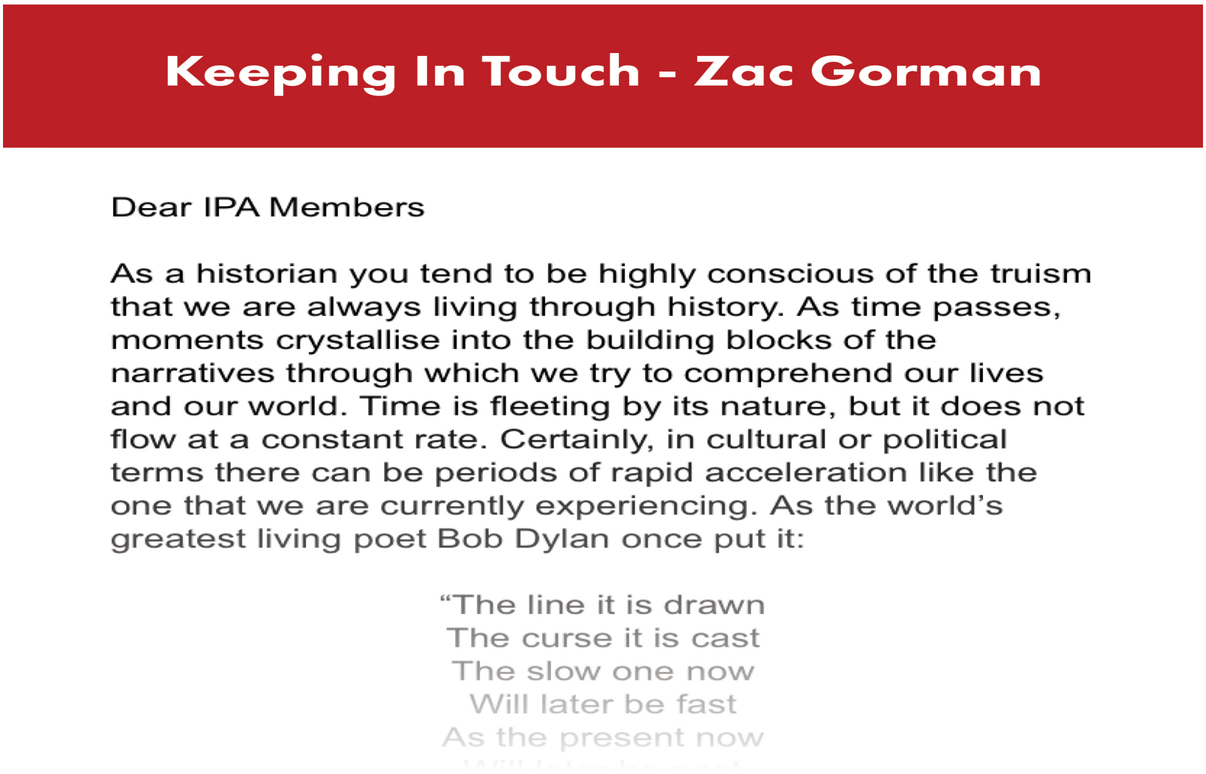

2020 In Historical Perspective – IPA Keeping In Touch – 9 April 2020

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Dear IPA Members

As a historian you tend to be highly conscious of the truism that we are always living through history. As time passes, moments crystallise into the building blocks of the narratives through which we try to comprehend our lives and our world. Time is fleeting by its nature, but it does not flow at a constant rate. Certainly, in cultural or political terms there can be periods of rapid acceleration like the one that we are currently experiencing. As the world's greatest living poet Bob Dylan once put it:
"The line it is drawn
The curse it is cast
The slow one now
Will later be fast
As the present now
Will later be past
The order is rapidly fadin'

And the first one now will later be last
For the times they are a-changin'"

In a period of such turmoil it is natural to reach out for precedents – events which, since they have already crystallised, seem to offer a comprehension unavailable in our flawed and limited understanding of the present. While the threat we currently face is certainly unique, it just so happens that Australian history offers two reasonably clear precedents which may yield some insights. Learning from these examples will help us chart a course back to prosperity and tackle the scourge of unemployment that is once again with us.

These precedents are the Spanish Flu epidemic of 1919 and the Great Depression beginning in 1929, two devastating events that our country handled so well that we were hailed internationally for it. Admittedly, the spread of aviation, let alone globalisation, means that a pandemic from a century ago was handled in a way that would be impossible to now replicate. Nevertheless, it still serves as an example of stoicism for us to follow, and it has even left us with some adorable May Gibbs illustrations of the gumnut babies wearing face-masks.

