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ON THE DRY SIDE \*\* THE ULTIMATE COST OF PROTECTION \*\* John Hyde

Alcoholics Anonymous know that the first step towards recovery, without which no other step will be taken, is admission that there is a problem. Goaded by gibes like Lee Kuan Yew's observation that Australians are becoming the poor white trash of Asia, and Professor Helen Hughes' prediction that our children will be taking table waiting jobs in Singapore, and by the low standing of our currency, most of us now admit that there is an economic problem. We did not always admit it: as recently as 1980 I waved well-sourced data describing Australia's poor economic growth in the face of a member of the Fraser Cabinet to be accused of exaggerating. That accusation would not be leveled today. The first step to recovery is taken.

Compared with, say Argentina, Australia is still strong. Our problem is caused neither by a deficiency of physical resources nor by the innate mental or moral deficiency of our people; nor although debt ratios and work habits must be changed need these yet be crippling. We employ our excellent human and physical resources badly in three principal ways. The government sector is too large, lacks economic discipline and is consequently inefficient. Our labour markets are dominated by powerful interests which prevent the efficient and full allocation of people to profitable jobs. Our industry is heavily protected from domestic and overseas competition, preventing the efficient and full allocation of people and capital and stifling entrepreneurship.

Most nations' economies are in varying degrees similarly afflicted. It is the high level of industry protection which makes Australia's case exceptional. It has been the clearing of protection 'log jams', or the absence of them, which has been central to every one of the post war economic success stories. Few Governments, in spite of talk by many, have done much to reduce budget expenditure and no government that I can think of has won a simple head-on law-backed-by-police confrontation with labour unions.

Although British Columbia and Sri Lanka are exceptions, few governments since the second world war have reduced nominal or even real public sector outlays. Those that have reduced public sector shares of GDP have done so only as GDP has grown, and the GDP growth has been achieved by competitive pricing in domestic and foreign markets, most notably through international trade, often following a SHARP reduction of the successful economies own trade barriers.

Because the production and job losses are passed to consuming industries, unions in protected industries don't suffer the consequences of their own actions. They are unlikely to show restraint unless their own industries (not just the individual firms) face competition from cost structures which are beyond the union's control. In practice, in Australia's case, that means international competition.

The easiest, surest and quickest way to reverse Australia's relative economic decline - about one place per year on the international wealth ladder - is to open our economy. Rapid reduction of trade barriers is the only common economic factor that I can find in the success stories of post war Japan, Federal Republic of Germany, South Korea, Taiwan, and Spain. The Original EEC six nations achieved spectacular growth when they opened themselves to each other's economies. Sweden, Malasia, Hong Kong, and Singapore were always open. Freer trade is common to the, not yet confirmed but promising, success stories of Sri Lanka, United Kingdom, Brazil, Hungary and the coastal cities of China. It is the central feature of David Lange's attempt to rescue New Zealand.

Professor Michael Levine, one time president of New York Air and at another head of the US Civil Aeronautics Board, said that an economy could have either stability or dynamism and he thought Australia had a lot of stability - a polite way of saying we were going nowhere. Bert Kelly argued for only gradual reduction of industry protection. Since there are once-off costs associated with the re-allocation of resources and these tend to be less when change is gradual, at the time he was right. But as the years have passed and the cumulative costs of not changing have mounted so have our opportunities passed. Now we must accept the discomfort of a more rapid adjustment than once would have sufficed, if we are to avoid the much greater discomfort of being irrelevant and insecure in a dynamic and dangerous world. And we must accept structural adjustment to avoid as much as possible of the social tension that seems to be the inevitable consequence of falling living standards. For fifteen years Australian consumption (living standards) has been artificially maintained by increasing foreign debt. Not only are we coming to the end of that penny section but it would be wise to repay some of the debt. Therefore some temporary decline in living standards, as we re-order our national finances, seems to me to be now inevitable; but the decline must be kept to a minimum. Running up further debt would merely delay and ultimately exacerbate the problem. If we are not successful, scenes like the ironworkers breaking down the doors of parliament house and the Victorian dairy farmers destroying goods in supermarkets will become common-place. I know it sounds alarmist to say so, but many other countries have not been able to confine tensions to such relatively harmless pastimes as breaking doors and jumping on cheeses and we cannot be sure that Australian common sense will always prevail. The fact that even the traditionally conservative farmers have taken to the streets is a straw in a wind that will become a howling gale if it is fanned by continuing poor economic management.

Protection is like borrowing in that it exchanges delay of one problem for a much worse problem in the future. We are starting to pay a heavy social price for an economy which lacks dynamism. To make our stable economy dynamic we should improve our labour markets and reduce the size of the public sector whenever opportunities present themselves, but the experience of other nations is that only by reducing protection is there a real probability of turning our economy around. The fall of our currency presents an ideal opportunity to reduce border protection (tariffs and import quotas) across the board without placing import competing industries in a worse competitive position than to which they are accustomed. The cuts should be bound in the General Agreement on Tariffs and Trade (GATT) to prevent reversal. Barriers to domestic trade like the Two Airline Agreement and Australia Post monopolies should be lowered as quickly as possible.

The social cost of trying to stand still in a changing world has become far greater than the cost of change and there is the near certainty that it will become much greater still.