CONTENTS

Page
Inflation Again ........ 97
Business and Government .... 106
The Balance of Payments .... 111
The Wage-earner's Share of the National Income. Memorandum from Professor Prest ........ 119

COUNCIL OF THE INSTITUTE
G. J. COLES, C.B.E. (Chairman).
SIR W. MASSY-GREENE, K.C.M.G.
C. A. M. DERHAM, C.B.E., M.C.
G. H. GRIMWADE.
H. R. HARPER.
W. A. INCE.
F. E. LAMPE, M.B.E.
L. J. McCONNAN.
C. N. McKay.
W. L. Potter.
HERBERT TAYLOR.
HON. A. G. WARNER, M.L.C.

EDITORIAL COMMITTEE
G. H. GRIMWADE, M.A. (Cantab.), B.Sc. (Melb.), Chairman.
F. E. LAMPE, M.B.E.
HERBERT TAYLOR.
C. D. KEMP, B.Com. (Director of the Institute).
G. R. MOUNTAIN, M.A.
H. N. WARREN, B.Com., A.C.I.S. (Secretary).

INFLATION AGAIN

It is two years since this journal drew attention to the mounting dangers of the post-war inflation. Since then, in spite of unceasing discussion and a stream of articles by economists and leader writers, the monetary balloon has continued to expand and the value of the Australian £ has continued to contract. Since March 1948 retail prices have risen by 23%, wholesale prices by 30%, and the volume of liquid spending power, as measured by cash and bank deposits, by 28%. Moreover, the figures of recent months suggest that there is little hope of any immediate abatement of the vast inflationary movement taking place. The rate of increase in retail prices has eased off only very slightly while the volume of spending power, urged on by devaluation, has risen alarmingly by 15% since September, 1949.

If the dangers of inflation stood out so clearly two years ago, why has nothing been done in the interim to arrest the rise in prices and to stabilise the purchasing power of the £?

Perhaps it is not strictly correct to suggest that nothing at all has been done. The Commonwealth Government has continued to drain some of the excess money out of the economy by achieving a surplus of receipts from all
sources over its total expenditure. The Commonwealth Bank has exerted a tight control over the volume and direction of bank lending.* Price control remains over those items in palpably short supply. But the course of economic events over the last two years proves that these anti-inflationary measures have been woefully ineffectual in coping with the immense pressures making for expansion.

Some inflation, of course, was inevitable. No policy within the bounds of economic and political practicability would have been sufficient to stabilise the internal price and cost structure in face of the altogether extraordinary increases that have occurred in export prices and income. Two years ago it would have been hard to anticipate that wool which was then realising the very high price of 40d. per lb., would today be bringing 63d. per lb., and that wool receipts would have risen from £155m. in 1947/8 (which was a record), to £194m. in 1948/9 and to £286m. in 1949/50.

But even when this is said, and conceded, it remains true that there has been a serious failure to grapple strongly with the declining value of the £. It remains true that the two years 1948/9 and 1949/50 have been years little short of financial neglect and drift.

Why is this so? If the threat of inflation were already becoming ominous in June, 1948, why is it that so little effective action has been taken since that time?

The popular course is to blame the government, and no doubt if the rebound from the present inflationary boom should precipitate an economic collapse, the party then unfortunate enough to be in office (no matter whether it is primarily responsible or not) would receive the full weight of the electors’ wrath. But, in fact, the responsibility for the policy of financial timidity of the last two years is as much the public’s own as that of any political party. It is perfectly true that no section of the community has been backward in urging that value be restored to the £. But, when it has really come

* Despite the strict control over bank lending, bank advances have expanded by nearly £100m. in the last 12 months. But the Commonwealth Bank itself whose advances have risen from £56m. to £104m. has contributed as much to this as all trading banks together. There may be good reason for this large increase in the advances of the central bank, but at first sight it hardly seems to conform with the need for a policy of credit restriction.
to the point, no section has been prepared to do anything about it; no section has been prepared to make any worthwhile contribution to achieving the goal for which all have loudly clamoured. Most people have deplored the sliding value of the £, but they seem to have been singularly unaware that they have any responsibility themselves for arresting the slide.

