

End of the ERA

The Labor supremacy in Australian politics seems to be drawing to a close. A new age of uncertainty looms. ALR assembled a roundtable discussion to assess the economic legacy of the Labor era, and to look ahead.

Tony Aspromourgos is a visiting fellow at the University of NSW. Mike Johnson is director of the Public Sector Research Centre at UNSW. Colm Kearney is professor of economics at the University of Western Sydney. Sue McCreadie is the economic research officer for the Textile, Clothing and Footwear unions. The discussion was chaired by Prudence Anderson, an economic journalist with the *Financial Review*.

It seems clear now that Labor's hegemony over economic policy in the 80s is coming to an end. Probably most of the Labor governments around the country will fall from power within the next two years. This makes it timely to look at the Hawke government's economic record over the last eight years. We first need to make some judgments about how successful the Hawke government has been in addressing the fundamental structural problems that have confounded all the social agendas that governments have tried to pursue for decades. You can't go constructing grand social visions on a very shaky

economic base. So: has the Hawke government been a truly radical government in terms of trying to come to grips with the economic problems facing this country?

Tony: Partly as a result of the way the Fraser government got burnt in the wages explosion of 1981-82, the basic strategy of the Hawke government from the beginning was built around employment growth within the Accord framework. Keating's argument was that the most important policy from a social equity standpoint was full employment. I've got a lot of sympathy with that. The policy of pushing the system to full employment should be an essential plank for Labor governments in power nationally.

The problem is that within two years, after a bit of pump-priming and a bit of help from the end of the drought, they came up against the external constraint. In 1985-86 the currency started free-falling and the central question which arose from that was: is the Australian economy structurally capable of generating full employment? Given the current rate of growth in the workforce, you're going to need probably a little over three and a half per cent real output growth per year to suck up that increase in the workforce



into jobs. Is that sustainable in our current situation? The answer that most people would offer is 'no'.

The strategy of structural adjustment was really an attempt to overcome those constraints. The buzz-word has been 'micro-economic reform'. I'd prefer to call it 'competition policy', because the basic logic of it is that an increase in competition will bring structural adjustment. I agree that full employment and a rate of growth consistent with that should be central to a Labor policy. The question is whether Keating's version of competition policy can get us there, and if it can't, what can, if anything?

So you're saying that Keating really hasn't spent enough time thinking about routes to adjustment.

Tony: He has, but he's come up with a policy which I don't think works. There's a lot of moralistic, almost theological nonsense about this—people are saying this is the recession we had to have, as if it's a cleansing experience. Well, you've got to get all that moral nonsense out of your head. The fact is that recessions do not restructure economies.

Mike: I think you're generally right, but you've missed the role of investment. Australia in the 70s and 80s clearly had an investment problem. That was critical to the government's priorities for structural change. Arising from the Campbell Committee in the 70s was the view that if you deregulated interest rates, and deregulation directed investment in the economy, you would get a flowering of entrepreneurial companies with new technologies and new directions. Associated with that, Keating specifically addressed the tax system to cure that investment problem. He did it in two ways. Firstly, he did away with the double taxation of profits. Then he reduced the top tax rates—adopting what has been the conservative view throughout the world during the late 70s and 80s, that if you redistribute wealth to the rich, they will invest it in productive sectors.

The truth of the matter was that they didn't do that because there weren't enough productive sectors to invest in. What they did was to go on a splurge in financial markets with a whole range of asset investments that have proved not to generate long-term real returns. The strategy to push structural change through redistributing wealth into new sectors collapsed on the rocks of the 1987 crash. And frankly, in 1991, the situation has not recovered. We've seen the rest of the speculative investments evaporate through the collapse of financial institutions in the late 1980s. That, as we look back from the 90s, was a critical failure.

Sue: We need to ask why there was this failure of investment. Was it simply a failure of Australia's corporate leaders to actually make the right investment decisions and turn their attention to the productive sector, or was it a failure of policy, or a combination of both? It seems the environment which the government created was one which biased investment towards non-productive investment. When they removed accelerated depreciation as a trade-off for reductions in corporate tax, that created a bias away from manufacturing and back towards the financial sector.

Mike: The other thing that's missing from the whole analysis is that Australia is integrated into the global economy. That is, we have become locked into a global financial system that has invested enormous financial assets, which were earned right back into the 1950s, in a whole range of speculative ventures, because real investment in productive enterprises in the sense of being concerned with tradeable goods and services has actually fallen away. So in the United States we have the Savings & Loans scandal, we have bank collapses in Britain, and in this sense Australia is just a follower, as it has always been a follower.

Colm: You asked: has the Hawke government been radical? And my answer to that is yes. Whereas previous Labor governments were concerned about the distribution of the national cake, as early as 1986, the World's Greatest Treasurer realised his policies had to be concerned about the generation of the national cake. That was traditionally the concern of the Liberal Party. So, that was radical for a Labor Party. But the policies that followed on from it were conservative ones.

