Wool Again

John Hyde

Australians were once said to ride on the sheep's back. But ill-advised market intervention has now turned the great wool industry into a major economic headache for an economy that can ill afford one. Since the whole fiasco was made possible by its legislation, the Federal Government has a clear responsibility to all Australians to adopt the safest and cheapest possible route out of the mess.

The Australian Wool Reserve Price Scheme is a conventional buffer stock arrangement. It has now run into the difficulty which seems ultimately to be the downfall of all buffer stock schemes, namely, an intervention price that cannot be sustained. This results in mountains of the product, high holding costs and a shortage of credit. This fate was predictable—indeed it was widely predicted—although I, and I suspect others, have been surprised that so many years elapsed before it happened.

The Wool Corporation has destabilised the production of wool. Now there is at least 25% over-production caused by an artificially high price that is holding resources away from other activities—grains and meat production in particular. When the wool stock is sold we can expect a converse under-production. It no longer behaves wool growers to criticise industries such as motor cars.

It is sometimes suggested that the wool reserve price has increased growers' average returns. The scheme was, however, never designed to do that. All of the wool purchased has, until now, been resold. There is no reason to expect that the price gains when the wool was taken off the market were any greater than the price losses when the wool was fed back on. The Wool Corporation had, as it were, been gambling in a casino where the games were honest and the table's take was modest. However, like all chronic gamblers it eventually met a run of luck that absorbed its resources.

Both the Labor and Liberal governments, which encouraged this pointless gamble by an industry which is
as important to the economy as wool were irresponsible. As they did it against clear Treasury advice I believe that they were also reprehensible. It is, however, an act of exceptional cowardice for the industry politicians now to blame Mr Kerin for the unpalatable decisions.

Up until now, the reserve price and buffer stock have provided Australian growers with a more stable wool price. They have, however, confounded the price signals which should have been advising growers when to get in and out of those marginal 500 wethers or whatever.

I have taken some distance to criticise the reserve price scheme because, in deciding what to do now, it would be wrong to look for a temporary solution which would allow another stockpile to develop at a future time or which would continue even the day-to-day inefficiencies of the buffer stock.

There is now no easy escape from the situation the Wool Corporation and grower organisations have created. These are to lower the floor price, tax wool growers to maintain the floor price, and have the Government bail the industry out.

Lower the Floor Price

This is the least risky option. If it were adopted, the industry would go through some years of depressed prices as the stockpile is sold down, but that would be the end of the matter. The grower is saved the need to pay a 25% levy, but would still have to pay a sufficient levy to cover interest charges on the debt incurred in his name.

The lower price would signal growers to reduce production. It also would signal processors to increase consumption regaining for us some of the markets we have lost to foreign wools and synthetics.

The gradual release of the stockpiled wool would assist the balance of payments.

Tax Growers to maintain the Floor Price

This is a high risk option. So high risk, in fact, that no-one is proposing that the reserve should be maintained in real terms. It is anticipated that inflation, and it is hoped devaluation as well, will whittle away the real value of the reserve when expressed in the currencies that matter, such as the Yen and US dollar. Lowering the real reserve price only by this means saves face, but has no other virtue.

The Wool Corporation would be gambling that the market would turn around before it reached the point where growers would tolerate no more levies—say 50%. The wool tax would send a signal to growers to reduce
production, but an unclear signal. But the high
Australian reserve would continue to encourage processors
to substitute foreign wools and synthetics for sales we
might have made.

This option is somewhat less satisfactory than the
first from the point of view of the balance of payments.

The Government Bales the Industry Out

This is fine from the wool grower's point of view in
everything, but a moral sense. Growers would be
maintaining their incomes at the expense of taxpayers,
many of whom are less wealthy than they are. (I would not
enjoy taking the chaff from my shearmen on the subject!)

As the sole solution it should not be on. But the
government might agree to take over part of the interest
burden, if it could see permanent economic advantage in
doing so. It might, therefore, take over much of the
interest cost of existing stocks, if the reserve were
abolished or reduced to a level at which the Corporation
stopped buying.

If growers were to achieve this, they would have
done well out of taxpayers and far better than they are
likely to do out of maintaining the reserve---even if
that gamble were not to fail spectacularly. It should be
remembered that because of high interest rates a receipt
taken even a short way into the future is worth a great
deal less than one taken today. To cover interest alone a
price some 40% higher than the current price is needed to
justify holding anything for even two years.

Suffer stocks always fail in ways similar to the
wool industry debacle. They are the sort of schemes that
get otherwise strong nations into trouble.

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