"THE MONEY ILLUSION."

The main explanation of this is to be found in a deep-seated fact of economic psychology. While the average person has a great dislike of high prices, he has an even greater liking for a plentiful supply of money in his pockets. We all like our purses packed to capacity with notes, even if that involves, as involve it does, high prices for the things we purchase. "A 1,000 a year" has a magical ring; and the vast majority of people would much prefer to have a yearly income of £1,000 with high prices to one of £500 with low prices, even though the purchasing power of the larger income were no greater, and perhaps even somewhat less, than the smaller. Money for money's sake has an irresistible psychological attraction. It is pleasant to feel the notes crackling in one's pocket or to have a tightly-packed wallet, even though the notes may not be worth very much. Moreover, a high money income seems to confer a certain social prestige or economic status; when John Smith moves into the "£1,000 a year" class he begins to throw out his chest and feel his importance. There is, too, always the hope that if one can build up one's money income while the going is favourable, it will be possible to maintain the ground won when prices fall.

This fundamental fact of economic psychology, "the money illusion" as the late Lord Keynes called it, has been the root obstacle in the way of any effective action to stabilise the Australian £. Such action would inevitably have involved a lower level of money incomes all round than has in fact prevailed and would have certainly encountered bitter opposition. A government embarking on this course would have been taking its life in its hands, and as governments are only human, and naturally have to place the retention of office high on their list of objectives, little has been done. The limits of government action, it is well to remember, are set by public...
Inflation Again (continued)

opinion; and it has been public opinion, and not any political party, which has been largely responsible for the failure to cope with inflation over the last few years. Not by any means wholly responsible! For it can still be argued that governments should have done much more than they have done to educate the public in the perils of inflation, and should have tried to create that climate of opinion in which strong action would have been feasible without a political upheaval.

WHY ARREST INFLATION?

Apart from the extremely annoying fact that as the months have gone by the £ note has purchased less and less, there is, for instance, still a great deal of popular misunderstanding of why it is necessary to arrest inflation at all. After all, the post-war inflation has brought great advantages to many people. It has brought about the condition, highly satisfactory to the great majority of income-earners, of over-full employment. It has resulted in record returns for many farmers and has bestowed high money profits upon industrialists. It has enabled us to import on a grand scale at the same time as we have been building up our overseas financial reserves to exceptional heights. It has resulted in an exceedingly high tempo of economic activity within Australia, and has made possible an unheard of flow of migrants into the country without the political resistance which such a flow would, under other circumstances, have certainly encountered. It has encouraged the investment of large sums of money from abroad in Australian industries. And it has brought about a great increase in the money savings of the lower income groups of the community, as shown by money held in savings bank accounts and invested in insurance policies.

From a superficial viewpoint, then, inflation is by no means an unmitigated evil. Is it an evil at all? Yes, partly because it brings a prosperity which is as much imaginary as real. It increases the money incomes of all sections of the community but not the real incomes. To many, particularly to those sections who are politically unorganised, such as pensioners and some salary earners, it means lower real incomes, and economic hardship. It diverts production into the inessential channels and obstructs the great work of national development. It weakens incentive and tends to make able brains
concentrate on the easy gains to be had from capital inflation rather than on work of real national worth. And, of course, it produces the irritating and to some extent distressing phenomenon of a constantly falling value in the purchasing power of money.