As I see it, these problems are that we have an entrepreneurial sector that is both inward-looking and has a short-term horizon. Look at Germany, for example, where the relationship between the banks and the industrial sector is such that both loans and investments are much longer-term than they are in Australia. In Japan you've also got a system where trade unions, business and government take long-term investment positions. They will actually operate at a loss over periods of between five years and a decade to wipe out the opposition in foreign countries so that they can create export markets. What has happened here is that the 'level playing-field', together with deregulation, means we're tied into a short-term horizon and we're going for short-term gains. So no matter what kind of indirect lever you pull, it's not going to work.

If you look at the top 50 exporters in Australia, more than half of them are owned by foreign companies. That is completely at odds with all other major exporters in the world because we're suffering from the historical result of a tariff system which was put in place to be purely inward-looking. The Right has used the abuse of the tariff structure in Australia to argue for a level playing-field, and that's completely wrong; we have to tilt the playing-field in favour of exports.

If the problem has been one of improving the trade performance, presumably we have to discover how best we can provide a structure to do that, a way of setting goals and priorities...

Colm: It's easy. We economists are taught that there are four goals of government: full employment; price stability; imports equal to exports; and economic development. The practical policy objectives put in place by governments usually also involve some level of inflation. But listen to Hewson: zero to 2% inflation. That's absolute poppycock. In an open economy you cannot have a target for inflation which is set apart from the level of world inflation. We have targets on inflation, we have targets on unemployment. I

have never heard of a target for exports. If you can target a composite aggregate like inflation, why can you not have a target for exports? What we need to do is to target export growth.

Sue: Colm pointed out that the government was radical because it was focusing on the size of the cake rather than simply the distribution. I suppose what was new about the union movement under the Hawke government and the Accord was that it too was focused on the size of the cake. But it had quite a different perspective. What it sought of the Accord was, first of all, participation in public economic management - something which has not really occurred. There's been some element of participation through tripartite bodies like the Australian Manufacturing Council. But generally the old bureaucracies continued to exercise a very strong influence, while the new tripartite bodies had limited power to influence government decisions.

Colm: It's poppycock to argue we've purchased low inflation

The unions' agenda was modified in the light of both external circumstances and what was achievable in the context of government policy, but only aspects of it were ever implemented. There were the sectoral plans - the steel and engineering plans, the car plan and the Textiles, Clothing and Footwear plan - some more successful than others. But although history might tell you that it would have worked, you never have had that package implemented. There was a real failure to address that entrenched power in the bureaucracy—partly it's inertia and partly it's the dominance of that economic rationalist framework, which has had an overwhelming influence on decision-making.

Tony: I want to come back to this investment question. I agree that investment is the key to restructuring. The government seems to believe that profit share is crucial to getting that investment; in other words, that the overall balance between wages and profits was wrong, and had to be altered in the favour of profits. I don't know why: this is the weirdest economic fashion I can remember in my short life. In fact, I know of no systematic theoretical argument, orthodox or otherwise, as to why profit-share should determine investment.

On the other hand, I don't think the behaviour of investment in the 80s is particularly mysterious from a standard Keynesian point of view. After the recession of 1982-83, you had two years of strong growth; it took two years to rebuild demand back to something like normal capacity. And at that point in 85-86, if demand growth had continued, you would have seen investment demand respond. It was at

just that time that the exchange rate collapsed, the monetary brakes were put on, and interest rates rose, and that's what stopped investment from taking off at just the point where it normally would have, from a Keynesian point of view.

If there has been any real success from the shakeout of the last couple of years it has been the decline of asset inflation. I don't think we should underestimate the importance of this. The old Australian entrepreneurial method of relying on asset inflation in excess of commodity inflation, and therefore concentrating on capital gains rather than trading and producing commodities, has suffered really serious blows in the last couple of years. As well there's the fact that the entrepreneurs who specialised in reaping the benefits from asset inflation are going broke and some of them are possibly even going to jail. I think that is a really important event for the psychology of Australian entrepreneurship, and I think it will prove very beneficial.

As I said earlier, I do not believe this recession will restructure the economy. However, we can't rewrite history now; this is where we are. It is very important to sustain our present low inflation rate, because that really is the only thing we have to show for the amount of working-class blood that's been spilled in this recession.

Colm: I am pessimistic about Australia's ability to sustain low inflation, because we have done nothing to restructure the economy into a low inflation path. It's poppycock to argue that, as a result of the recession, we have managed to purchase a creed of low inflation. We haven't. As soon as demand picks up, commodity price inflation is going to take off again, depending on the vagaries of the exchange rate. Also, we have built into the system five years of wage restraint just waiting to bubble over and build again into price inflation.

