Embargoed until 9.30 p.m.

16

# PRIME MINISTER

FOR PRESS

17 NOVEMBER 1977

## ADDRESS AT MORGAN GUARANTY DINNER, MELBOURNE

I heard an overseas visitor the other day describe Australia as a land of opportunities - a country which North Americans and Europeans regard as one of the few still having the potential to offer the excitement and adventure that goes with new development, and the potential to challenge and to extend the horizons of its people. I found it encouraging that overseas visitors should once again be talking like that. It is a sign that times are changing.

Five or six years ago, most Australians, as well as our overseas friends, were thinking along similar lines. Since then, we have been through a period of doubt and uncertainty - a period during which we tended to blame others for our misfortunes, and during which we became unsure of our capacity to solve our problems. In a word, we lacked leadership.

I believe that we have passed through that period and that a new prospect is now emerging - a prospect that Australia will not only provide much greater opportunities for advancement of its own people, and those who may come and join us here, but also a prospect that Australia will provide an example which others will look to when setting their own economic policies in the years ahead.

That is a large claim. Let me elaborate upon it. In doing so I want to refer to some basic simplicities about the Australian economy - and other such economies - that I fear were lost sight of during the leaderless period which I referred to, but which cannot be ignored if we are able to have regard to our underlying health and the future of our country.

I want also to comment on economic developments in Australia in relation to those overseas, and to put them into some perspective. You will not be surprised if in present circumstances I start by referring to the years before the present Government came to office. I do so because an understanding of the record of those years is fundamental to an understanding of the present state of Australia today, and because, as someone said, if we are not prepared to learn from history, we shall be doomed to repeat it. That is a thought, indeed, which I believe all Australians should have in their minds in just over three week's time.

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You will all be aware of the explosion, during the 1973-75 period, in both unemployment and inflation rates in Australia. It is a matter of clear public record that in the second half of 1974 inflation soared at an annual rate of 19 per cent, and at the end of 1975, unemployment was 5.4 per cent. These frightening developments - and I use that word quite literally - were accompanied by, and a product of, a sharp fall in business profitability and an equally sharp rise in personal savings. By the end of 1975 the share of company profits had fallen to 12.7 per cent compared to the long-term average of 17.5 per cent. While on the same basis, the proportion of incomes that people saved jumped from 9.8 per cent to 16.2 per cent.

The business community found itself on the anvil of a basically anti-business Government, while the hammer of the 1974-75 wage explosion - itself promoted by that Government - descended upon it. The results were entirely predictable. We saw the development within our business community of a "survival mentality" - an atmosphere in which only fools took risks because the future had become largely unpredictable; and because risk-taking, the fundamental process which underlies all private enterprise economies - and hence all free societies - was nolonger, so it seemed, to be rewarded appropriately in profit terms.

With labour costs exploding and profits plummeting, businesses went into their shells. As part of the cost-cutting processes of doing so, they found it necessary to lay off, or cease to take on, labour. The resulting sharp jump in unemployment itself added to the uncertainties from which ordinary consumers were also suffering, and which in turn were leading them to "button up", to slow down their spending and increase their saving.

What these events signified was that businessmen and consumers alike had lost the confidence to spend. They were too uncertain to commit themselves beyond the immediate future and for essentials. But over and beyond these developments, there loomed another threat to the future of Australia, or at least the kind of Australia that most Australians had come to hold dear. I refer to the threat of "Big Government" itself.

It is now a matter of history that the Government of the day reacted to the onset of the problems I have mentioned by trying to pump up the economy. In a series of wild decisions they raised the 1974/75 Budget deficit to no less than 4 and a half per cent of GDP, in the process increasing Commonwealth outlays in one go, from 24 per cent of GDP to nearly 30 per cent. The 1975/76 Budget deficit was originally set even larger in relation to the economy (5 per cent of GDP), and would undoubtedly have turned out even larger still if, half way through that year, a new Government had not set about reining it in.

But, you may say, pump-priming - however ill-judged - is one thing: "Big Government" as a philosophy is another. What became clear at that time to all with eyes to see - whether Australians, or our friends abroad - was that here in Australia we had a particularly virulent case of both.

