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Proceedings of the Summary Session

DISCUSSION PAPER NO. ~~B11~~ B10

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DISCUSSION PAPER SERIES B

THE BROOKINGS SURVEY OF THE AUSTRALIAN ECONOMY

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SUMMARY SESSION

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BROOKINGS CONFERENCE SUMMARY SESSION

FIRST SPEAKER: Professor Fred Gruen, ANU

There are three things I thought it would be useful for me to do in this final session. Firstly, I would like to say something about the draft introductory chapter for the Brookings volume which has been prepared by Professor Krause and circulated with the Survey papers. Secondly, I would like to make some possible suggestions as to what might be included in the final chapter of the book. I know there have already been a lot of comments but I will add mine as grist to the mill. Thirdly, I will highlight those parts of the Survey which I have found new, useful and surprising. I will leave the major summarising of the papers to Vince FitzGerald.

The question of Australia's economic performance is tackled by Krause very early in the draft introduction. In fact on page 2 he says that a case can be made out that our economy has been performing badly for a very long time. Using Maddison's[1] data, which is reproduced in Table 2 of the Introduction, the GDP per capita in Australia and in a large number of other countries is presented as a percent of US GDP per capita. There are a number of points that need to be raised about these data.

Firstly, there is the possibility that the figures for the

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1 Angus Maddison, "Phases of Capitalistic Development", **Banca Nazionale del Lavoro Quarterly Review**, vol. 30, June 1977.

earlier periods will be revised. These figures have been derived largely from work done by Professor Noel Butlin.[2] At present Ian McLean and Jonathon Pincus are engaged in a certain amount of rewriting of this economic history; hence it is conceivable that these figures are shakier than we have been led to believe.

Secondly, if you look at Table 2 (Table 1 of this Summary) you will in fact find that the deterioration of Australia's economic performance compared to that of the US occurred entirely in the first part of the period. The really disastrous performance of the Australian economy - if we believe the figures - is during the period 1890-1929. After that we have had some improvement in our per capita growth relative to the US. Not only have we had an improvement in the actual growth rate but we have also become more respectable by international standards. As you can see from the figures Australia did not drop relative to the US after 1929. If Krause had provided more detailed figures then I think you would find that there was some evidence of an improvement in the 1960s, and some deterioration which set in again from the late 1970s.

In as far as the Australian performance following World War II is a bad one, it is a bad one that is shared by the other Anglo-Saxon economies. In other words, if our performance is bad so is that of the US, and we all know about the UK. My personal belief is that the figures suggest (although this particular

2 N.G. Butlin, **Australian Domestic Product, Investment and Foreign Borrowing 1861-1938/39**, Cambridge 1962.

TABLE 1 *

GDP Per Capita and Economic Growth in Industrial Countries, 1870-1976

(1970 US prices)

	GDP per capital as percent of US (US=100)						Annual average growth rate (%), 1870 to 1976	
	1870	1890	1913	1929	1960	1976	GDP	GDP per capita
Australia[a]	173	145	107	74	75	80	3.2	1.1
Austria	53	na	58	48	54	69	2.6	2.1
Belgium	123	104	82	75	66	84	2.1	1.5
Canada	80	77	81	70	78	91	3.8	2.0
Denmark	69	66	73	64	66	76	2.9	1.9
Finland	52	42	41	39	54	71	3.1	2.2
France	87	71	67	66	67	87	2.2	1.9
Germany	68	60	58	51	70	81	2.5	2.0
Italy	69	46	42	37	43	53	2.3	1.6
Japan	35	33	29	32	35	77	3.8	2.6
Netherlands	123	87	69	70	69	80	2.7	1.4
Norway	63	52	47	50	65	85	2.9	2.1
Sweden	54	48	55	61	79	88	3.0	2.3
Switzerland	104	88	74	85	85	78	2.4	1.6
U.K.	124	103	81	67	70	67	1.8	1.3
U.S.	100	100	100	100	100	100	3.5	1.9

Source: Maddison (1977).

a. The Australian aboriginal population is not included in these data except in 1976. When included GDP per capita drops (and population increases) by 9 percent in 1870, 4 percent in 1890, and less than 1 percent in subsequent periods (according to estimates of the aboriginal population reported in Smith (1980)).

* This Table formed Table 2 of Professor Krause's Draft Introduction, as circulated to the Brookings Survey Conference.