More directly relevant is our response to the Great Depression, which I have long maintained was one of our finest hours. It involved the conservative populism of the "All for Australia Leagues", one of only two Catholic Prime Ministers to have served on the centre-right, and the Premiers' Plan of hard-line debt repayment and fiscal restraint. The latter centred around a blanket 20% reduction in all adjustable government expenditure and won international praise as the "Australian Plan", a model to be studied on how to respond to financial crises. In the present circumstances the plan serves as a timely reminder of the need to spread the impact of an economic downturn across the breadth of society and ensure that any inflationary measures do not come at the cost of the integrity of the system.

Australia entered the Great Depression early and hard. At the start our governments' balance sheets carried vast public debt from the extensive infrastructure programs that had characterised a spendthrift 1920s. When international markets for agricultural produce began to fall, we struggled to find the money to service the loans which had overwhelmingly been raised on British capital markets. In an era when government borrowing was a far more direct process, this tied our hands.

There were those who wanted to experiment with inflationary policies, like ALP Federal Treasurer Ted Theodore (sometimes known as "Red Ted"), but even he was forced by circumstances to embrace strict fiscal conservatism. Cutting spending, reducing centrally fixed wages, and devaluing our currency against the pound sterling, were the only way the Commonwealth Bank (then the central bank) could guarantee that the government would still have money in the coffers to spend.

The policy was not without controversy. It would end up producing the third of the great Labor Party splits, first with Joseph Lyons and then with radical New South Wales Premier Jack Lang. Lang toyed with debt repudiation and was eventually dismissed by the Governor for instructing his public servants to wilfully evade federal law. On the other hand, the plan had the backing of influential local economists like Edward Shann in what was perhaps the golden era of the profession in Australia (my apologies to current IPA affiliates both internal and those working on blockchain).

The result was a spectacular success. Australia was "first in and first out" of the depression, according to contemporary Dean of Commerce at the University of Melbourne Douglas Copland. We were able to grow manufacturing to compensate for volatility in agricultural prices, and gradually lift consumer confidence by avoiding the devastating scenario of a loan default.

Sadly, few people know about this as Australia is a comparatively small country and America's more prominent "New Deal" became the influential blueprint for dealing with economic downturns. By the late 1960s this Keynesian orthodoxy had become so ingrained that even local economists began dismissing the positive view contemporaries had of the Premiers' Plan and complaining that short term unemployment was needlessly increased by the spending cuts.

Bizarrely, this transformation of viewpoint occurred despite Keynes himself praising the plan for having "saved the economic structure of Australia". He saw that devaluing the currency produced some of the positive effects he sought from inflation, while avoiding a default on the loans was so important to the public's perception that it had to be prioritised in any recovery effort.

There is an important lesson here about the central but nuanced role incentives and perception play in a healthy free enterprise system. The purported aim of Keynesian demand-side economics is to maintain consumer confidence and have interest rates and inflation set at such a level that they encourage people to spend. Bailouts and cash hand-outs are a more extreme version of this same premise.

The problem is that over time the system has become more used to these interventions so that they no longer have the positive effect that was once intended. As even Keynes recognised, sometimes it is necessary to "pay back the loan", i.e. to signal that the integrity of the whole system will be maintained no matter what the short-term cost.

As Australia's experience in the Great Depression showed, this can do more to produce long-term consumer confidence than ensuring people have money in their pockets in the short term. This is particularly the case when handing out money has damaged the incentive to save for a rainy day, and thus produced a cycle that encourages people to be dependent rather than independent and resilient. Critically, sound policies also give business the confidence to invest, the only sustainable source of wealth and jobs.

The current shutdown is government mandated, hence the state has a direct responsibility to help those affected in a manner that it otherwise would not. Nevertheless, if we want to protect the overall balance, to protect people's confidence in the integrity of the system, we should take a page from the Premiers' Plan and drastically reduce public sector spending so that relief measures like the "jobkeeper payment" produce as little debt and long term damage as possible. As Cian Hussey has warned , our credit rating is already under threat. That is why the IPA has been advocating reducing public service wages for all employees on greater than $150,000 by

20%. It would be a signal that we are all in this together, and that the money currently being spent by the government is real and not the product of dangerous inflationary printing.

I look forward to the day when this current crisis is relegated to history. The hope is that when things crystallise and we are able to produce a narrative of what has gone on that we are able to comprehend, we will not be trying to digest an event of the magnitude of the Great Depression. We are starting to see signs that we might avoid this pessimistic scenario. Thanks in part to the work of my colleagues the conversation is changing, and governments are realising that this lockdown cannot endure indefinitely. I eagerly await seeing you all out enjoying the free air of our great country once again.

Kind regards,

Zac