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Through one scheme after another, the Government of the day sought to intervene more and more in the everyday lives of the people. The spending programmes involved were too numerous to count. Both the overt and the convert thrusts from the centre to undermine the independent powers and role of our state governments were clear for all to see. In one way and another it was sought to make as many of our citizens as possible dependent upon the Federal Government for their nourishment and even survival. This was the nation of pensioners which "Big Government" in Australia set about creating.

As to our economic troubles, there is of course a view that none of our troubles at that time was home-produced, but rather, some kind of malady imported from abroad; and there is of course the associated view that many overseas countries, faced with economic problems not wholly dissimilar, also took the pump-priming route in trying to solve them.

The first of these views is generally a self-serving one. I do not propose to waste your time by rebutting its obvious untruth. But as to the second view, I do have to say in all fairness that Australia under its previous Government was not the only country that tried to solve its economic problems at that time by restoring to the traditional post-war "Keynesian" pump. There were, however, a few countries that clearly or otherwise perceived that pump-priming "remedies" of that kind were outdated and inappropriate in a situation of high inflation and depressed profits.

They say that pumping out more money into the economy through swollen budget deficits, with the associated risk of exacerbating inflation, made no sense when the community's fears and reluctance to spend were evidently closely related to the uncertainties created by inflation itself. They saw that the problem was not in fact any shortage of purchasing power, but rather an unwillingness to employ that power until greater confidence in the future value of their currencies could be restored, and above all, an increasing distrust of Governments and the destabilising consequences of their interventionist proclivities. These countries, therefore, gave priority, first and foremost, to bringing down inflation, primarily by reducing their budget deficits and the growth in their money supplies.

I am referring of course to countries such as the United States, Germany and Japan, all of whom took strong action along these lines during 1973 or 1974. This action was successful in sharply braking and then reducing inflation in those countries. But initially, it also caused a reduction in their economic growth rates and an increase in their unemployment. In each of the years 1974 and 1975, for instance, the United States recorded falls in GDP and increased levels of unemployment. In both those years unemployment also rose in Germany while GDP was either flat (in 1974) or falling (in 1975). However by the end of 1975, the three largest industrialised countries were seeing a sharp decline in inflation, and economic activity was steadily recovering. While there have since been some periods of hesitancy, that recovery in economic activity has continued since that time in all those countries.

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The comparative success of the policies pursued by the three strong countries (in particular) did not go unmarked internationally. In some quarters - such as the OECD - it led to a significant rethinking of economic policy strategy. For example, the so-called medium-term strategy which was adopted at the June 1976 meeting of the OECD Ministerial Council recognised that "The restoration of full employment and normal levels of capacity utilisation in the OECD area will be progressive and take a number of years." Most importantly it recognised that ".. The steady growth needed to restore full employment and satisfy rising economic and social aspirations will not prove sustainable unless all member countries make further progress towards eradicating inflation." In short, it recognised that in the process of restoring economies shattered by inflation and its associated uncertainties, there could be no short cuts - no easy options.

Six months before this strategy was in place internationally, my own Government had already started to implement its essential elements here in Australia. On taking office, we moved immediately to cut back the growth in Government spending; to bring the budget deficit and the money supply under control; and to reduce the Federal bureaucracy.

You might be interested to know that if we had allowed Commonwealth staff to grow at the same average annual rate of the 1972/75 period, about $770 million would have been added to the Commonwealth salary bill. We did not seek to reduce Government spending in any unduly drastic way because we recognised that the economy had already experienced severe shocks and structural changes.

Nevertheless, within the past two years we have contained the rate of growth of Federal outlays in our first budget to less than half that of the previous year; provided for no real growth in our budget outlay in the current fiscal year; reduced the budget deficit this year to around two and a half per cent of GDP compared with five per cent or more when we took office; even though we have, at the same time, reduced the burden of taxation at a cost to revenue of no less than three and a quarter billion dollars, halved the underlying growth of the money supply, to less than ten per cent, and restored Australia's external competitiveness by a devaluation which we did not want and which we resisted for almost a year while giving our policies time to work, but which in the end, because of the deterioration in competitiveness which occurred under the previous Government, was forced upon us. The Government was confident that this devaluation would result in only a minor check to the downward movement in inflation, owing to the continuing firmness of its other policies. I am pleased to say that the Government was right. There can be no doubt that these policies have resulted in a transformation in the underlying health of the Australian economy.