Table doesn't show this) that the gradual freeing of the economy in the 1960s and the mineral developments in the later sixties did have a favourable effect on GDP growth per capita. Something of that can be seen if one looks at the figures for the period, say, from 1960 to 1976. But from 1970 on there is evidence of some substantial deterioration relative to other countries. I think that one ought to break down the figures for this period and look at them in more detail because it is an important part of the story.

Why the economy went wrong in the 1970s is of course something that will require detailed historical, economic and other social research. My hunch - for what it is worth - is that the breakdown of an authoritarian, centralised wage fixation system when the union movement rendered inoperative the sanctions provisions of the centralised wage fixing system, was one of the major factors responsible for our relative deterioration after about 1967. Attempting to bring the anarchical powers of individual trade unions back under some economic or social control is, I think, a major underlying reason for the relatively worsening performance of Australia in this period of the 1970s. This is of course entirely my own view. There are people who believe it is still all the fault of the Whitlam Government; others that it is entirely the result of the restrictive policies of Federal governments which have led to this relatively worse performance. However, it is my view that the fundamental cause was the breakdown in the 1960s, of an authoritarian, centralised wage fixing system.

Once large scale unemployment returned in Australia, all sorts of beggar-my-neighbour growth reducing policies from the 1930s were reinstituted: we have myopic market protection, myopic job protection, myopic regulation to stop change and growth of all kinds. It is hard to get concrete evidence as to whether the beggar-my-neighbour growth reducing practices here are worse than those in other countries. But I would argue that there are some reasons why they may be worse. We are a smaller economy; we are not part of the Common Market - which makes it easier for pressure to be applied to government to shield particular groups from competitive forces. The fact that New Zealand has done even worse than we have confirms a thesis of that sort.

As most of the Brookings authors have noted, Australians are very concerned with distributional issues and that there is a good deal of resentment of income changes which are imposed by outside forces. Hence attempts are made to resist such income changes by calling on the government to aid individual groups. This is, in my opinion, one of the reasons why we have had perhaps more of these myopic protective policies than some other countries.

With regard to the final chapter of the volume, it could contain all the things that are not covered elsewhere in the Survey papers. There are very many topics which are candidates, David Morgan has suggested taxation but I don't think that the final chapter is the right place. More obvious candidates are immigration, perhaps transport, perhaps something on the growth of government, and perhaps something on regulation. Another topic which that chapter could include and highlight is the whole issue of continuity and change in Australian economic policy. In particular I think it would be useful to have an assessment of the impact of the Hawke Government so far on the areas surveyed by the authors.

The chapter could also highlight the major findings on policy issues which confront this country. Amongst those that have been indicated are inward-looking policies, the stance of fiscal policy, wages policy, taxation reforms and related federal issues.

Overall I am very happy with what the authors have delivered, especially the useful way in which they have summarised the general options that face policy makers in the different fields. I am not going to comment on all the papers but will mention some of the things that struck me as particularly interesting.

For instance, Henry Aaron's characterisation of the Australian social welfare and tax system as being generous both at the top and at the bottom. He was referring in particular to the aged, but I think it is something that may be more generally applicable. There is something really rather strange about government policies which are generous at these two ends: it goes completely contrary to the Down's median voter principal. Aaron's observation prompted me to ask, how did we get a system with these characteristics? It may have arisen in this way: first of all an attempt was made to help the poor - this is the background of the original old fashioned welfare state notions that go back to the Poor Laws in Britain, in Australia and in many other countries. Australia retained that system and subsequently a lot of pressure was brought to bear for the provision of tax incentives to encourage people to look after themselves - and not to rely on government largesse. Such incentives tend to be taken advantage of by those with higher potential tax liabilities - in other words the rich. Hence we get a system which is paradoxically generous at both ends of the income scale. It is not surprising that such a system is widely regarded by "the community" as unfair. The median voter compares him/herself with the people at either end of the scale and finds a system which Henry Aaron has called anachronistic.

In the same paper, I was surprised to find that Henry Aaron considers that we have established an institutional framework for containing an escalation of health care costs. I would like to see it in operation for a few years before I will believe that to be the case. If we have done so, we have found out how to square a circle.

There is one point on which I would take issue with Henry Aaron. He says that he finds it not surprising that the group one might broadly call "the left" in Australia cannot accept what he calls the image of the government as repairman, or what other people call the residual model of welfare. Granted that the left believes that the results of market pressures are fundamentally immoral, why is it that if people feel the existing system of income distribution to be unfair they cannot also logically argue that those inequalities should be removed and not squander public monies on those who have made ammoral gains. I do not quite understand why anyone who believes that market forces fundamentally give the wrong income distribution, cannot also accept the image of government as repair man. (I might add that a very large number of thinkers from across the political spectrum, from Hayek on the right to those on the far left, believe that it is basically not so much an immoral system as an amoral system).

