



PRIME MINISTER

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SPEECH BY THE PRIME MINISTER
CONFERENCE OF ECONOMISTS
SURFERS PARADISE - 26 AUGUST 1987

John MacLeod, Federal President of the
Economic Society of Australia;
Jon Stanford, Queensland President;
Ladies and gentlemen.

Your invitation to address the 16th annual Conference of Economists gives me my first opportunity since the July 11 election to articulate publicly the Government's thinking on issues of economic management.

By nominating as your conference theme the issue of "Economics Towards 2000", you rightly direct our attention to the long-term challenges Australia faces.

The dozen years which separate us from the end of the 1990s must see fundamental changes in the Australian economy and society if we are to meet those challenges.

Quite simply, if we do not make those changes we will not be a prosperous nation by the year 2000.

That is why over the first two terms of my Government we have focused our efforts on encouraging those changes through a strategy of economic reconstruction.

At the outset of this speech - in effect, at the outset of my third term as Prime Minister of Australia - I want to affirm in the clearest possible terms that this strategy, begun over the first two terms, will be continued in the third term.

We in the Government - and, I believe, the majority of economic professionals - have long recognised that thorough-going economic reconstruction is the essential response to the challenges the nation faces.

What is different since the election on July 11 is that our strategy has now received a resounding confirmation from the Australian people.

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In fulfilling our mandate we will carry through a full and testing agenda of change - an agenda which I wish to address today.

And let me approach that task by saying something of the achievements of the two recipients of your Distinguished Fellow Awards, Colin Clark and Trevor Swan.

Colin Clark has attained eminence in both academia and policy making. It is no secret that he and I have had some fairly profound differences, dating back to days at Oxford.

However I unhesitatingly pay him tribute as one whose work first elucidated many profound questions about the Australian economy.

Trevor Swan too, is a giant of the profession. His pathbreaking paper on "Longer-Run Problems of the Balance of Payments" is as relevant to the economic challenges facing policy makers in Australia today as it was when it was first penned in 1955.

We are all familiar with the Swan diagram and its analysis of policy prescriptions needed to secure simultaneously internal and external balance - prescriptions which vary with the initial economic conditions.

Australia, as you all know, has received a massive external shock. That shock coincided with a strong economic upturn, which compounded the inevitable balance of payments crisis.

In Swan diagram terms, the shock precipitated a massive external imbalance and policy makers had to find the correct adjustment path. The correct path was one which would both restore external balance and continue the progress which had been made to eliminate the internal imbalance originating in the high wage/low growth era of our predecessors.

The policy choices available to the Government in such a situation are far from simple.

Some adjustment paths would restore external balance rapidly, but at the cost of prolonged high levels of unemployment.

Other paths would press on with domestic growth but at a pace which would so prolong the task of external adjustment as to precipitate an external crisis of another kind - one born of an inability to fund the current account except at ruinous interest rates, which in turn, would jeopardise the attainment of internal balance.

The policy choices need also to pay heed to the varying speeds with which policy instruments can take effect.

Having freed up the exchange rate, the quickest response to the external shock was a large depreciation of the Australian dollar.

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That unleashed the most powerful force for change known in economics - a massive, not a marginal, change in relative prices. Moreover the deterioration in our terms of trade directly reduced the world purchasing power of Australians, which of itself will contribute to the restoration of external balance.

But those forces were not themselves sufficient to reduce domestic consumption and raise domestic saving to the extent required to lower substantially our dependence on foreign saving.

The magnitude of the external blow-out and the associated explosion of our nominal indebtedness further complicated the problem.

The longer it takes us to achieve the necessary domestic adjustments, the higher will be Australia's overseas indebtedness as a share of GDP and the more we will have to export in future just to sustain today's living standards. That fact has added an important time dimension to policy choices.

Labor's choices have struck the balance between promoting steady balance of payments adjustment while preserving jobs growth and rolling back inflation.