What would be required to generate low inflation?

Colm: I don't believe we can generate permanent low inflation in this economy. Our inflation rate is tied to the rate measured as an average of the inflation rate of our major trading partners. And until we realise that, and build up our productivity and export performance, we're not going to do it.

So you see it as a totally inappropriate target?

Colm: It's completely off the planet. Our inflation rate is temporarily low; it's going to catch up.

Tony: Colm raised the question of targeting exports. I have to say I am doubtful, if you look at the sort of trade surplus required for Australia to stabilize foreign liabilities, whether export growth is capable of carrying the burden of restructuring. I wonder whether we're not also going to have to keep in mind import replacement.

Sue: That's probably one of the major failings of the Hawke government's strategy. There's been an obsession with exports, and there's been a move away from the initial goal of a more diversified manufacturing sector towards a more

specialised export-oriented one. The legacy of high tariffs has fostered the belief that tariffs alone are responsible for inward-looking and anachronistic practices and industrial lethargy. That in turn has tarnished the image of import replacement. That's a real problem because if you look at the approach of more successful economies you can see that in order to successfully replace imports you've got to have the latest in manufacturing technology; you've got to have high product differentiation; you've got to acquire all the things that the drive towards high value-added manufacturing and services require. But we've paid very little attention to this in the context of import replacement.

Colm: I agree that insufficient attention has been paid to import replacement. Rather the policy has been import curbing. That's of course the easier thing to do. If you want to replace imports, you've got to have an entire industrial policy, whereas if you want to curb imports, all you do is raise interest rates. And this government has gone for the easy solution. All I'm saying is, if you don't want to get caught in a cycle where you're dependent on external developments, then what you've got to do is raise exports.

Mike: That takes us back to the point Colm raised before. In other, more successful economies there's a longer time horizon and all the elements of the economic picture are interlinked. So, for example, German banks are interlocked with industrial concerns with an interest in exports. Yet in Australia this sort of interlocking of interests — which was in a sense the original intent of the Accord — has just never happened.

The most sustained attempt to achieve precisely those sorts of interconnections in Australia was of course in Victoria. Yet that legacy is now under a cloud. What happened in Victoria? How was it that a few major high-profile financial cock-ups eclipsed the value of all that was achieved beforehand?

Tony: There were two arms to the Victorian strategy — one of which I think was disastrously ill-conceived, and the other which may have survived if it hadn't been for the failure of the former. If I understand it correctly, the Victorian government believed it could run fiscal policy in the old-fashioned Keynesian way, independently of any back-up from the federal government. That was a fatal mistake. In severely constrained economies like ours there are grave limits on one's room to manoeuvre even at a national level. Moreover national governments have two things that state governments don't have, which make it much easier to cope with these constraints — they can dictate interest rates, and they can print money. Without that ability state governments can't set their own independent strategies at will. So Victoria should never have been in that game.

The other arm to the Victorian strategy was of course micro-economic intervention, which is clearly diametrically opposed to the Keating position on how to restructure the economy. And that I think had merit. It is a great pity that two or three disasters — albeit massive disasters, which will fiscally cripple Victoria for a long time — should be used to discredit the whole strategy. I don't know what

the hell the VEDC was trying to do, but whatever they were doing they were screwing up very badly.

Mike: The Victorian problem was a managerial failure resulting from the inability of the political apparatus to ensure that enterprises were financially responsible and accountable. The government utilised the existing financial apparatus and leadership without imposing any strong controls to ensure that investment capital didn't go into the pockets of enterprises or organisations that in some cases may have been corrupt, but which more often were just incompetent. Now all the bright features of the Victorian economy, which were a few, have been lost in this overall failure.

Colm: The same happened to the first Mitterand government in France in the early 80s. He tried to pump-prime demand, to "ride it out", while in the US and Britain they were running really tight fiscal policy stances. Mitterand was forced to bring his economic policy back into line with his major trading partners. Likewise Victoria was running a looser fiscal policy, when the federal government was tightening the reins.

Tony: The fact is, recessions do not restructure economies

Sue: Victoria has the VEDC fiasco and Tricontinental disaster among others. But overlaying them all is the problem of the recession now — that is arguably the most severe problem in terms of employment and output, and it's caused federally by tight monetary policy.

Colm: We can point the finger if we wish at the level of business enterprise activity in Victoria, but have the austerity policies of the Greiner government in NSW done much better? I doubt it.

Connected to these questions are the trends in public sector administration and management over the 80s — which, as Mike points out, played a role in the Victorian debacle. Obviously there's been a revolution in Australia in the 80s around these sorts of questions. How does this revolution measure up now?