"PUTTING VALUE BACK IN THE £"

It is at this last point that public criticism of the post-war inflation has been chiefly directed. The popular clamour to "put value back into the £" grows louder as the months go by. What does this mean when it is closely examined? It cannot surely mean restoring the value of the £, and thus prices, to pre-war levels. If it means that it makes nonsense. The pre-war level of prices has gone for good and all. In the last ten years the great world inflation brought about by the war has revolutionised the income and cost structures of all countries, and to adjust those structures so as to revert to pre-war standards would require monetary deflation on a scale impossible to contemplate.

A return to the pre-war purchasing value of the £ is therefore unthinkable. In fact it is even highly doubtful whether in the next 12 months it would be practical politics, or economics, to increase in any substantial measure the value of the £. The best that can probably be hoped for—and an objective which we would do very well to achieve—is that 12 months from now the value of the £ will not have deteriorated any further, and that the rising trend of prices experienced over the last decade will at long last have been arrested. All that the objective of "restoring value to the £" can mean from any realistic standpoint is that over the next 12 months the purchasing power of the £ will be stabilised around present levels. This is a realistic objective, but only just realistic. Failing an unexpected drop of substantial proportions in export prices, it could be accomplished only by the most stringent and positive measures of internal financial policy.

THE POLICY OF "DO NOTHING"

There are, thus, two ways in which we might hope to stabilise the value of the Australian £. First, there is the passive way of waiting till the reaction from the world post-
war boom forces a lower level of prices and costs within Australia. Second, we can take definitive action now by embarking on positive measures of economic and financial policy.

Is there, then, any likelihood of a large fall in overseas price levels in the immediate future? Very little likelihood, it would appear, within the next 12 months! All the present indications are that present price levels will hold fairly well for another year at least. Beyond that it would be foolish to say anything. We can of course wait until world prices for basic foodstuffs and raw materials adjust themselves to a new post-war level and until world currencies shake down at a new post-war set of relationships. That might take some years and it would certainly be putting value back into the £ with a vengeance. It would in all probability force a very sudden adjustment of Australian prices to the new world level of prices. The purchasing power of the £ would rapidly improve, but with drastic and painful effects on industries and individuals in the Australian community. It is unlikely anyhow that we will be able to avoid eventually some reduction of money incomes and costs within Australia as the world buyers’ market gathers strength, but this necessary adjustment will be the greater and the more painful the longer we delay in taking steps to arrest the rising price and cost drift, and the higher prices and costs in Australia are permitted to go.

Another two or three years of the present trends and the disparity at present appearing between our own costs and overseas costs might become of glaring proportions. An adjustment then could be accomplished only with severe hardships and unemployment on a considerable scale. That is why it would be most foolhardy to wait for a change in the economic weather overseas to bring an automatic end to inflation in Australia. That is why the stabilisation of the £ is not something we can or should postpone till next year or the year after, but something to be done right now. That is why the inflation problem is not an occasion for interesting or showy intellectual exercises but one of the most immediate and vital practical importance. For nothing will save Australia from the supreme tragedy of depression and unemployment if we allow the gap which is beginning to appear between our own
costs and overseas costs to widen until it becomes an unbridgeable chasm. No ingenious devices of financial or fiscal policy, or even large-scale spending on public projects, will then serve to save us from the unhappy and painful task of economic readjustment so that our economy can again proceed to operate on stable foundations.

TO PREVENT UNEMPLOYMENT.

Besides the threat to the future involved in the present inflation, the discomforts and irritations suffered by the Australian public from rising prices are of little importance. It is not so much for its own sake that we should take steps to put value back into the £, as for the sake of what will probably happen to us if we neglect to do so. The real argument for stabilising prices is not to add a little now to the real purchasing power of the weekly wage or salary, but to prevent unemployment later on—nothing more or less than that.

