

ON THE DRY SIDE 200 THE PREMIERS' PLAN John Hyde
Many commentators have said "Watch out; the world is again like 1929" - low commodity prices, excessive Third World debt, high public sector debts in the developed countries, increasing protectionism in the United States and stock market bouyancy. Others say that the world is through the bottom of this recession. Some of the latter are not so sure about Australia. They point to deep-seated structural problems which will deny us some of the benefit of world recovery.

The Australian Institute for Public Policy has commissioned Professor Schedvin, of Melbourne University, to compare and contrast then and now. It will publish him shortly.

Collectivists have told us that the Great Depression was "a crisis of Capitalism" so often that we have come to believe them. But was it? Economists do not agree what causes the ups and downs of business cycles. But if Marxists, who see depressions as episodes in the historically-ordained demise of Capitalism, are excluded, a consensus of a sort about what happened in the thirties can be stitched together.

The Austrian school has it: Governments had kept interest rates artificially low during much of the twenties; investments were made that could not service themselves at market rates and lenders would no longer oblige at regulated interest rates. There was a shake-out of the bad investments when real interest rates rose, and a shortage of loanable funds and new investment until they rose. There had been short-lived precedents in 1923 and 1911.

The Chicago school has it: a government agency, The Federal Reserve Board of the United States, caused a sharp monetary contraction between 1929 and 1933 by preventing the rescue of collapsing banks and refusing to buy bonds. This turned a common-or-garden recession into a full-blown depression.

The neo-classical school has it: The depression was prolonged in almost every Western Country by regulated prices and practices which prevented businesses and employees adjusting to deflation. This was particularly the case in labour markets: as prices fell those who had jobs found that their living standards rose but businesses collapsed and millions had no work.

The three positions are compatible and all three schools see the Great Depression as a crisis caused by governments interfering with capitalism. The depression was without doubt a crisis for capitalism but it was not a crisis inherent in capitalist system.

It was also a crisis for the Australian governments from which they were rescued by the 1931 Premiers' Plan.

I was recently given "The Battle of the Plans", by Shann and Copeland (Angus and Robertson 1931). It is an eighteen-page account of the events leading up to the Premiers' Plan backed by

157 pages of extracts from official and other documents. Its authors were the academic economists largely responsible for drafting the Plan. Published in 1931, the book is an attempt to set the record straight and encourage politicians to honour their promises. In 1986 it is food for thought.

The State Governments all, in varying degrees, had bankrupted themselves by excessive expenditure and irresponsible borrowing. The Premiers' Plan was the arrangement by which the States and Commonwealth defaulted on what they owed to domestic lenders. With the exception of a war debt payment to Britain Australian governments met their overseas obligations.

In May 1931 the Hon. F. W. Eggleston wrote to the Melbourne *Argus* in these terms: "Debt adjustment has been a feature of the law for several thousands of years. There is no process of bankruptcy applicable to state debt...not to recognise that [the need] has come to Australia at the present time is simply foolishness...It is true that we need not have got to this position. Four years ago I showed that Victoria was drifting at the rate of £2,000,000 a year but could not even get a report of my statement."

By the time the plan was adopted there was no doubt that the Australian Governments were bankrupt. During the Autumn of 1931 debate had been about whether default should be a surreptitious eroding of Australian bond-holders' capital by inflation or by more honest repudiation of the terms of loans. (Few Western Governments had such scruples by the 1970s.) It is difficult to see how inflation could have stimulated an Australian economy locked to the world by fixed exchange rates, and if the policy had precipitated further devaluation, foreign debt would have become an even greater burden than it was. Should we feel a small sense of *deja vu*?

Australians must have been aware that printing money had been tried on a grand scale by pre-Hitlerite Weimar Germany with disastrous consequences. It is now said to have been a prime reason for Hitler's rise to power.

Federal Treasurer E. G. Theodore's proposal for a fiduciary note issue (printing money) to pay the government's debts was abandoned after defeat in the Senate, and after the New South Wales State Savings Bank had closed its doors, causing people to question the wisdom of loading the banking system with even more government debt at a time when the governments were unable to service what they had already borrowed.

In 1931 the total revenue of the six State governments and the Commonwealth government was £168 million. Expenditure was £209 million. The deficit was £41 million or 24% of revenue. The Premiers' Plan called for reducing the deficit by £26.5 million or 16% of revenue---by modern standards not too bad an effort!

Apart from objections which were more rhetorical than substantial from Premier Lang of NSW, all governments of both

sides of politics agreed to the plan. Salaries and other adjustable expenditures, including pensions and benefits, were to be cut by 20% and interest payments by 22.5%.

The situation the Premiers faced by 1931 was considerably worse than today. It had not looked so bad in 1928 but with a prolonged stretch of adverse trading conditions the situation had deteriorated rapidly. With hindsight we know that the 1920s governments had been irresponsible. They incurred potentially disastrous debts to buy votes. It seems to me that the recent record of Australian governments is not appreciably better.