Turning to Larry Krause's paper, I had not thought that he would be able to say something about Australia's comparative advantage that we did not already know. I must confess I was surprised by what he came up with. The most innovative part of his paper was the analysis of where in the technology spectrum Australian comparative advantage might lie. I was somewhat disappointed that this was not taken up in the discussion. However it did not surprise me that it is likely to lie with middle technology and specialised items of the type he lists in Table 8, and does not lie with Barry Jones' grandiose high technology scheme of attempting to pick sunrise industries. Krause's suggestion makes intuitive sense and seems to me to be the sort of useful by-product that we are going to get out of this study.

I found particularly useful John Helliwell's lucid discussion of Australia's econometric models and what they have failed to tell us about the mineral boom. There are a few paragraphs (pp.113-114 in the Survey volume) which tell us the direction econometric models ought to take if they are to give us more useful information about the short-run and macroeconomic effects of large scale resource developments. I would like Helliwell to develop two notions to which he has referred very briefly in his conclusions. Firstly, that incentives to encourage downstream processing are more likely to dissipate economic rents than to create a stable, long-run industrial base. This seems to me intuitively sensible but I would like him to spell out more fully why be believes it to be so. Secondly, I would also like him to develop the notion that the really important decisions related to resource development are likely to be the microeconomic decisions.

On the fiscal federalism paper, Ned Gramlich may be pleased to hear that he has found a convert. I was one of the people who did not take the federal system seriously. In fact when the Brookings Survey was first commissioned I could not see why we should have a paper on federal-state financial relations; it seemed to me that that Russell Mathews handled that area quite adequately. I was told that the Americans might be interested and could look at the system in a different light. The result is that I am a convert - we ought to take our federal system more seriously. I am also convinced that we do not need a Loans Council; I am convinced that it does more harm than good that we subsidise all State government borrowing to the tune of 33.3%.

Let me turn to Dan Mitchell's paper. I had considerable worries about the likely treatment of this critical part of our economy. Dan Mitchell spent only two weeks here, how could he possibly gather all the information he would require? I need not have worried as it is one of the best chapters. I will focus here on only two of the labour market issues discussed by Mitchell, and also parenthetically by Dornbusch and Fischer.

The first issue is, would a successor system to arbitration be likely to show greater sensitivity to demand restraint? I think the discussion on pages 31-32 of Mitchell's paper (pp.161-162 of the Survey volume) provides a reasonably persuasive case as to why it would not. Unless the loosening or abolition of compulsory arbitration also involves a major contraction of union coverage, it is difficult to see it having any major effects on the overall response of wage movements to changes in levels of economic activity. As Dornbusch and Fischer put it in their pithy way, if the Arbitration Commission were somehow abolished, the Australian wage determination system would show all the discipline of the British system!

The second labour market issue I will mention is the prospects for an incomes policy and can there be one under an arbitration system. Here I do have some worry about Mitchell's suggested solution - that we should have "a creative differentiation of settlements to break the force of comparative wage justice". In as far as he will succeed in doing this, he will be doing it at the expense of a further erosion of the tax base. That may seem a good idea in the short run, but not, it seems to me, in the long run. Nothing much has been said about the mechanism which the present government has attempted to put in place, which basically relies on inflation. It relies on the six-monthly money wage increases being awarded only to those unions who sign the Accord. This I think, has the prospect of lasting for a while, provided inflation and legally passed back money wage increases do not get too small in the process. In other words, if the Accord were too successful in reducing inflation then we would have the position where there is no quid pro quo in the system. Although this seems fairly obvious, the point does not seem to have been made publicly until now - though someone in the official family may have done so. Dornbusch and Fischer say, and I concur, that the Arbitration Commission does not represent an ideal vehicle for an incomes policy. Nonetheless it may be the best wheel in town with which to play.

Finally, let me pick one bone with our visitors. I had expected to get informed outsiders' views of the features and problems of the Australian economy. What we have is one particular outside view - a view very much conditioned by the experience of our visitors as US economists. With the access that these authors have to the relevant information on other western economies through their ubiquitous data banks, I had expected fewer US-Australian comparisons and, for example, many more Dutch-Australian comparisons. In many ways the US is not the most useful comparison for us: it is twenty-five times larger, it is much less unionised. And just to name one other example, I think it is the only western economy where unemployment now is less than it was ten years ago, whilst of course in Australia and most other western economies it is many times higher. There are many other differences, and I do think it would be useful to have some non-American/Australian comparisons in the book.

