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A DEREGULATION LED RECOVERY

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The Treasurer and the Minister for Finance have each admitted our international debts are serious. But Government policy seems to be to ignore them in the hope that they will go away. I say `seems' because the Government is doing more than it talks about, but it could do more than it is to reduce the risk of really becoming a Banana Republic or going down the Argentina road. To do more it will have to be more frank about the problem.

There is a general hope in the community that the foreign-debt-to-GDP ratio will stop getting worse by about 1991. (The expectation was first enunciated by EPAC and `Stabilise' is the favoured euphemism.) However, all we have managed to do so far is to live a little less beyond our means. If the foreign debt should merely stabilise, say at 45% of GDP, the need to service it will continue gobbling up about 5% of each year's GDP and 40% of each year's exports. Unless it is greatly reduced the debt will be a menace the next time export prices turn sour.

Australians are thus hostages to fortune in a gamble with awesome stakes. I feel sure that a political party which undertook to improve the odds---and was credible---could count on support and votes for quite tough policies.

Debt is a potential election-loser, so the government blames bad luck rather than bad management for it, talks down the risk, and pussyfoots about with the most important policy changes. As so often happens, the sense of urgency and drama which would call forth public support for radical policy reform is lost. The Government is talking about many of the most desirable policies---tariff reduction, deregulation and privatisation---only in the context of economic growth and not in terms of our foreign debt. Real labour market reform is not on any Government agenda. The sense of urgency that Prime Minister Lange and Treasurer Douglas are able to call to the aid of good government in New Zealand is missing.

In Australia the Hawke Government was taking some steps in the right direction---budget deficit reduction and privatisation for instance---and talking about others, but progress is so slow that the debt problem is growing faster than the solution.

The first step on the way to the solution of any problem is to tell the truth about it. Political considerations encourage Ministers to fib a little, and ill-informed markets produce perverse results. Mr Keating should neither talk up the economy nor talk it down. Only with hindsight can he know whether under-confidence or over-confidence in the economy was the bigger problem anyway.

As I see it, the truth is: we are a First World country with a Third World problem. Lack of competitive edge, adverse balance of payments and debt are already serious and without luck will get worse. They are caused by bad public policy--- yet they can be cured. They cannot be fixed this year or next, but a full cure should take only about ten years if we apply ourselves diligently to achieving it. Our stark choice is to live poorer or produce more.

Most commentators are looking for a macro-economic policy to reduce immediate consumption and increase production. Possibilities are: reduce public sector borrowing, reduce public expenditure, change taxes to favour investment against consumption, reduce award wages and taxpayer-funded benefits, and employ tighter fiscal policy with looser monetary policy. They are all good, but the political will to implement them is in short supply.

EPAC wrote, 'The appropriate policy course in the short run involves continued restraint in fiscal settings together with moderation in labour cost growth....Longer term, the solution lies in a restructuring of the supply side of the economy and a lifting of Australia's productive capacity.' Clearly the longer-term solution is the more attractive and as it does not involve making most people poorer should be politically easier. What can the second 'solution' contribute to the short and medium term?

Since World War II many governments have successfully employed the second, supply side, approach, and some, including Thatcher's and Lange's, are using it now. Unlike the various macro policies, economists agree about the gains to be made from deregulation, privatisation and tariff reduction. Further, once the restructuring is done, its rewards compound so that small initial gains become large, without further political effort and cost. And while these policies initially improve the output of existing processes they change the nature of rewards and punishments to produce new processes. Unfortunately, micro policy does not lend itself to sweeping rhetoric but that shortcoming does not seem to have prevented either Thatcher or Lange from being re-elected.

With no change in aggregate consumption or in the terms of trade, a 5% improvement in output, above what is needed to keep pace with the rest of the world, would approximately balance the foreign account.

It is not hard to provide anecdotal evidence that the opportunities to improve productivity are big. Here are a few examples. The Bureau of Agriculture Economics say that the cost of grain handling could be almost halved by deregulation. Allowing foreign vessels to cart rock phosphate would reduce the cost of superphosphate by as much as the super bounty does. Robe River Iron doubled productivity in just a few months, by eliminating a few wasteful work practices. What could we expect to save by removing Telecom's and Australia Post's monopolies?

The Business Regulation Review Unit estimates that regulation costs Australians between 20% and 40% of GDP. The dead weight cost of protection is about a third of the direct cost. If the same proportion holds good for all regulation, universal deregulation would more than fix the foreign account. And that is only part of the story. Releasing the 'animal spirits' to make better widgets, instead of chasing political favours, will do more for the economy than the estimate above---even though economic modelers cannot say by how much. A deregulation-led recovery really beats telling people to reduce their living standards---ask David Lange or Margaret Thatcher.

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