals and for communities.

5 CONCLUDING REMARKS

This paper has described why increasing the number of New Zealanders who have an ownership stake is vitally important for securing a better future for New Zealanders and for New Zealand as a nation. There are two key messages in this paper.

First, asset ownership is increasingly important to people in terms of their economic and social well-being, and also to the functioning of the communities in which they live

The creation of an ownership society in New Zealand is likely to generate significant economic and social benefits to individuals, communities, and the country as a whole.

For individuals, asset ownership provides direct financial benefits in terms of the returns generated. As a result, those who own assets are in a position to get ahead financially in much greater measure than those who do not own assets. Further, the benefits from economic growth are often capitalised into asset values, so that asset owners benefit disproportionately from growth. Those who own assets – like a home – get ahead while those without assets get priced out of the market.

And it is often the case that accessing these return opportunities requires some initial asset ownership. For example, a deposit is required to buy a home, and initial equity capital is generally required to start a new business. Because of this, wealth inequality is frequently self-perpetuating.

Assets also provide a buffer, which allows people to better manage risks. This insurance function provided by assets is increasingly important, as the extent of social insurance reduces and as the risks that people face become more diverse.

The ability to access opportunity and get ahead, and to better manage risks, also generates powerful social and psychological benefits. Asset ownership gives people a sense of control and independence, enables people to focus on the future to a much greater extent, and is an increasingly important determinant of meaningful participation in society. Asset ownership has been strongly linked to better health and employment outcomes, quality of life, marital stability, and educational outcomes for children. Encouraging asset ownership seems an important way in which to build a genuinely inclusive economy.

Widespread asset ownership also has significant community-wide benefits in terms of generating social cohesion and a feeling that everyone has an opportunity to get ahead and build a future. To the extent that people own a house, a business, or financial assets, they are better able to participate meaningfully in society and will share in the benefits of economic progress as their asset appreciate in value. Indeed, the evidence shows that people who own assets tend to be more involved in their communities. Conversely, communities in which many people do have an ownership stake – and where people feel marginalised – tend to generate worse outcomes.

Second, moving towards an ownership society will require deliberate action

Creating an ownership society provides a promising way of creating a community in which many more people have the ability to meaningfully participate. But currently many New Zealanders do not own significant assets and many – if not most – New Zealanders are finding it difficult to get ahead financially. Given the increasing importance of assets, and the very poor nature of the current outcomes in New Zealand, creating a broadly based ownership society is a first order priority that needs to be pursued with considerable urgency.

Creating an ownership society will require concerted, deliberate action by both the government and business and community organisations.

The current hands-off approach to wealth accumulation in New Zealand is inadequate to significantly increase the level and broaden the distribution of household wealth. Indeed, over the past decade the current approach has contributed to low and declining household financial wealth, and the difficulties that many New Zealanders are facing in terms of building an ownership stake. By themselves, economic growth and financial education are unlikely to be sufficient to enable many more New Zealanders to get ahead financially.

Deliberate action is required because of the self-control issues associated with savings that make it difficult for many New Zealanders to save, in order to ensure that all New Zealanders are able to accumulate assets, and because of the powerful externalities that are associated with asset ownership.

Indeed, governments across the world understand the importance of this and have been establishing and expanding policies that encourage and assist wealth accumulation. This focus on asset based policy and creating an ownership society is bipartisan in nature, with champions being found in both left and right wing political parties and governments. And the evidence consistently shows that these policies work in terms of increased and more broadly distributed savings and asset accumulation.

The challenge in New Zealand is to move deliberately towards meaningfully improving household wealth outcomes, by encouraging and assisting New Zealanders to get ahead. The aim is expand the population of asset owners and ensure that many more New Zealanders have a genuine stake in the future. Improving these outcomes will involve deliberate action by the government, as well as by business and community groups.