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There are two ways in which that can be seen. The more common way, but also the more superficial one, is to look at the usual economic indicators.

Inflation, as measured by the broadly based indicators in 1976/77, was around 5 per cent less than in the previous year, and, so far in 1977, consumer prices have risen at an annual rate of around 9 per cent, about the same as the average for our trading partners. Company profits rose by 24 per cent in 1976/77 and the profit share is gradually moving back towards more normal - and more appropriate - levels. The household savings ratio has moved back about two thirds of the way to "normal" and the external current account position has improved markedly during 1977.

Since September last there have also been significant reductions in interest rates on Government Bonds, ranging up to more than half a per cent. This is the first consistent downward movement in the structure of Government Bond rates for more than four years.

These reductions reflect businessmen's reduced inflationary expectations and rising confidence. The yield movements are in line with the declines which have already taken place in important private rates.

I am confident that if current policies are continued, the downward momentum will gather pace and spread to a wide range of financial assets and securities.

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At times this will involve the Government taking the lead in reducing one or more of its rates: on other occasions it will involve the Government responding to movements already underway in non-Government rates.

The policy is to achieve, gradually, on a sustainable basis, a much lower interest rate structure.

In order to understand the transformation which the last two years have wrought in the Australian economic scene we have to understand what those two years have been all about.

They have not been about producing a "quick fix" for economic output, or unemployment, or any of those things, because, as I noted earlier, ther is no hope for us in policies of that kind.

What they have been about is the hard and undramatic grind of putting in place - and maintaining - the kind of policies which can gradually lead to the restoration of the pre-conditions for a return to more normal levels of economic activity and employment.

Seen in that context it is remarkable in one sense that we have been able to put our policies in place while continuing to achieve growth in economic activity and in employment. Not even the United States and Germany succeeded in doing that.

Thus, our non-farm GDP in the June Quarter of 1977 was 5% higher than in the December Quarter of 1975, and, over the two years to August, 1977, employment rose by 180,000.

By contrast in the last year of the Labor Government there was a fall in the number of employed persons.

But what I seek to emphasise tonight is not, as I say, those usual economic indicators. Much more fundamentally important, over this time, has been the re-establishment of broadly appropriate settings for our fiscal, monetary and external policies. I cannot emphasise that too strongly.

It is quite basic to any appraisal of the future of Australia in the years ahead. As a consequence, we have gone a long way towards restoring business and consumer confidence by bringing down inflation, and inflationary expectations and improving profitability. And above all, the shadow of "Big Government" is lifting.

What, then, of the future outlook?

I notice some suggestions overseas that it may now be appropriate for thos countries that have made some progress against inflation to stimulate their economies so as to deal with "unduly slow growth and increasing unemployment".

What these suggestions do not appear to take fully into account is that "unduly slow growth and increasing unemployment" in those countries are basically a reflection of inflation rates that are still too high, inflationary expectations that are insufficiently diminished, profits that are insufficiently restored, and above all, fears of the policy instabilities of governments. Fears the force of which, indeed, these very suggestions I referred to are in danger of confirming.

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In the United States, the Chairman of the U.S. Council of Economic Advisers, Mr. Schultze, recently complained that:

"Our inflationary problem also continues to plague us. Inflation is no longer running at the double digit rates of a few years ago, but the underlying rate of six and six and a half percent that persists is far too high for comfort."

He went on to note that:

"The years of deep recession and double digit inflation from which we are emerging left scars on the economy that will take a long time to heal. The severe economic decline of 1974/75 with the consequent reduction in employment, income, capacity use, and business profits was a shattering experience to business firms and to workers and consumers. Double digit inflation also had a devastating effect on business and consumer planning for the future. Memories of these events linger on and generate a climate of substantial uncertainty and nervousness aobut the future."