Of course the initial policy responses relied heavily on the most flexible of the macro instruments, monetary policy. However, over-reliance on tight monetary policy is not a feasible medium-term adjustment strategy, not least because of its dampening effects on employment and investment.

An essential element of the strategy, therefore, has been a medium-term assault on fiscal policy.

The external shocks of 1985 and 1986 gave added urgency to that task.

Labor began in 1983 to wind back the extravagant fiscal inheritance from our predecessors. Labor inherited a prospective budget deficit of 5 per cent of GDP. This year it will be less than 1 per cent - and real outlays growth will be substantially negative.

We will maintain our efforts to contain the growth of public consumption and reduce the call on total savings for as long as economic conditions require it.

There are some in the economics profession who believe that we have adjusted fiscal policy to Australia's external imbalance too slowly. They are advocating a balanced Budget or a surplus in 1987-88.

I believe this view seriously misinterprets the nature of the policy choices which lie before Australia.

Pursuit of external balance is vital in the long run. However no country should pursue external balance to the exclusion of everything else. Indeed, looking around the world these days, one might be pardoned for believing that none of the majors takes the achievement of external balance as a serious policy objective at all! However that may be a subject for another time.

Recent work within the Office of EPAC nicely illustrates the policy choices. They have extended the analysis presented in their paper entitled "External Balance and Economic Growth" to show that it is possible to accelerate balance of payments adjustment by almost 2 per cent of GDP over the next 4 years, compared with the adjustment paths of that paper.

To do so, however, at a constant real exchange rate, would require holding GDP growth back to a rate which would be insufficient to prevent significant increases in unemployment - unemployment which could only be avoided by further substantial real wage cuts. These are not policy alternatives which I believe the Australian people are prepared to accept.

That judgement was vindicated by the community's response to the May Statement - the toughest expenditure cutting exercise in 30 years - and most resoundingly, as I have already said, in its decision on July 11 to renew our mandate to govern.

As Paul Keating and I have said, there will be no horror Budget in September: this year's expenditure cutting task was largely completed with the May Statement and the Premiers' Conference.

We said that the 1987-88 Budget deficit would be well under \$2 billion.

We will keep those promises, and for three reasons.

First, it would be politically irresponsible to break such commitments in the absence of any intervening fundamental change in economic circumstances.

Second, we recognise that part of the reason for the success of our economic policy making lies in its consistency and credibility.

Third, it is our judgement that the fiscal adjustment path upon which we have embarked is appropriate to our circumstances - and a much faster pace would put at risk community acceptance of the broader economic reconstruction which is necessary in the longer term.

The second area in which there is some disagreement in the economics profession over the appropriate pace of adjustment is in the wages area.

There is one certainty in the debate over wages policy and that is that the best way of ensuring that there is no wage freeze is to call for one. Our political opponents elevated this to an art form with their insistence on both a wage freeze and decentralised wage fixation.

Trevor Swan and Colin Clark have lived through periods in Australia that have been characterised at one end of the spectrum by fully centralised wage fixation and at the other by a completely decentralised system, as well as various combinations through the range.

During the period of my Government the wage fixing system has evolved co-operatively to incorporate within a highly centralised system a significant degree of enterprise level flexibility.

This evolution has been no accident: it has been in response to the changing economic circumstances facing this country. It has the potential to become a major new instrument in our endeavours to progress towards simultaneous restoration of internal and external balance.

No Labor Prime Minister can take pleasure from presiding over cuts in the real wages of Australian workers.

But such reductions have been recognised as necessary by both the Government and the union movement in creating work opportunities for the unemployed and in adjusting to Australia's large external imbalance.

Only one set of statistics is needed to demolish the argument that Australia's response to our external imbalance would be more effective if a decentralised wage fixing system were installed in place of the present system.

Since 1983 real wages in Australia have fallen by around six per cent. This was despite a period, from mid-1982 to mid-1986, when a year of weak economic growth was followed by three years of strong economic growth. There have been four other such occasions since 1950. Only in the most recent period have real wages fallen. It is our cooperative, centralised wage fixing processes that have made this unique outcome possible.