On the whole, I believe we have the makings of a good and very useful volume on the Australian economy.

SECOND SPEAKER: Dr Vince FitzGerald, Dept of Finance:

I should note at the outset that Fred Gruen and I have not worked out any very precise division of labour between our two presentations, so there may well be some overlap or omission. No doubt the subsequent general discussion will fill the gaps.

I will try to do two things:

- first, to recapitulate and draw together into a reasonably connected summary what seemed to me to be the main themes and most interesting points emerging in each of the sessions
  - looking particularly for those insights which came from taking a fresh look, through **foreign** eyes, at our economy; and with the emphasis on points of policy relevance; and
- second, to single out along the way topics which seemed not to be covered adequately in the survey papers as they now stand
  - and which might receive more attention in the final versions, or which the concluding chapter might look at.

Given the time constraint, I will necessarily be rather selective.

Generally speaking, the view of the Australian economy which is emerging from the survey papers is one of an economy which is fairly well managed (with some problems) but - even against the background of the new data just presented by Fred Gruen, which seems toput the U.S. (and the U.K.) in the same boat - has turned in a rather lacklustre performance over the decades. Why this should be the case has not been addressed in a fully integrated way, although some elements of a diagnosis are there in a number of the papers:

- protection policy is, to no-one's surprise, implicated; but there is not yet a solid treatment of this, and virtually no treatment of other forms of regulation **not** at the border;
- our wage-setting institutions and other labour market rigidities also feature at the micro level and, at the macro level, in the form of real wage rigidity;
- generally, other "macro" factors seem less important than "micro" (including non-economic) ones in explaining our relatively mediocre economic performance, although there were suggestions that more scope was available to us than was exercised for fiscal stimulus to maintain or raise our growth rates, and that our exchange rate could have been managed so as to be more conducive to growing involvement in world trade.

As I have said, I think there is scope for the opening and/or concluding chapters to attempt to draw together such elements, and others, into a more satisfying overall diagnosis than has so far emerged.

(i) **Dornbusch and Fischer**

The Dornbusch and Fischer paper was one of the most interesting and the discussion following it gave a lively start to the conference. The paper itself has its flaws. There are about 30 pages which cover mainly familiar factual material before we get to the interesting ideas. There is also a question whether in such a survey as this the authors should have given as much weight to the real wage resistance hypothesis they advance, resting as it does on some rather preliminary research.

Such quibbles aside, the paper is an interesting and provocative discussion of key questions:

- is there a Phillips curve and where and how favourable (or not) is it? What makes it shift?
- in particular, do our wage setting institutions shift the curve?

- is our unemployment classical, Keynesian or a mixture of both?

- what scope is there for expansionary fiscal policy?

- how should monetary and exchange rate policy be used?

Wages and labour market issues were also addressed by Mitchell in his paper. I will come back to one or two of those issues under that heading. As for what Dornbusch and Fischer themselves had to contribute here, their suggestion that real wage resistance has been an important factor in making the Phillips trade-off more adverse is well worth following up: I think Adrian Pagan was persuasive in arguing that the research done so far has not established the proposal very securely.

Dornbusch and Fischer's suggestion that in a country like Australia, with downwardly rigid real wages, a floating exchange rate carries particular risks is very policy-relevant and their suggestion that monetary policy should be used flexibly (with nominal income targets) to minimise those risks requires spelling out and more detailed canvassing of the issues it raises. Indeed this points to one of the gaps in the Survey. Neither in this paper nor in Andrew Carron's is the general topic of monetary policy - objectives, targets, instruments and conduct - covered adequately, as Tom Valentine and Peter Jonson both noted.

Perhaps where Dornbusch and Fischer run most against Australian orthodoxy is in their criticism of the exaggeration (as they see it) prevalent in Australian official circles of limitations to the use of expansionary fiscal policy. This may be a case where the view through foreign eyes is not the same as the view from closer up. Taking their points about "crowding out" being unlikely to be more than partial and the structural deficit being more relevant than the actual deficit, nevertheless leaves unsettled the issue of just how far there is scope for **sustainable** fiscal expansion.

The most recent data on the stock of public (not just Commonwealth) debt in Australia would show sharp rises following the low 1981 figure which is the latest presented in the paper's Table 13, and the figures are certain to rise significantly further. In that light Peter Jonson's question abut the effects, in an open economy context, of enlarging the public debt through continuing deficits needs addressing.