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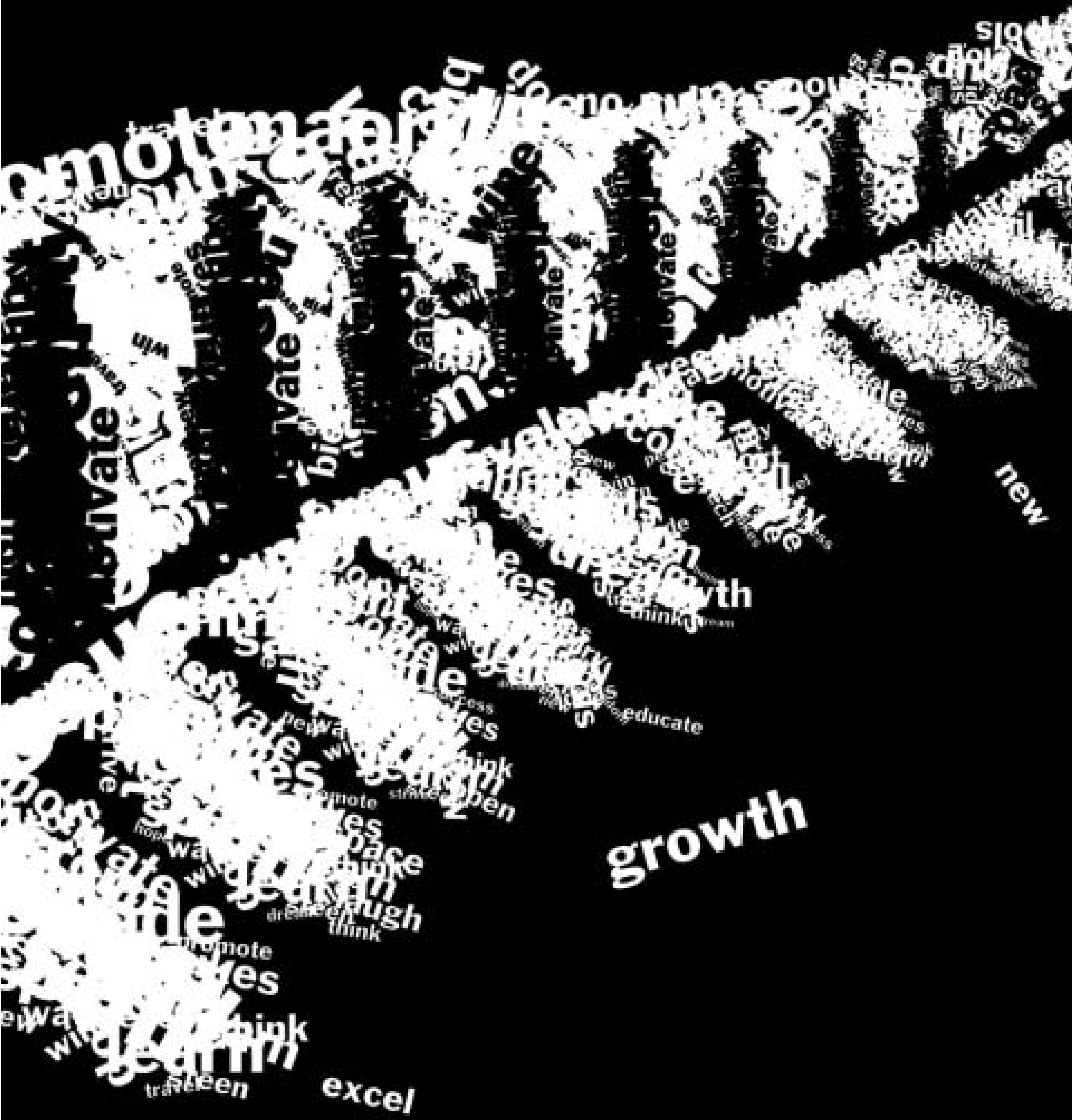

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