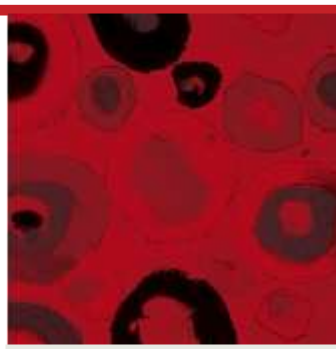
Choose kids: Why investing in children benefits all New Zealanders



Children are our future. Demographic changes impacting our labour force, the skills needed for economic growth, and the costs of poor childhood development, all present urgent reasons to invest better in children.

New Zealand needs every single child to thrive in order to support a future of high productivity, innovation, economic growth and improved social cohesion. Currently we have a significant proportion of children who are not getting what they need to thrive. This paper outlines why we will all benefit if we invest better in children so they can succeed.

WHY IS INVESTING IN CHILDREN IMPORTANT FOR US ALL?

New Zealand has some key challenges on the horizon. An ageing population, the increasing costs of pensions and healthcare, and our desire for a high standard of living, mean that we need the economy to be more productive than ever.

These drivers are placing greater pressures on this generation to ensure each and every child can grow up with fully developed skills and become productive citizens. At the same time, the rate of childhood poverty is twice what it was a generation ago putting at risk our potential skills development, future productivity and social cohesion.

To grow our economy the government is focused on increasing exports and high value industries. These are dependent on entrepreneurial people, skilled labour and investment in creating more diverse, high value service and production jobs. Key to this is the development of a skilled labour force.

This paper describes what children need to become skilled and productive adults and how poverty in childhood can constrain skills development.

One in four of New Zealand children live in low-income households, and 17% of children regularly go without the basic things they need.[1]

Growing up in poverty poses barriers to future success such as: poor health, lower educational attainment, lower-paid employment, and higher rates of unemployment, criminal offending, mental health problems, welfare dependency and teenage pregnancy. While some children are resilient to these effects, for many, poor outcomes impose significant personal costs and costs on society.

We already spend $6-8 billion a year addressing the consequences of child poverty. We can continue paying for ‘ambulances at the bottom of the cliff’, or we can consider how a more strategic approach to investing in children will lead to the skilled labour force required to drive productivity and economic growth.

This paper reviews the case for strategic investment in young and disadvantaged children. It also presents the link between improved child development outcomes and how to:

- address skilled labour shortages in the face of aging population trends
- improve productivity and economic growth, and
- reduce expenditure on the ‘costs’ of child poverty.

The evidence is clear: we will suffer a serious brake on the economy unless all our children achieve the skills required to contribute to our future productivity.

INVEST IN THE RIGHT PLACE AT THE RIGHT TIME FOR HIGHER RETURNS

We already invest a substantial amount into health, education and social services for children. How can we ensure we can achieve the best return on our investment?

We want every child to grow up able to contribute positively to our economy and society. To achieve this, society invests billions annually so that children and young people:

- achieve a basic education, and go on to get a qualification
- have the skills for employment
- have good health and mental health, and
- are socially connected.

But a significant proportion of young people are not achieving these things, for example 15% of young people leave school without any qualification. As a result New Zealand is not getting the best results from its current core investments in children.

Growing up in poverty is an underpinning factor for the poor outcomes of disadvantaged young people - such as poor health, social skills and qualifications, and greater likelihood to require state support for extended periods as adults. If we want to reverse these results, we need to acknowledge the current approach is not working for many children and young people. The reasons start in early childhood development.

More investment in younger, disadvantaged children will make the most difference for future skills and productivity

While the government invests significant sums in early childhood education (ECE), primary, secondary and tertiary education, the OECD concludes that New Zealand should spend considerably more on younger, disadvantaged children[2].

For all children, and particularly those who are disadvantaged, there are greater benefits when investments are made *earlier* in a child's life, when key cognitive and physical developmental processes are occurring. If *all* children were to have equal opportunities for early development then we would achieve greater benefits from subsequent core investments in education and health.