Other speakers (including Max Corden and Michael Porter) were also persuasive in suggesting that alternatives to the paper's acceptance of centralised wage setting need more careful consideration.

(ii) **Helliwell**

John Helliwell's paper presents well three main topics - an historical and basically macroeconomic perspective of resource development in the Australian economy, an investigation of the significance of the so-called Gregory thesis and various micro-economic issues arising from resource development.

Perhaps the most useful aspect of the paper is the broad historical perspective it provides. It would have been useful for Australians to have seen the recent so-called "resources boom" in such a perspective at the outset. Perhaps it might have helped us avoid some of the exaggerated expectations that were evoked, with markedly adverse consequences, if we had more clearly seen the prospective increase in mining and related investment as a fairly "normal" "up" in a long history of ups and downs.

One of the most interesting aspects of the paper, to me, was its survey of what available quantitative analyses with the various Australian econometric models show about the sizes of the "Gregory" and other effects of the "boom". However it would have been more interesting if some of the identified deficiencies of those analyses had been further resolved (of course this would have required more help from the modellers).

The paper and the discussion of it canvassed interesting "microeconomic" issues, including electricity pricing, resource rent taxation, and so on. Some of the subsequent comments were very interesting, for example, those of John MacLeod on capital cost inefficiencies in public constructed infrastructure and the credibility (or rather, the lack of it) to the private sector of front-end bidding systems for attempting to extract resource rents.

Ed Shann made a point in this session on the volatility of Australia's terms of trade, reinforcing Dornbusch's point about the significance for macro policy of fluctuations in the exchange rae, given the downwards rigidity of real wages. John Helliwell was right to come back to this point about the link between the terms of trade and wage determination in the session on Mitchell's paper on the labour market.

(iii) **Carron**

The Carron paper complements the Dornbusch/Fischer coverage of macro-economic policy although as I have noted I think neither paper adequately covers the subject of monetary policy in

Australia. I also think that, at least for those Australians who have read the Campbell Report and some of the subsequent discussion of it, this paper may be one of those which can be regarded as directed more to an audience of foreign students of the Australian economy and its institutions, than to Australians. Nevertheless Carron does succeed, in this very well traversed area, in bringing out a number of interesting insights:

- he canvasses well the implications of the strong seasonal pattern in liquidity formation (due to the Budget) and is right to suggest we put this matter on the agenda for policy attention;

- also, Carron points out an interesting aspect in that our financial institutions seem to provide less intermediation than do financial intermediaries in overseas economies, possibly due, in part, to regulations which have now begun to be dismantled (but which are still fairly fully reflected in the available data).

I suggested a moment ago (as others did in discussion) that the topic of monetary policy has fallen between this paper and that of Dornbusch and Fischer. There are one or two specifics I would mention in that context. Remedying the gap might pick up Peter Jonson's concern about the effects on the ability to do monetary analysis, and to conduct monetary policy, of rapid financial evolution (including the move to a floating exchange rate which came since Carron's paper went to press). Also, the aspect of direct controls versus market-oriented monetary policies could also be canvassed more, as Kevin Davis suggested.

(iv) **Gramlich**

I personally found Ned Gramlich's paper one of the most interesting, in that it traversed matters with which I had thought I was reasonably familiar, in a way which did generate some fresh ideas. His raising of issues such as the future of the

Australian Loan Council will no doubt spur further debate. This was one area of his topic where a difference of approach with Russell Mathews emerged - one of them would abolish the Council; the other would make more "rational" the allocation of general purpose funds, and possibly reduce the grant element, while keeping the Council. While there is an issue of the appropriate degree of Commonwealth control over the borrowings of the remainder of the public sector, I myself felt Gramlich put the better case.

I am not sure who, of Gramlich and Russell Mathews, won on points the various other debates which arose between them, but Gramlich certainly scored highly for raising the relevant issues in such a clear way:

- he stressed the amount of diversity which we have in public expenditures in Australian notwithstanding our long history of fiscal equalisation, while Russell Mathews sought to show both that there may be less diversity, looked at in the proper light, than Ned Gramlich thought and that in any case it is only through effective fiscal equalisation that equality and diversity can be satisfactorily reconciled;

- Gramlich's querying of the efficiency costs (in terms of a distorted geographical distribution of activity) of equalising the tax prices (costs) of public services scored points in my book, notwithstanding the reservations expressed by Mathews; I agree with Gramlich that while we may choose to bear such costs on equality grounds we should nevertheless be clearly aware of them.