The next twelve months are likely to be critical. On present indications, export incomes may not increase greatly but will probably remain very high. They will in all probability be sufficient to maintain a high degree of activity internally with considerable pressure on prices and costs. At the same time wages and other incomes are almost certain to increase further. Apart from whether or not the wage claim before the Commonwealth Arbitration Court is successful, the quarterly adjustments still retain a strong momentum. Higher wages lead to higher salaries and other incomes by way of compensation. The immigration flow will buttress internal demand more than it will solve the problem of internal supply. The profit outlook is on the surface excellent and the volume of private investment will no doubt remain high. Moreover, with war gratuities amounting to £60m. falling due in the current year, and with government costs rising for other causes, Commonwealth finances, which have had an anti-inflationary bias over the last few years, are beginning to take on a flushed inflationary appearance.

It is now time therefore when a supreme effort should be made to grapple with the problem.

What can be done?
A MULTITUDE OF PROPOSALS.

A multitude of proposals have been put forward over the last few years. Many of these, such as a return to price control and subsidies and the restoration of the 44 hour week, are of academic interest only: They are outside the ambit of what is strictly practical. Others, concerned mainly with the expansion of internal production, while eminently good in themselves, will bear fruit only in the long term—they cannot be taken seriously as a solution of the immediate problem. In this category are incentive payments, profit-sharing, the elimination of Communist-inspired industrial unrest and increased mechanisation. We should push on with all these measures as fast as we can, but we should not regard them as a remedy for the short term issue of inflation. Something might be done to increase supplies by heavier imports of machinery and essential materials—steps are apparently already being taken by the Commonwealth Government to this end—but the short term remedies, must, of necessity, be mainly concerned with the monetary or demand side rather than the supply side of the economic equation; with reducing, or at least damming back, the monetary pressures on the price level. And, of course, it is here that the great obstacle of the “money illusion,” which has been fundamentally responsible for the failure of all previous attempts to deal with the problem, so strongly persists.

A NEW APPROACH.

Is it not possible to take a new approach—an approach that would enlist the combined goodwill and commonsense of all sections of the community? This might be achieved by the Commonwealth Government inviting all major organised sections to appoint representatives to a conference on inflation for the purpose of thrashing out immediate remedies. Representation at such a conference, in addition of course to the Commonwealth and State Governments, would embrace the manufacturers, commercial and other business sections, the primary producer bodies, the trade unions and banking and financial institutions. This conference would enable the Commonwealth Government to place its proposals for monetary stabilisation before the representatives of those people directly concerned, and the sacrifices which each section might legitim-
ately be expected to make for the ultimate good of all. It would provide the government with a unique opportunity for educating the community in the basic economics of the problem. It would open the way to that kind of national co-operation to reach a solution of a national issue, which is the real inner test of the strength of a democracy.

And apart from those advantages it has obvious political merits from the Government’s point of view. The great obstacle to stabilisation lies in the reluctance, and up to the present tacit refusal, of the representatives of any section to contemplate any measures which would involve some immediate sacrifice on the part of their members. If these sections of the community persisted in this attitude after the full facts of the situation were placed before them, the government would, in the eyes of the public, shift quite a large part of the blame from its own shoulders, and responsibility would fall where it rightly belongs.

THE LAST CHANCE.

The threat of inflation to the future stability of Australian economy presented in this article is no alarmist picture. Three years ago those who thought most deeply about the economic problems of this country were sufficiently concerned to emphasise the dangers inherent in a continuation of the inflationary trends. Since then the trends have continued and gathered force and the dangers have magnified and become more imminent. It is not too much to say that we are now presented with our last chance, and that if we fail to take it we may as well resign ourselves to the consequences—which will certainly be severe, and could be disastrous. This is a problem above politics, above sectional interests, above all narrow and short-sighted concerns. It is a problem which demands the united intelligence and sacrifice of all sections of the community if a solution is to be found.

NOTE:—
The above article was completed before the serious implications of the Korean War became fully apparent. At present it is impossible to tell what effect the Korean outbreak may have eventually on the world economic position and on the Australian economy in particular. While there will be greatly increased emphasis on defence expenditure, at the time of writing it appears that the economies of the countries of the western world will continue to be devoted substantially to peace production. The analysis and conclusions of this article, therefore, in our view, still hold good.
Constructive co-operation between business and government is as vital to economic welfare and progress as labour-management co-operation.

