ON THE DRY SIDE

An evaluation of OECD cures for economic ills

*By JOHN HYDE**

IF soundings in my electorate are a fair sample of public opinion, unemployment is overtaking interest rates and taxation to become the foremost issue of political concern. It cannot be doubted that unemployment is a very serious economic and social ill.

A great deal is said about its consequences but much less about its root causes. It is indeed remarkable that there should be so little public debate (as opposed to mere breast-beating) about so obvious and so serious a problem which, one way or another, affects so many families.

While nearly all of the 24 OECD nations have experienced slow growth and rising unemployment, they have adopted differing economic strategies. Comparison might therefore throw light on the problem even if only to show us what not to do. One OECD nation, Switzerland, has an unemployment rate of only 0.4 per cent of the working population.

Switzerland's performance is particularly remarkable in the light of constant insistence by some that Australian, British and US unemployment is caused by monetarist policies, because Switzerland is one of the few places that I can think of that have actually practised anything close to Friedmanite monetarism for 10 consecutive years or more.

Several nations have practised monetarist policies for short periods and some, including Australia, have talked as if they were, but almost no-one has stuck to it.

Switzerland has, it is true, been able to export unemployment by sending guest workers home. On the other hand, Hong Kong, which has been more monetarist than most, has, during the same time, absorbed a vast and continuing flow of refugees — its population has doubled in about 26 years. Despite that and despite real uncertainties about its future, its unemployment rate is still between 3.5 and 4 per cent.

It is a fallacy to say that Governments can decrease aggregate unemployment by increasing aggregate demand. Unemployment tends to have risen particularly rapidly in some places which have attempted, in recent years, to stimulate their economies by increasing public sector expenditure or by adopting expansionary money supplies — note France and Canada. But it has also climbed rapidly in the UK which some say has adopted monetarist policies.

There is certainly no clear correlation between unemployment and monetary and fiscal policy adopted over the preceding two to three years. There may well be a high positive correlation between tight monetary policy and low unemployment over the long run but the sample is small. The point to be made is that, if there is a correlation, it is opposite to that often claimed by those who seek political milage out of accusing the Fraser Government of being monetarist (which it is not).

Economic theory suggests that unemployment will be associated with a rigid labour market, particularly where the price of employment (wages) is kept artificially higher than that at which each potential employee can find an employer who can sell the fruits of the employee's labour.

Artificially high prices resulting in market failure are most often brought about by monopolies. Trade-unions are monopolies which control the supply of labour dedicated to raising cost. We would therefore expect unemployment to be associated with a powerful union movement.

I know of no measure of union strength; nevertheless, the OECD nations again provide us with a helpful insight.

Japan twice suffered what became known as an "oil shock" — the first in 1973, the second in 1979. The prices of imported energy rose sharply at a time when the prices of Japan's exports did not, seriously prejudicing Japan's terms of trade.

After the first oil shock, real wage growth remained high and output was squeezed. In the second oil shock there was a dramatic drop in real wage growth for 1979/80 which, this time, made room for Japan's terms-of-trade loss, and this time output growth hardly dipped. On the second occasion the whole nation's lost earnings were shared reasonably evenly rather than being concentrated in unemployed workers and, since the productive process was not disrupted, losses were quickly made up. Japanese unions had learned from the past episode.

Sweden and Finland provide us with another example. To bridge the 1974/76 recession, Sweden employed expansionary policies which enabled real wages to go on expanding. Finland did not. At first the Swedes looked better but the advantage lasted little time at all so that since 1977, Finland has done far better.

The coincidence of general economic malaise, poor world commodity markets and the drought this year, have caused Australia to suffer a shock more serious than Japan's oil shocks. If real wages do not fall sufficiently to accommodate that shock, then circumstances will be hard on the many additional unemployed.

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