Despite Ned's doubts, I think that there is a useful sense, as John Nevile noted, in which the Commonwealth Grants Commission formula is in practice equalising. Nevertheless I found his alternative suggestions stimulating, but I think it rather implausible that our political institutions in Australia could be persuaded to adopt any of the approaches involving ratios of econometric estimates of various elasticities. One can imagine Mr Bjelke Petersen's comments on such proposals.

Gramlich touched upon tax matters - specifically taxing resources - and there is a territory problem to work out on that with the paper by Helliwell (who, in fact proposed in discussion what seemed a sensible division of labour). However this was the first session in which it became apparent to me that there is a major gap in the Survey at present in its leaving out any reasonably deep treatment of the overall tax structure in Australia and issues in, and options for, tax reform. Some of the issues were mentioned in discussion during this session. Others came up in the Aaron discussion - which I will cover under that heading.

(v)Krause

A central question which Krause raised is what explains why Australia's world trade involvement ratios declined over the last two decades (or, if you get away from the Korean war peak, were about static) while other advanced economies were becoming markedly more involved in world trade. Why did we "miss the bus" and - linking back to the Helliwell paper and on to that of Caves - so lose opportunities for growth in activity and living standards?

In fact these links among these three papers point up the rather narrow coverage of sectors of the economy (resource industries and manufacturing get most attention) in the Survey's treatment of Australia's economic development. Services (except for particular aspects of financial institutions), the public sector etc. are largely left out.

The other possibilities raised by Krause to answer the question may matter, but the main policy-relevant factor identified is of course our **protection** regime. It was disappointing then, as Max Corden said, that this draft did not cover the Australian debate on protection, and how (if at all) its importance has changed, in any depth. Larry Krause has promised to remedy this in the revision and I would urge that he also take up Corden's suggestion that - as well as making his case for a major one-hit protection cut - he give some coverage to the pros and cons of alternative methods of cutting protection ("top down" etc), not ignoring Neville Norman's point about the dilemma posed by the commitments given in respect of the "sectoral policy" protection arrangements. The IAC discussion papers and report on general reductions in protection are a basic source on all this.

As Fred Gruen has noted, one of the most interesting insights in the Krause paper is the suggestion that Australian may have an unexploited comparative advantage in "middle technology goods and specialised items". However, I think that there may be as much force in Helen Hughes' suggestion that there may be significant prospects for greater Australian involvement in trade in services. I think she was the first to note the tendency - more than a tendency - in the Survey to focus on goods production and trade relative to activity in services. The lack of coverage in the Survey of the vast structure of regulation which burdens the service sector most directly, and which may be as significant as protection is in its costs to our economic performance, is a reflection of this.

(vi) **Caves**

The Caves session was - I think it fair to say - not the most productive of well nailed-down new conclusions, although it was a fairly lively session.

My own reaction to the results of the quantitative work presented by Caves lies somewhere between those of Brian Johns and Adrian Pagan:

- a useful first step has been taken towards quantifying factors underlying differences in technical efficiency between Australia and the US, but the data limitations and econometric problems are severe, to the point that the research undertaken so far will not really support strong conclusions about explanatory factors - although our old friend protection is once again clearly implicated.

This lack of conclusiveness of the Caves study so far is a pity, because the differences in productivity which are the focus of the study are closely linked to the issue I have pointed to as arising out of other papers also, notably Helliwell and Krause, that the Survey needs more satisfactorily to pull together a diagnosis of our poor overall economic growth performance. In this context, the suggestions made to Caves (from Wolfgang Kasper, I recall) about looking at changes over time - and **dynamic** effects generally - are worth trying to pick up further in his revise, if only in a qualitative way.

Just to show that "soft" conclusions can still yield insights, the conclusion that Australian manufacturers seem to have found a "niche" in activities which are small-scale and not capital intensive is not entirely plausible to me, but does give food for thought.

(vii) **Mitchell**

The Mitchell paper is already, I think, the basis for one of the best chapters in the Survey volume. Although many speakers - more than could be accommodated - participated or wished to in this morning's excellent discussion of the paper, this was not a reflection of weaknesses in the paper giving rise to contention. Rather it reflected how well the paper identified and focused on the issues (as was acknowledged on all sides). From a macroeconomic viewpoint, the paper well complements Dornbusch and Fischer in canvassing the issues of

- wages and inflation and the effects of real wages on employment and unemployment, including the interaction of high real wages in the mid-1970s with the restrictive macroeconomic policy response to that;
- the possibility of an incomes policy in Australia and the role our institutions might play in one.