BUSINESS AND GOVERNMENT

Once upon a time—it seems a long while ago now—government and business had comparatively little to do with one another. Government was government and business was business, and the more government kept out of business and business out of government the better, it was thought, for everyone concerned.

They occupied and moved in two separate, almost water-tight compartments, and the points at which they touched were relatively few. The doctrine that as little government as possible was the best government possible held sway through general acceptance. It is true that in the comparatively early period of modern industrialism the state began to lay down minimum standards of protection for employees and investors. But apart from that and its participation in the great perennial issue of free trade versus protection, the role of government was, in the main, the negative one of keeping the ring as clear as possible of obstructions to the operation of free business enterprise. This general picture, with few modifications, prevailed up to the beginning of the first World War, and in the United States even for a decade after.

But all this was changed beyond recognition, first, by the Great Depression, and second, by World War II. Government from being a more or less interested observer, and occasionally an umpire, of the economic game, came right into the arena as an active and even controlling participant. Business and government were no longer separate entities moving independently in their own distinct fields of activity. Their concerns began to touch at many points, and they found themselves to be partners in a common enterprise devoted to the objective of economic welfare—although there soon sprang up violent disagreements between the partners on the way in which the enterprise should be run.

Profound Changes.

The Great Depression wrought profound changes in the thinking of the public and of economists on the responsibilities of government in the economic field. The classical idea that the automatic forces of the free market, so long as it were kept free, would ensure the maintenance of economic stability at high levels of employment in the economic environment of the post-war world was discredited. In the United States we had the New Deal, in Australia the famous Economists' or Premiers' Plan, and in all countries governments were forced by economic circumstance and the pressure of public opinion to interfere with normal economic processes in order to promote recovery and relieve distress. Out of the depression was born "the new economics" of which the late Lord Keynes was the most notable exponent in his great work "The General Theory of Employment, Interest and Money." The old classical conceptions, which had dominated economic thought for 150 years, were subjected to critical re-examination, and the idea that governments would have to take a larger, more positive role in the stabilisation of economic conditions and the pre-
vention of unemployment became widely accepted.

And following hard upon this revolution in thought and practice came World War II when the exigencies of total war forced governments to assume, temporarily, virtually total responsibility for the direction and management of the economic mechanism. The things produced, the prices charged, the distribution of incomes, the content of international trade, the pattern of employment, and the investment of savings, were no longer decided in the main through the normal more-or-less automatic processes of the free price market, but by conscious government direction and regulation. And even after the storm tides of war had receded, government had to continue in control to clean up the vast confusion of economic flotsam and jetsam that remained, so that business enterprise could operate again with reasonable effectiveness to supply the peace-time needs of the people.

Soon there arose a violent debate on the period during which the government should remain in control in this “clearing up” operation; and allied with this was the larger question of the extent to which government should, as a permanent thing, assume responsibility for economic processes. The controversy still rages; the issue is not yet finally determined, and may not be for a long time to come.

**Employment and Distribution.**

Two important points on the relation of government to business have, however, been removed from the field of dispute. The first is that the level of economic activity and of employment can no longer be left to the automatic dispensations of the free price market; in all countries and by all shades of political belief these great questions are regarded, at least partly, as matters of government responsibility and determination through the weapons of banking and credit policy, exchange rates, budgetary finance, and public works and spending. The second is that government must assume some responsibility for ensuring that all members of the community are provided with a decent minimum of food, clothing, shelter, education and health.