If those comments are true of the United States-which of course they are - how much more true are they of Australia, whose experience in all those regards cited by Mr. Schultze has been so much worse.

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Against this sort of background, it seems appropriate to ask what a policy involving increased government spending would do to further reduce inflation and inflationary expectations? The answer to that question is that it would clearly make them worse. And that, by doing so, they would further delay the full recovery of economic activity and employment.

By contrast, Mr Chairman, policies in Australia for the last two years have been based - and will continue to be based - on the firm conviction that rooting out inflation, and the restoration of confidence in the ability and determination of government to achieve and maintain that, are the key to restoration of economic health in this country.

I have indicated elsewhere that, with inflation in Australia in 1978, now forecast at around seven and a half percent or less, we expect to achieve growth in that year of around five percent. We also expect unemployment to decline steadily from February.

With more appropriate outcomes in the area of wage determination than we have been getting, the outlook could be even brighter. I emphasise, Mr Chairman, that all of these expectations are based on a continuation of existing policy settings. These will enable consolidation and further progress in reducing inflation and in restoring confidence.

In this latter regard it is significant that the engine of sustained recovery - business investment - is now moving into a higher gear. For without additional investment we cannot in the longer run, have growth in real product - or therefore in real incomes - or employment.

The government attaches particular importance therefore to the indications in the Statistician's latest survey that private enterprises expect to increase their aggregate new capital expenditure in the six months to December by no less than fourteen percent, in seasonally adjusted terms on the level of the previous six months.

On the same basis, the expected increase is thirty-three percent in the manufacturing sector and sixty-six percent in mining.

For over a year now, the government has monitored the extent and possible timing of planned investment of a large scale nature in the Australian manufacturing and mining industries. Major projects to commence in the next three years, some of which are under-way, are estimated to involve expenditure (in 1976/77 prices) of $6,000 million during their construction or development phases.

Aggregate estimates of intentions of this kind must inevitably be subject to some qualifications, such as trends in international trade and domestic political developments. However, the government is advised that $6,000 million in major projects can be classified as "firm".

Mining investment in particular appears set to increase significantly. Major project investment in manufacturing is also foreshadowed concentrated in a few industries, especially chemicals and mineral processing.

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In addition, a substantial, but as yet unmeasured, scope exists for the manufacturing sector to participate in the construction, mining and processing phases of the major mineral developments.

Looking ahead into the medium term, investment trends will be influenced significantly if a small number of very large projects proceed. These are the North West Shelf gas project, uranium mining, and processing, alumina production, open-cut coking coal projects, and petrochemical plants. It seems quite clear that Western Australia and Queensland will become increasingly important locations for investment not only in mining but also in manufacturing (mainly mineral processing).

I note also that the latest United States Commerce Department Survey of Expected Capital Expenditure by U.S. affiliates in Australia points to a twenty percent increase next year. A clear sign of the increasing confidence being shown by overseas investors in this country.

Since the removal of the V.D.R. capital inflow controls on 7 July this year, the flow of applications for private overseas borrowings has, as must be expected, been fluctuating. Nevertheless, there have been 93 applications over this period for private overseas borrowings, totalling $718 million of which $253 million is for mining; $199 for finance; $123 million for manufacturing; $83 million for commerce; and $60 million for property development. Approvals so far total 79 for $535 million.

This too is evidence of the confidence of overseas investors in Australia. It supports the case for the government overseas borrowing during the period while private investment is in the process of recovering.

To this internationally oriented gathering, it is particularly appropriate that I should say that the prospect of a new era of exciting development is opening up for Australia. The resources are there to be developed; the labour force is there to help develop them. Increasingly, too, the good sense of most of the people who make up that Labour force is re-asserting itself; as the great majority of Australian workers are coming to realise that higher wages do not reduce unemployment but increase it.

With the outlook for profits improving, capital will be coming forward to undertake the necessary investment projects. And is indeed already beginning to do so.

Last, but by no means least, businessmen and consumers alike can now look forward to a stable and predictable framework of government policies within which to go about their respective affairs. Australia is not yet out of the woods. But we have set out feet on the path towards goals which, when achieved, will make this country once again a land of which we can be proud, a land which can be an example to the world.

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