There was also a range of microeconomic labour market issues covered, including comparisons between centralised and atomistic wage setting schemes, and the nature and mechanism of **relative** wage rigidities in various settings ("comparative wage justice" being the name of the syndrome in our system). I think one of the more interesting issues among the speakers in the session attached to this point - is there a trade off between a better outcome on wage levels, on the one hand, and flexibility in the structure of relative wages (which Michael Porter was the first to stress, in the Dornbusch-Fischer session), on the other? Mitchell's suggestions about experimenting with such initiatives as gain sharing (to attempt to loosen up rigidities) seemed worthwhile to me. I do not think there is any necessary conflict in these suggestions with the desideratum of not making tax avoidance easier.

Mitchell's comments about the possibility of an incomes policy - and the role of the Arbitration Commission - complement well what Dornbusch and Fischer had to say on this in the macroeconomic context. However, I think all the discussion on tax-based incomes policies in this session was poorly focused and that Max Corden was right to bring in what seems to me to be the more relevant proposal at present, and more worthy of coverage, of **general** tax cuts in exchange for general wage restraint (in our present centralised system).

Other important points this session included:

- Russell Mathews' suggestions about the effects of taxes on wage claim behaviour (especially that of the personal income tax); and

- many other microeconomic issues, including about the appropriate aims and potential achievements of manpower programs

  - the merits of "queue shuffling" were nicely put by Michael Keating.

(viii) **Aaron**

The final session on Henry Aaron's excellent paper highlighted again what seems to me (as already noted) the major gap in the Survey's coverage - that is, the omission of a treatment of our overall tax structure and issues/options for reform, particularly as this matter is fairly high on the Australian policy consideration agenda at present. It was, in fact, clearly recognised in the discussion that it is difficult to talk about the re-distributive, equity, incentive etc. aspects of our social welfare system without discussing our tax structure in conjunction. If there is to be a fuller treatment of taxation in the Survey, I think this is the most appropriate chapter (even though business taxation does not fit well here), rather than, say, in the Gramlich chapter.

Henry Aaron's main thrust was that whatever other objectives we have for our social welfare system we must not lose sight of incentive effects. I think this was well recognised by the discussants:

- Phillipa Smith raised clearly (but did not resolve) the problems of combined marginal rates of withdrawal of tax and benefits. This was a point, however, on which Aaron made a most interesting observation - that to minimise **aggregate** disincentive effects it may be better to have short (or no) tapers of welfare benefits, rather than long ones extending far along the income distribution. This seems to go against the Australian conventional wisdom (consider the recently introduced Family Income Supplement), but strikes me as probably right.

His other interesting observation Fred Gruen has already referred to - that our tax and transfer system is most generous to rich and poor, and surprisingly, least generous to the middle class who comprise most of the voters. This needs to be looked at in more detail.

As the other points of that last discussion period will be fresh in people's minds I will mention only a few more key points which came out:

- that our hospital funding arrangements now embody relatively good incentives against over-use. Fred Gruen's comment that this "remains to be seen under Medicare" will I think apply more to medical services than to hospital services;
- that the future budgetary costs of our social welfare system, and their wider implications, need more prominence;
- that we still have a major "loophole" in our tax system in the treatment of superannuation, notwithstanding the phasing-in of new arrangements (over 40 years) which has recently begun. John Helliwell's remarks about the resemblance of the (ultimate) system to a direct expenditure

tax system were, however, a very interesting different view of this; and

- that there is an inconsistency in the unit we deal with between our tax and social welfare systems (Henry Aaron prefers the family as the unit).

Concluding Remarks

While I have mentioned a number of additional things which might be covered in the final volume, I realise I have suggested no deletions. As I am not aware that there are more chapters (or a second volume) planned, obviously these suggested additions will have to be succinct. Of course it may not be possible to adequately cover all of them in the space available except by reference to other sources. These matters are, of course, for the authors and editors to sort out.

It remains for me to express my admiration to those very gentlemen (and to Fred Gruen and his associates) for the excellent job done - I am sure that all of the Australians present have found the draft Survey papers and this conference very rewarding. We all look forward to the Survey volume itself.