In setting the timetable for, and in designing the policies to achieve, external and internal balance, my Government has rejected the short-term perspective so characteristic of post-war Australian macro policy.

Worldwide conditions clearly indicate that it is a forlorn hope to suppose that another commodities boom is around the corner waiting to revive the Australian economy.

Accordingly, we have to look to long term reforms as well as adjustment to macro policy. These reforms, essential to provide the basis for viable long term growth, will assume greater significance in our third term.

This is not simply a matter of awakening a previously comatose manufacturing sector so that it can play a pivotal role in the reconstruction of the Australian economy. That is challenge enough.

But the challenge goes deeper - and it will continue to confront us for decades to come.

Australian manufacturers - workers and management alike - must be prepared to take on and beat the most nimble and most inventive of our highly efficient competitors, especially those in our region.

Our manufacturing and our services sectors must also recognise that it will be some time before Australia's dependence on commodity exports has diminished sufficiently to insulate our exchange rate from fluctuations in commodity prices.

In these circumstances, our management and work practices have to be sufficiently flexible over time to sustain our competitiveness.

Our competitors have developed this skill. So must we.

This is not a new imperative for our major commodity exporters. As a group they tend to benefit from high commodity prices - the converse being that in a depressed market such as now exists, they too must be flexible enough to remain cost competitive while maximising employment.

In cases like the coal industry there is an additional danger that inflexibility can translate temporary losses of competitiveness into permanent mine closures. This is a prospect that both workers and management must recognise and seek to avert.

However the need for reform goes beyond one or two industries. All sectors need to be efficient and adaptable lest the imperfections in one area handicap the performance of the others. Moreover, successful micro-economic reform can accelerate the pace at which external and internal balance can be re-established.

We have to extend and build upon the more general reform of the micro-economy begun during our first two terms. The objective is simple: to boost national productivity and to create the flexibility to respond to external shocks and opportunities both quickly and decisively. We want, through national reconstruction, to build a more adaptable and a more resilient economy.

Our agenda will undoubtedly grow as the task proceeds. But as our third term begins, I see the following broad areas deserving our early attention: transport including aviation, communications and the information industries, government-owned business enterprises, education, industrial relations and industry assistance.

Transport and aviation services account for a high proportion of costs in many Australian industries. Past transport policy and practice have not kept costs down, and this has exacerbated the disadvantages of Australia's isolation and our dispersed population.

Accordingly one of the major items on the agenda of this term of government is a sweeping reform of the nation's transport infrastructure.

An information reference has gone to the IAC on coastal shipping; a joint Australia/New Zealand study has been conducted on trans-Tasman shipping; the Interstate Commission is overseeing efforts to improve waterfront productivity.

We have announced our intention to terminate the two-airline agreement. We will complete the national highway. And we will seek to improve performance on the waterfront and in the rail freight network, including grain handling.

In the communications field, we are currently seeing the merging of communications technology and the information industry to such an extent that communications is both a significant input cost to Australian industry and potentially a major growth sector.

Legislation, and the dominance of Government business enterprises, mean that Government decisions, or the lack of them, will have a major influence on the future of this sector. The question is how do we ensure that it operates at peak efficiency.

This raises the wider issues associated with public ownership of business enterprises - issues which were canvassed in the Government's Green Paper on Statutory Authorities and Government Business Enterprises.

We will need to examine ways to improve the performance of these enterprises. Options include improved performance criteria, exposure to greater competition, and the consideration of sales to the private sector.

As you know I recently called for a comprehensive debate within the forums of my Party on those parts of its Platform which express opposition to the sale of Government business enterprises.

I suggested two tests must be applied.

First, does public ownership of a given enterprise mean that significant functions are undertaken that would not be if the private sector had the responsibility for funding, owning and operating the enterprise?

If the answer is 'no', then, second, what are the disadvantages and advantages of retaining public ownership of that enterprise, as opposed to transferring it to the private sector?