What is needed is strategic investment that aims to reduce the number of children growing up in poverty, rather than reactive spending to mitigate the effects of poverty.

In the book *Child Poverty in New Zealand*[3], Boston and Chapple report that the cost of raising household incomes to eliminate those under poverty lines is between $800 million and $1.8 billion, (about 0.5 to 1 percent of GDP). This compares with the costs of poverty (described more fully later in this paper) that add up to about 4 percent of GDP[4]. The long-term benefits justify spending $2 billion per annum on eliminating child poverty for at least the next ten years. It has been calculated that this would achieve $50 billion of savings[i] over that generation's life expectancy[4].

Investments that reduce poverty will remove a barrier to skills development and change the outcomes we currently see. Instead of having one in five young people leaving school with no or low qualifications (and having a high likelihood of requiring additional social supports during and after the schooling years), a high proportion of these young people will be well placed to contribute positively to the economy and society.

This will reposition New Zealand to meet the challenges of an aging population and decreasing supply of skilled workers and will contribute to productivity growth. This win-win investment approach will also generate savings, as less spending will be needed to mitigate the costs of a poor start to life.

Why is early child development susceptible to disadvantage and poverty?

Child development is at its greatest acceleration in the first few years of life, and sets up a child on his or her life course.

Development of brain connections ('hard-wiring' of the brain) begins during fetal development. Connections are rapidly forming during the first three years of life. It is in this period that infants and toddlers bond with care-givers (usually parents), and develop pro-social behaviour, cognitive skills and emotional intelligence.

[i] Savings at present value of investment (2010 dollars at time of analysis).

Children who go on to have better average educational achievements and lifelong earnings are those who are best prepared for school. They have typically received the right inputs from an early age, including prenatally.

Investment (of time and money) in children is usually provided by parents with the support of their communities. It includes good nutrition during pregnancy and childhood, helping the child develop from infancy (through warm parenting and talking etc), developing social skills (through role modelling, reinforcing good behaviour, having consistent boundaries, and providing chances to play with other toddlers, etc), and supporting cognitive development through reading and games that foster thinking skills.

Some parents don't have the resources to provide a healthy, stimulating environment while others lack knowledge of critical child development needs. What parents know about children's development is positively correlated with them providing the environment and opportunities conducive to stimulating their child's development.[5]

Time-poor parents often have constraints on what they can do to support their children's development. Low hourly wage rates often mean people work extra hours so they can earn enough to live on. This reduces the time a parent can invest in his or her children.

Low incomes can create stressful family situations. Constantly stressful home environments alter the chemical balance and brain development of babies. This makes them less able to learn, less sociable, and more likely to grow up aggressive. Childhood poverty is also associated with delayed language development, so children are less ready for school and likely to suffer long-term learning and literacy difficulties.

Children who 'miss out' in early stages can often 'catch up', but this becomes progressively more difficult with age.

Children who suffer from any kind of delayed development need to have their issues addressed at an early age, through remedial efforts, if the subsequent core educational and health investments are to reap dividends. Waiting for a diagnosis at school age may be too late or costly.