CONTRIBUTIONS FROM THE FLOOR

Professor Wolfgang Kasper, University of NSW:

When overseas visitors ask me what differences characterise the Australian economy or economic culture, my reply is: its greater rigidity and lack of market competition. To illustrate what I mean, and why this may be relevant to a summary chapter, let me ask what do we want of a flexible market system? The market functions well if it basically fulfills three social requirements. First, it should give us cyclical stability, responsiveness to demand management policies, and good macroeconomic performance. Secondly, it changes the allocation when relative prices change. This contributes to economic growth. Thirdly, the invisible hand avoids visible conflicts. The competitive order avoids the concentration of economic and political power, as long as competition works well.

If we take that as a basis, Australia has not done too well. Its macroeconomic performance is locked into a fairly poor Phillips curve. Typically, when the rigid Australian economy was locked into a low Phillips curve in the 1950s to mid-1960s it looked quite good, it could not be easily pushed out of it because of the rigidities and that was a benefit. After the massive combination of shocks - undervaluation of the currency, oil shocks, Whitlam shocks etc. - we are now permanently locked into a pretty bad Phillips curve. Realisation that such rigidities exist can be tied in with our general unhappiness with some aspects of the Dornbusch paper. The crucial issue in Krause's draft Introduction, Australia's poor economic growth, can also be related to the problem of structural rigidity.

What is peculiar to Australia is the degree of visible lobbying, the sorting out of allocational issues by non-market forces (e.g. the Arbitration Commission); and frequently this does not work to our greatest benefit. Despite the espousal of egalitarianism, the powerful seem to be well ahead. To sum up, I see the issue of structural rigidity and lack of competitiveness at the base of a number of major problems. We have that rigidity because we do not use the market.

Mr Norman Fisher, Bureau of Labour Market Research:

I would like to echo a point made by Fred Gruen in his summary, and that is to encourage Professor Krause and his fellow authors to pick up the migration element, especially in the final chapter.

Although the migration aspect is commented on in a few papers - including Dan Mitchell's, it does strike me that it has been and continues to be one of the unique features of the Australian scene. Canada used also to be a major recipient (among Western countries) of immigration flows, but Australia is probably now the only western country where such flows have an important impact on the economy and its performance.

In this context I might also take up the discussion of protection and use of the phrase "protection friend". Many people have argued that immigration to Australia has been sustained because of the large intake of unskilled people; alternatively, it is argued that we have sustained our immigration in order to provide skilled cheap labour for industry.

I think some of the deficiencies with respect to youth as pointed out by Peter Karmel, also reflect inadequacies in our whole approach to education training. That is a slight gap in Dan Mitchell's paper. I suspect that in part our inadequacies in relation to training reflect the fact that for so long we have been able to coast on the investment in human capital made overseas by importing the products of overseas education and training systems. Similarly the investments gaps between housing and other forms of more productive activity in Australia in part reflect our long-term high levels of immigration. It has been argued before by policy makers in Canberra that the level of immigration has had a major impact on entrepreneurial expectations.

Without wanting to argue further, it does strike me that even if there is disagreement as to whether immigration is a unique characteristic of the Australian scene or whether it has a major impact on the economy, it would be useful to address the issue directly.

Professor Max Corden, ANU:

It is usual for Australian economists to focus on what is wrong with our economy - it always seems worse here than anywhere else, bearing in mind protection, over-regulation, real wage rigidity and so on. I would like to suggest some perspective, and put another side. In some respects, and taking a very broad vie, we actually do better than a number of other countries. I will put just two points.

Comparing ourselves principally with the United States and Britain, our governments (excluding the Whitlam period) are generally less extreme in the ideological swing from one direction to another. The Fraser government, in spite of the strong advice it received from senior Treasury officials and in spite of Fraser's own rhetoric, was in fact a very moderate conservative government - it was not a Thatcherite government. Now we have a new government and yet we do not have a big swing in policy; we have gone only from moderate right to moderate left (and possibly noteven that far). This is very different from the British atmosphere, and I feel, is also different from the big swings experienced in the United States - e.g. from Carter to Reagan. There seems to be less ideology in Australia than in a number of other countries; we live in a more pragmatic sort of country and, on balance, we are probably better off as a result.

My second point involves a comparison not with the US and Britain but with northern European countries which is perhaps a more relevant comparison. In some respects we do well in such a comparison. This is clearly not so with respect to industrial relations, where we obviously do worse. But there is the fact that we do not have the huge budget deficits, for example, of Sweden and Denmark; we do not have the - possibly excessive - levels of social welfare and expenditure commitments that a number of European countries have. We have gone their way but we have not gone that far. Hence I would like to reiterate the point: in some respects we have not done too badly.