Tony: The key issue here is the shift towards commercialisation and corporatisation in public sector management. The Greiner Government in NSW has adopted these ideas with a great deal of ideological fervour — too much, in fact. But the federal government has also been adopting them much more quietly — possibly because it has to appeal to a different constituency.

I have to say — and I know this is unfashionable on the Left — that I personally am in favour of a great deal of this trend. I think the financial balance between the budget sector and the trading enterprise sectors in government expenditure was clearly wrong, and that there was a need to reduce the subsidy from the budget sectors to the traded sectors. A lot of the cross-subsidies, both within the traded sector, and between the budget and the traded sector, were really a product of a massive dose of pork-barrelling. They had no real social justice, or equity, or access rationale, and there was a need to redress that. I think it's also true that the intervention of executive government in commercial government enterprises has an appalling history in Australia. The balance between accountability to the executive and ultimately to parliament on the one hand, and managerial freedom on the other, is a very complex question — much more difficult than either Carr or the Greiner government have understood. But nevertheless, I think the shift towards commercialisation is desirable and a good thing.

Mike: I agree that the government business enterprises were in need of shaking up, and the major enterprises within the sector — particularly electricity, water, and the banking system — needed to be put on a commercial basis. The truth of the matter is that in the past it wasn't on a commercial basis and there was a regime of jobs for the boys — and there were plenty of them, too. The health of the government business enterprises is vital to all other sectors of the economy, and so it's essential that they be run efficiently. The problem is that the debate has focused on reducing staffing levels, rather than restructuring them to become more effective and efficient. In the case of electricity authorities total efficiency means assessing not just supply-side efficiency but also demand-side and end-use efficiency. In the case of the transport system, the railways have to be adjusted to the needs and objectives of industry in Australia. Running rail lines to little towns may have a good social rationale, but even if it does it should be explicitly separated from the business objectives of the enterprise.

Did the labour movement ever really think that the conservative agenda for economic reform would work?

Sue: Those in the union movement who had an interest in industry policy always said this agenda wouldn't work. We don't really have a macroeconomic industry policy in the sense that none of the real problems about investment have been addressed. Tony earlier stressed the importance of aggregate investment. I think you have to break down that investment and look at the real failure to take up advanced manufacturing technology, and to look at things like flexible manufacturing systems in which Australia's performance is very poor. I agree, in a sense, with those in the union movement who said that the corporate sector has a lot to answer for in its failure to take up the opportunities available to it. In fact the blame lies jointly with government and the corporate sector; the problem for the unions is that they don't run either.

I feel somewhat pessimistic about the future of industry. If I wanted to look for a ray of hope then I would have to say

that one of the great visions of the Labor government has been to try to modernise the economy. There has been a commitment to a new workplace culture. The national training system, the focus on the skills base, the centres of excellence and the drive to try to link R & D establishments to industry and to TAFE colleges, are all part of that vision. It remains to be seen to what extent all that workplace reform is a permanent change in the way we operate or whether a drive towards labour market deregulation under a Coalition government would undo it all. The idea of the workplace resource centres was that they would survive a conservative government because they were bipartite, and perhaps industry would have had time to see it was worthwhile. The German national training system has survived a conservative government and it's something the country's very proud of. So perhaps when we look back at the Labor government in five or ten years we'll say that at least they laid the foundations in training and workplace reform.

This brings me to our final question. Here we are with our political cycle moving us towards what seems almost the inevitability of overwhelming domination by conservative governments-in-waiting with pretty hardline agendas. Yet elsewhere in the world these agendas seem to have been considerably discredited. How plausible are they for Australia in the 90s?

Tony: There is a strong feeling in sections of the Liberal Party that the Fraser years were wasted years; they had a tremendous mandate and controlled both houses — something which won't happen again for many years — and basically they did nothing with it. The conservatives may have more backbone this time than last time, but the nature of our entrenched two-party system is such as to move parties towards the centre in government. So the crucial question is: how much of the rhetoric of conservatism in opposition will be translated into policy in government? I think you've got to be sceptical based on historical experience.

Colm: This era of Labor government is now going to end as it began, with Australia emerging from a deep recession. When the boom comes, it's going to be a gradual boom in the United States, Europe and so on, and our trading constraints will be relieved even if we do nothing, so the conservatives will come to power shortly after the recession bottoms out. There will still be a rising economy when they go to the next election, and they will be judged as having engineered the emergence from the recession in the early 90s.

What are the implications of all of this for the labour movement and the Labor Party? We're going to have a Labor Party in opposition with a diminished trade union movement. There's going to have to be a fundamental rethinking of the role of the trade union movement in Australian politics and Australian economic policymaking. That is rather a pity, because one of the great positive contributions of this Labor government has been the enhancement of the standing of trade unions in the economic process. What is going to emerge from that rethinking process, I don't know.