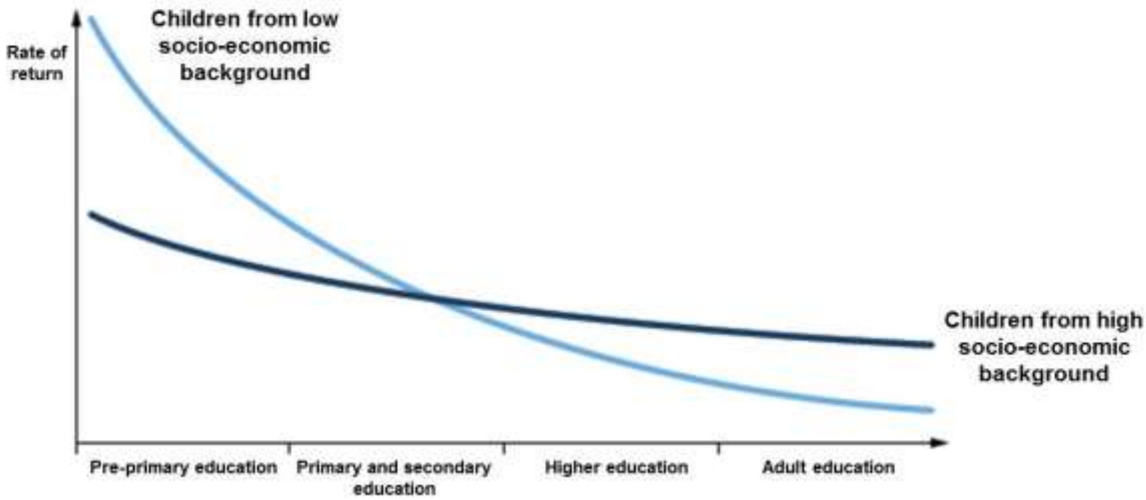
Investments yield greater benefits when they are made for younger children

It is critical to give children the best start possible in the first three years of life, when their development is at greatest risk from disadvantage. Many adverse outcomes for disadvantaged children and young people continue to have detrimental effects on their lives well into adulthood.[7]

While children who 'miss out' in early stages can often 'catch up' given appropriate interventions, this becomes progressively more difficult and expensive to achieve with age. Nobel prize-winning economist, James Heckman, has demonstrated the importance of investing early in a child's life, from birth, to get the greatest economic returns.[8]

Figure 1 shows that investment in the early years of education yields the greatest returns.

Figure 1 Return on educational investments for different socio-economic backgrounds



Source: Report for the European Community 'European Expert Network on Economics of Education', p12; derived from Cunha et al (2006) and Wobmann and Schutz (2006). [Reported in EAG paper.[6]]

In addition, those returns are wholly greater for children from low socioeconomic backgrounds.

For example, ECE provided to poorer children so they are ready for school by age five, will maximise further returns from subsequent educational investments in these children and young people.[9]

It is possible to model the elimination of early childhood disadvantage due to poverty, while accounting for other variables such as heritable effects, unemployment rates, and income).[4] This model shows that we could expect to see an improvement in productivity of 1.2 percent of GDP, if all those children currently attending decile 1-3 schools achieved the same average educational success as those in the school deciles 4-10. That's about $2.2 billion of increased earnings in 2010 dollars, which represents an 'opportunity cost' of the status quo.

So how can we reduce childhood disadvantage?

Evidence shows that gaps in success rates between those born to poor families and non-poor families is greater than 20 percent across all life stages from early childhood to adulthood.[9] By modelling the effects of poverty between those who receive ECE and those who don't, we can demonstrate that those who receive ECE close the gap in achievement (down to a 3 percent poverty effect) when starting school.

However, of itself, ECE is insufficient to close the gap for life. Continued investments at primary school age and adolescence will reduce the gap in adulthood (from 21 percent to 11 percent).

While there is a cost to closing educational gaps, the cost-benefit analysis shows lifelong gains that warrant such investment, with a return in the order of seven dollars for every one invested.[9]

Closing the gaps between achievements of children from different socioeconomic groups is particularly important to ensure all children develop protective factors such as basic literacy skills and positive peer relationships. While this requires concentrated investment in the early years (birth to age five), continued benefits can also accrue from further investments from ages five to ten.[9]

We can reduce disadvantage and support learning through early life interventions

It is not inevitable that poor children will fail to thrive. Preventative measures can alter the effects on the life-course of children.

Investments in early childhood development programmes and parental supports mitigate some of the effects of poverty. For example support for good parenting can ensure the neurological foundations are laid for a child's future learning, alongside developing social skills and resilience. These open the doors to full participation in school life, skills development and the future work force.

Some of the interventions required to mitigate early developmental risks include:

- universal parenting skills education, to ensure all parents are responsive to, and engaging with, their babies and children in a way that supports the child's mental, social and physical development
- high quality, affordable child care and education support
- physical and mental health checks and treatment
- good quality (dry, warm, not crowded) housing, and
- social services and community supports for families.

