

Economic activity can be viewed as long and short term trends---a jumbled sea of waves within waves.

Australians have been getting wealthier but at a slower rate than many other nations; the longest meaningful trend, or wave, I can identify is a slow relative decline of Australian living standards since the First World War. So far, from the wealthiest people on earth we have slipped to about sixteenth wealthiest. I don't know how long this trend will continue but if there is not an upward slope in the next twenty years or so my wave analogy might be the least important loss. This long swell is caused by fundamental changes to the productive part of the economy; our decline is caused by high levels of regulation, tariffs and labour market monopolies.

In the 1970s, by recourse to loose money management and deficit budgetting, we started another wave on a shorter cycle. Initially we were lifted on its crest but as we plunged from that the short wave reinforced the long.

In more or less the same cycle, in the 1980s, we started another even uglier wave. As if there were no tomorrow, we started borrowing abroad to support living standards depressed by the long trend. In 1984 and 1985 its crest too raised us up; we are still riding near the crest but the waters are combining to produce a most awful dumper.

The Australian dollar value of foreign borrowings was greatly increased by devaluation. Foreign debt is already equivalent to about \$6000 per man, woman and child and still accumulating. Three years ago the relative prices of our imports and exports deteriorated. To service the debts we now have no option but to accept a lower level of consumption.

Moody's and Standard and Poors apparently doubt that we will tighten our belts sufficiently soon enough; they have downgraded our credit rating. We are not yet an Argentina but clearly, for a while, until we catch up, living standards must decline a little---not just in relative terms this time, but absolutely.

I think these trends will be reversed; but must concede that there is nothing in the laws of nature that says they will. I base my hopes and expectations upon a new-found realism about industrial unions, tariffs, discriminatory government expenditure and taxation, and economic regulation. This dawning realism is our children's best hope and the last thing they need now is a mineral, wool and energy boom such as has in the past enabled us to delay facing facts.

Against the background of these major trends a short-run business cycle ebbs and flows. Just as a short steep chop has little effect on a big vessel but is thoroughly unpleasant in a

dinghy, this economic chop has little effect on a nation but it can swamp a business. It tends to preoccupy business management. Just as when you are in the water the closest wave obscures even the biggest on-coming waves, short run changes in economic activity tend to obscure more fundamental changes. Heaven help us if we forget that dumper.

1983/84 and 1984/85 were years of strong growth induced by strong government demand but they were not years when our commodities enjoyed international favour. Although domestic demand induced higher levels of business activity it also sucked in imports and raised costs which inhibited exports. When the current account and the dollar collapsed, domestic demand and growth were cut back in 1985-86. The economy seemed to be growing again by the December quarter of 1986. High interest rates restricting private demand were the principal instrument employed to reduce private domestic spending; government demand continued at record levels. Business activity declined while we waited on the so-called J curve to fix our balance of payments problem.

It would be extraordinary if the balance of trade had not responded to the devaluation; and it has. But gains made in the competitiveness of Australian production are being offset by wage rounds generally higher than those of our foreign competitors. While in the absence of offsetting cost increases a devaluation improves competitiveness it also increases the burden of debt service. Since costs are rising the J curve becomes just the trough and upward slope between two waves. How long is the cycle? What does the short term hold?

At the Economics Society meeting on February 13 twelve leading economists expected overseas economies to grow at about 2.5 - 3%. There will be major currency realignments involving risks for some Australian commodities. Wheat and sugar now seem to be a little better than was anticipated early in the year. For the rest of the year foreign demand will probably be ordinary but not awful. What happens after that will depend on what THE ECONOMIST called "the thundering charge of an approaching trade war". Australia could be trampled underfoot by the warring parties.

1987 is an election year; the government will try to delay anything too unpleasant. The economists expected our economic growth to be 2.5 or 3% in 1987---much less when adjusted for terms of trade.

During 1986 domestic demand was restrained except in the public sector which seems incapable of restraint. Net exports made a strong contribution to GDP growth. This trend must continue but reinforced with meaningful public sector restraint if we are to overcome our balance of payments problem. It is an election year; there will be more fiddles than real restraint.

Growth in 1987 will be concentrated in manufacturing production

but even so the growth will be only sufficient to take production back to the 1981 peak. Capital expenditure is expected to be better than last year but still insufficient to achieve vital structural adjustment. Real average earnings fell in the latter half of 1986 but the recent wage settlement will have reversed that trend driving labour costs up again.

This last point will be disputed. The conflicting figures employed by the ACTU and employers are better understood when the role played by government is added to the equation. Since the late seventies wages' share of gross domestic product has fallen from 62.8% to 60% and the share of company income after tax from 11% to 9.7%. Government's bigger share forced both down.

I don't think there will be a slump this year; I think the effect of the devaluation will be felt for a while yet; I think Mr Hawke will have time to get his election behind him.

I don't think we have reached the top of the shortest wave or the bottom of the longer waves but the longer and bigger waves are the ones that really matter. A smaller monthly balance of payment deficit is not a surplus. The foreign debt problem is still growing, if at a slower rate.