These questions, as we have just indicated, are beyond party division or any serious difference of public opinion. Thus in a broadcast before the last general elections in Britain, the great Conservative leader, Mr. Churchill, said:

> “The scheme of society for which Conservatives stand is the establishment and maintenance of a basic standard of life and labour below which a man or a woman, however old or weak, shall not be allowed to fall. The food they receive, the prices they have to pay for basic necessities, the homes they live in, their employment must be the first care of the state, and must have priority over all other peace-time needs.” Also: “All parties are agreed that the prevention of unemployment ranks next to food in the duties of any government.”

**Size of Government.**

Whatever may be the future area of government responsibility—we have always urged the minimum consistent with the objectives just mentioned—in the two great matters of total employment and the provision of a basic standard of living for all, the position and role of government are now established by an almost universal consensus of opinion. This development has naturally led to a remarkable expansion in the size of government and to an entirely new set of relationships with the everyday business life of the community. Its magnitude can be illustrated by one or two simple figures. In 1939 there were 42,000 administrative public servants in the employ of government and local government bodies in
Australia; in 1950 there were 117,000.* In 1938/9 all government revenue from taxes amounted to £125m. or £18 per head of population; and in 1948/9 revenue from taxes totalled £527m. or £68 per head of population. In ten years we have seen what almost amounts to an administrative revolution in the economic functions of government and in its relations to the business community.

Difficulties and Misunderstandings.

It is hardly to be expected that this revolution would have occurred without difficulties and misunderstandings, often amounting to antagonism, in the attitude of government to business and of business to government. Many hard things have been said on both sides. On the one hand business has, almost overnight, had many of its old-time freedoms restricted and found itself subjected to a degree of interference and direction naturally difficult to stomach. Controls and regulations, the meaning and purpose of which it does not always easily comprehend, have invaded it from every quarter. Where formerly the businessman could retain the greater part of his hard-earned profit, he now finds he must pay back the greater part to the government. Where formerly he could buy where and what he wanted, he now frequently finds he must obtain a government licence. Where formerly he could borrow money for whatever purpose he wished, he now finds that he is restricted to those purposes laid down by the Commonwealth Bank. It is hardly to be wondered at that some businessmen have come to regard government as, at best, an unmitigated nuisance, and at worst as an enemy; and government servants as an unnecessary and unproductive encumbrance on the back of the community.

On the other hand, it is scarcely surprising that government officials, armed with new and unheard of authority, should at times have exercised their new powers in an undiscriminating and unsympathetic fashion. Nor is it surprising that in a world-wide movement toward the assumption of great responsibilities by government for full employment, social security and economic stability, that the servants of government should sometimes tend to overlook the importance of the practical knowledge of the businessman and to under-estimate the cardinal significance of the business function.

It is not, of course, suggested that these attitudes of mind are universal, or even general. There are many government officials who recognise fully the significance of the business function and who are invariably sympathetic and understanding in their dealings with businessmen. Equally, there are many businessmen who have a wise comprehension of the need for a broader scope of government direction and activity than that which existed in 1939, and who are helpful and co-operative in their transactions with government officials.

Mutual Indispensability.

It is, however, still true that there is much antagonism, much suspicion and resentment, in the general relationships of business to government. In the mixed economy of the modern world, both government and business must eventually come to recognise the indispensability of one to the other. If business is to yield its best fruits, it needs strong and wise government and the economic stability which such government can provide. If government is to achieve its great objectives of full employment and rising standards of economic security and living for all, it needs virile, confident and efficient businesses. In the Keynesian doctrine businessmen's expectations on the future level of profits are just as important to the maintenance of full employment as

high levels of government spending. Governments which go out of their way to engender business confidence have therefore a much better prospect of fulfilling these objectives than hostile or indifferent governments possessed of even the most sweeping economic powers. It is worth remembering that the failure of "pump priming" government expenditure in the early stages of the American New Deal was primarily due to lack of business confidence in the administration at that time.

Constructive co-operation between business and government is just as vital to economic welfare and progress as the much more frequently discussed need for co-operation between management and workers. Without bold and enterprising business, government cannot hope to realise its central aims of full employment, maximum production and economic security. And, on the other hand, unless government is successful in its central aim of preventing large-scale unemployment, business will suffer the losses and bankruptcies which follow inevitably from economic instability.