If we fail to invest in these areas, we will not only reduce the potential returns from core government investments in children, but we will incur additional, remedial costs.

Importantly, we will continue to suffer the economic opportunity cost of disadvantaged young people who are poorly prepared to engage in productive, high skilled jobs of the future.

EFFECTIVE EARLY CHILDHOOD INVESTMENT WILL SET US UP TO MEET LABOUR MARKET CHALLENGES

Our demographics will put pressure on the labour market

Reducing disadvantages for children will help people of all ages. Demographic changes are occurring that will put pressure on the labour market, creating a strong driver to ensure every child will develop fully, with optimal skills, to contribute to our future economy and society. New Zealand cannot afford any children to be beset by the impacts of poverty.

The most important demographic change in New Zealand is our ageing population, which is due to the trends of more people having fewer or no children, and having them later in life. This lower birth rate has occurred alongside decreasing manual labour, advanced nutrition, and health care[10] that are helping people to live longer.

It is important to recognise that economic growth in the period 1960s to 1980s was fuelled in part by the increasing labour supply of the baby-boomers. There were at least two or three people entering the workforce for every person retiring. We are now approaching the end of excess labour supply. Labour shortages are expected to get worse and to put a brake on economic growth, starting in provincial areas.

The ratio of labour market entrants (aged 20-29) to exits (aged 60-69) will approach one-to-one nationally by about 2025. Of New Zealand's 67 Territorial Authorities, 32 have reached this ratio already[10]. 22 percent of these regions have already stopped growing or are 'in decline' meaning their populations are getting smaller. This is a mainly a result of internal migration (urbanisation) of young working age people to the main cities, such as Auckland, Wellington and Christchurch.

Population decline can create a negative circle. As the number of children in an area declines, investment in infrastructure that supports children and families (e.g. schools) becomes less justified, and authorities may respond by investing less in that infrastructure. This feeds the negative circle by making the area less attractive to families bringing up children, with fewer young families in an area exacerbating the local shortage of labour.

Alongside these demographic changes, there are some mitigating factors currently buffering the impact on our labour supply. Healthier people aged over 65 are staying in the workforce for longer, and New Zealand still manages to compete internationally for skilled labour as our country remains an attractive place to live.

> We are now approaching the end of excess labour supply. We need every child to develop fully so they can *all* contribute to our society and future economy.

Children are important as they will provide sustainability for our communities in an ageing society

Our ageing demographic profile will put pressure on New Zealanders in the future, to provide for older people through pensions and healthcare, as well as personal care and support. This is a driver both for economic growth and a supportive younger population to share the obligations of caring for their elders.

Given the ratio of working people to dependents (children and pensioners) will continue to reduce in the coming decades, taxes and productivity will need to increase substantially to offset the added costs (even just to maintain current standards of living).

Family support for older people is being limited by small family sizes and offspring emigrating to join the diaspora of New Zealanders living overseas. This means more older people will be increasingly dependent on the state for social assistance that used to be provided by grown-up offspring and grandchildren.

Todays' children will have added demands on them, to support their elders and provide skilled labour toward national productivity. We need every child to develop fully so they can all contribute to our society and future economy.

SKILLED LABOUR IS A KEY TO PRODUCTIVITY

New Zealand suffers from skills mismatch

New Zealand needs substantial economic growth to address the growing demographic challenges while maintaining our standard of living. To achieve this, our current economic policy is for New Zealand to increase exports and the number of high value jobs.

Innovation is widely seen as the way to increase productivity in New Zealand, particularly when labour participation rates appear saturated.[ii] Innovation requires particular skill sets that need to be developed in New Zealand's human capital. These skills also need to be at the right qualification level to support the labour market.

The government has an indisputable role to play in educating children and facilitating training for youth so that they are well prepared for work. However, despite our internationally well-regarded education system, there is currently a skills mismatch constraining our productivity.