This in effect reverses the onus of proof: the question should be not 'Why should we sell a given enterprise' but 'Why should we continue to tie up our resources in it?'

What must emerge from this debate is the formulation of relevant and contemporary criteria describing how the totality of Government resources and instruments can most efficiently be applied to the achievement of our broad national objectives.

I believe some of the parameters of the debate have already emerged.

For example, it will be apparent from what I have already said that the Government rejects the dogmatic view that public ownership of business enterprises is inappropriate by definition.

Similarly, we reject the proposition that the current pattern of public ownership is by definition the necessary and most desirable one.

Efficiency in the achievement of national goals is the key, not some ideological debate about appropriate aggregate levels of public ownership.

Of particular relevance to the broader themes I have been presenting today is the assessment of whether publicly owned enterprises in the late 1980s and into the 1990s may actually be hampered in the effective delivery of their services by the fact of their public ownership.

We must, for example, examine whether the need to further reduce Budget outlays and the Public Sector Borrowing Requirement is itself constraining the ability of the Government to provide the capital which some publicly owned enterprises need to perform their tasks efficiently and effectively.

Freed of these constraints, these enterprises may become more efficient and more viable - an outcome which could only benefit consumers, taxpayers and the employees of the enterprise itself.

Turning briefly to education and training, the depth and breadth of labour force skills will also have a strong bearing on our capacity to boost competitiveness and enhance the flexibility of the Australian economy. Indeed the need for continuing education and retraining throughout the working life has never been greater.

In Labor's third term we will build upon our very considerable achievements, which include and increase in school retention rates from around one-third to over 50 per cent; the removal of financial disincentives to stay longer in education and training; a 37,000 increase in tertiary places; and a doubling of funds provided for training.

There is also further room to improve our industrial relations and productivity performance - although Labor's policies have already yielded a 60 per cent reduction in working days lost through industrial disputes.

A basic factor in this achievement has been the increasingly sophisticated understanding by the trade union movement of the challenge of competitiveness.

The most recent measure of this awareness is the ACTU's report "Australia Reconstructed". While I do not necessarily endorse every single proposal in that report, I welcome it as a valuable contribution to the debate about the key issues the nation must resolve. As such I believe it deserves the very close attention of industry and of the economics profession.

I have spoken already about the two-tier wages system and the removal of outmoded work and management practices. But there is more to do. We will encourage the gradual amalgamation of trade unions and make necessary reforms to the industrial relations system without changing existing sanction provisions in the Conciliation and Arbitration Act and other relevant legislation.

Finally on this list of micro reforms the next three years will see a continuation of Labor's efforts to lower gradually the levels of industry protection.

We cannot, as a nation, hope to be internationally competitive if we persist in insulating key industries against import competition.

We are asking Australian industry to stand on its own two feet after a period of adjustment.

Sectoral plans are already in place for our most heavily protected industries, designed to phase down protection levels while easing the burden of adjustment on those directly affected.

Our R&D incentives and our industry extension services are designed to facilitate this industry restructuring process.

These items on Labor's agenda of micro-economic reform are not unrelated. Progress on some will make progress on others easier. To take an example, if transport and communications costs are lowered and our education system better meets industry needs, the need for industry assistance will lessen.

In working through this agenda, my Government will of course be seeking to enlist the support of the States, for in many areas it is they which have the immediate regulatory or administrative responsibility.



Ladies and gentlemen.

The past few years have served to highlight the structural weaknesses in the Australian economy and its vulnerability and inflexibility in responding to external shocks. From day one my Government has set about tackling those weaknesses, through both macro-economic and micro-economic policy tools.

Fundamentally the task demands attitudinal change. As such it is a task which government cannot successfully perform alone. It is one which requires the understanding and application of the whole community.

Let me finish by calling on you, then, as an audience with a matchless understanding of the challenge we face, to help make clear to our fellow Australians the urgent necessity of the strategy of structural reform I have outlined today.