Employers report experiencing skilled labour shortages.[iii] Current skills gaps exist in high-technology manufacturing and design, information and computing technologies, health services (mainly specialists), some primary sectors (such as agriculture and forestry), and construction (recently exacerbated by the Canterbury rebuild).[iv]

These are sectors for which our own young people could and should be up-skilled to meet the needs of the labour market.

Structural shifts in the economy have reduced the availability of low-skill jobs

Poorer educational achievement resulting in low skills usually limits people to low-wage jobs. However, in recent decades, there has been a structural shift, particularly in the manufacturing sector, such that low-wage and low-skilled work is automated and/or being done overseas. There is less capacity for the economy to absorb low skilled workers, creating a risk of a growing number of long-term unemployed.[11]

Groups of young people who suffer the worst rates of poverty and disadvantage are also over-represented in unemployment statistics, mainly due to poor educational outcomes, e.g. Māori and Pacific island groups, and children from sole parent households.

Importantly, these disadvantaged groups also have younger age profiles. They represent a key opportunity to mitigate future labour shortages, if we could better support their skills development.

Businesses may not be able to rely on immigration to fill labour needs in the future

The limited supply of skilled labour does not bode well for businesses and the economy of New Zealand.

While many businesses currently rely on immigration to replace skills shortages, this may create long-term problems:

- The international labour market will become increasingly competitive – it may be hard to attract talent to New Zealand.
- Labour market shortages will result in higher wage costs for employers and inflation of the overall cost of living.
- When there is high youth unemployment, importing labour may exacerbate the negative impacts of poverty on those youth. They will have fewer opportunities for training and skills development, and may experience greater income inequality.

In the long term, businesses will find the international skilled labour pool is more mobile and there may be risks that skilled labourers 'return home' to care for their elders. A New Zealand pool of labour may be more likely to be 'sticky' to the New Zealand market due to familial connections. Training local youth would reduce this risk, and would therefore make good long-term business sense.

Mitigating the skills mismatch

Investments in education, vocational training and active social assistance are required to address low skills and support people into new, or more productive, jobs. Yet, as

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[ii] In 2012, the New Zealand labour force participation rate of 15 to 64 year olds was fourth in the OECD, at 82 percent (range: Turkey 55 percent - Iceland 89 percent).

[iii] Deloitte's 2013 Talent Edge New Zealand survey found that 83 percent of responding organisations were experiencing talent shortages that affected business results.

[iv] Lists of skills shortages are maintained by the Ministry of Business Innovation and Employment

illustrated earlier in Figure 1, we know this is not the most effective or efficient way to invest in human capital development.

The evidence is clear that disadvantage in early childhood has longstanding effects on a person's life course and, with one in four children growing up in poverty in New Zealand, we are losing significant opportunities for skills development.

Ultimately, this will put a brake on future economic growth. It will also burden tax payers with additional costs to mitigate the consequences of poverty.

REDUCING THE COSTS OF POVERTY

It's 'poverty' that matters

As well as the opportunity costs of childhood poverty described above, there are immediate costs that are being incurred to mitigate the well-described effects of poverty[1].

Poverty poses a barrier to future educational and economic success. It increases mental and physical illness, unemployment, social exclusion, and is correlated with committing and being a victim of crime. While some children are resilient to these effects, on average these outcomes add up to significant costs imposed on society.

A longitudinal development study[12] in New Zealand determined the family effects of poverty on educational achievement and income in adulthood. Income had a significant effect, *independently* of the child's academic ability and the family context.

In the absence of prevention policies to significantly reduce childhood poverty, its negative effects, especially on children's health and development, incur additional costs, including mitigation costs.

4 percent of GDP is spent directly on mitigating and addressing the consequences of child poverty

Current estimates are that mitigating the impact of poverty costs this country about $6 to 8 billion annually (4 percent of GDP). This amount represents the potential savings to be made were poverty to be eliminated.[4] This figure includes the costs of health and education interventions that are delivered to mitigate the effects of poverty, lost productivity due to lower skills, and the costs of crime. In addition, welfare costs were calculated for New Zealand in 2011 at $1.7 billion or 0.9 percent of GDP.[4]

If we turn around our approach and make more strategic, preventative, investments in young and disadvantaged children, in key areas at the right time, we could make great gains in reducing our remedial spending on the longer term costs of poverty.

Where we spend on education

New Zealand tries to achieve a highly skilled labour supply by investing $7 billion each year in early childhood education and compulsory schooling services. This core investment aims to ensure children grow up with the socialisation and skills required to contribute broadly to society's needs. New Zealand also spends $3 billion per annum on tertiary education[v] to promote the advanced learning required for high value jobs. The government also incentivises career choices through greater subsidies for courses or transfer incentives to help to fill skill gaps[vi].

There are a number of other investments that aim to close the gaps that result from poor achievement in school. The Ministry of Social Development invests $33 million per annum to help people re-engage in education, training or work-based learning, particularly aimed at youth.

Reducing child poverty would not only lead to higher rates of return from our existing investment, it would reduce demands for investment in second chance learning.

Added healthcare costs

Childhood poverty has negative effects on health that cost healthcare systems an additional 1 percent of GDP (in both NZ and international studies).[4, 13] The Child Poverty Monitor[1] reported on these negative effects. Children from the most deprived areas are

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[v] This excludes about $0.6 to 0.8 billion on writing off student loans, but includes $280 million for research related to tertiary education.

[vi] For example: the '3K to Christchurch' subsidy for beneficiaries to support the city's rebuild; increased investment in tertiary training for science and engineering degrees.

much more likely to be hospitalised for illness such as asthma, eczema, and viral and non-viral pneumonia.

Some of these illnesses are considered to be 'third world' diseases (e.g. acute rheumatic fever and tuberculosis) but are prevalent in New Zealand's underprivileged areas due to overcrowded or damp housing, the diseases' infectious nature, and lack of early treatment.

Poor health is not limited to the duration children are in poverty, with several New Zealand and international studies finding that childhood poverty results in 40 to 80 percent higher likelihood of poor health in adulthood, and about twice the risk of work-limiting chronic illness.[4] This represents a long-term health care cost to be borne by the state. It also represents a productivity cost to individuals, businesses and the nation.

Added justice system costs

Children growing up in poverty are more likely to be involved in the justice system, both as offenders and as victims.

The costs of crime in New Zealand total about $9 billion based on a 2006 Treasury study.[14]

About $4 billion of crime costs can be attributed to children and youth (under 21 years).[4] Four fifths of all convictions for crime are a result of young people drifting into crime before age 21. It has been calculated that, by eliminating child poverty, the costs of crime could be reduced by about $2.3 billion annually which is 1.2 percent of GDP.[4]

Our current spending to deal with the negative consequences of poverty represents potential savings that we could direct at reducing taxation or growing our economy.

CHOOSE KIDS: STRATEGIC INVESTMENT IN CHILDREN WILL BENEFIT ALL NEW ZEALANDERS

We can invest smarter and have greater beneficial impact on everyone's future

This paper presents the case for investing in younger and disadvantaged children to generate greatest and positive returns. Without greater strategic investment we will suffer a brake on the economy.

Today's children are the labour resource of our future. They will support the sustainability of society through an ageing demographic change. They are the roots of their, and our, future productivity and social fabric.

Given the size of the country's investments in health and education, it is imperative that these investments are effective for all children. This is particularly important for children in poverty for whom education and good health can break the vicious cycle of poverty.

All children should get a fair go

By choosing kids, we can create a better New Zealand for everybody. The ongoing costs of poverty, at 4 percent of GDP per annum, are simply too high for us to fail to address the underlying causes.

When we choose to invest more in young and disadvantaged children, we will position New Zealand better to meet the challenges of labour market demands, ageing demographics, and the drive for economic productivity so we can maintain our standard of living.

Strategic investment in children will benefit all New Zealanders.

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