When the truth that business needs government as much as government needs business is firmly ingrained in the minds of both parties, the antagonisms will dwindle and the foundations will be established for a really constructive and positive era in government-business relations. It will need an effort of mind and will on both sides.

The Public Interest and Private Interest.

One of the causes of the trouble lies in the tendency of government to identify itself with the public interest and to identify business with the narrower motive of private interest. To this it may be said that those who are usually the most ardent advocates of the public interest have as a rule no private interests to tempt them to stray from the path of virtue. It is not difficult to remain pure and undefiled so long as you are able to stand aloof from, or refuse to enter, the hard competitive field on which the game is played out. Government should therefore be very careful not to assume an attitude of moral superiority over business, an attitude which was too much in evidence during the war. It should bear in mind that the function of government is to protect and advance the public interest, and that the performance of that function merely means that it is carrying out its duty and does not entitle it to any assumption of moral superiority. The public official should remember that, if the positions were reversed, he would in all probability find it much more difficult to take the lofty, disinterested stand. It is true that in the long run the interests of business in general are coterminous with the interests of the community in general; but that does not always apply to individual businesses in the short run and the businessman on occasions finds himself confronted with a conflict of loyalties not easy to resolve.

Sectionalism.

Another point at which the government official needs to move warily is in the allegiance he gives to any political party or doctrine. In an age when socialism has become a leading political force, a doctrine that on the face of it would lead to increased prestige and responsibilities for those in the employ of government, it is not surprising that some government officials appear to associate their own interests with the advance of socialism. It would, however, be an evil day for Australia if this tendency should become pronounced. In that case public administration would inevitably become tainted with sectionalism, and public servants would, in practice, conceive their function as one of service not to the whole public but to a particular section of it. Not that public servants can help having political convictions and ideals, but they should remember their unique position and more
than any other section of the community strive to see the elemental political truth
that "conservatives and radicals represent the two sides of the human head. Both defend a truth which is not all the truth." Whatever their natural political inclinations they should be unceasingly alert to keep them apart from their everyday responsibilities.

Need for Consistency.

A further point by way of illustration: One has only to have dealings with government departments, particularly on matters of high policy, to realise the over-suspicious attitude which government officials sometimes display in their dealings with business. There are occasions when the businessman's recommendations tend to be handled as gingerly as if they were loaded with high explosive. If public officials can bring themselves to give the businessman credit for some degree of sincerity and some practical understanding of economic issues a great advance will be possible.

The Attitude of Business.

But the fault is not entirely on the side of the government official. There is room, too, for improvement in the attitude of the businessman. Some businessmen tend to be too sweeping and general in the criticisms they level at government regulation. All forms of government "interference" are to these critics necessarily bad; they conveniently overlook the benefits which large sections of business receive from government by way of tariffs and subsidies, or through an ordered system of wage payments made possible by government-provided machinery for the regulation of industrial relations. They condemn all government control over business as an encroachment on freedom of enterprise, but they are not slow to solicit the assistance of government departments where they feel the laws of competition are operating rather too harshly for their peace of mind.

There is a great deal of inconsistency in the attitude of business to government. While it should always hold itself free to criticise those government policies or actions which it considers detrimental to the public welfare, it should strive to be more selective in its criticism and support those extensions of government activity which are clearly beneficial. It is altogether desirable that business should exert a strong influence on government policy which affects it, but this purpose is hindered rather than advanced by the tendency to indulge in undiscriminating indictments of all forms of government control.

Business should not precipitately condemn what it dislikes on an incomplete cursory examination of the issues, for what business dislikes may not seldom be in its own long-term interests, if it only knew it. Before businessmen give voice to their opinions on complex public questions, they should pay those questions the compliment of sincere and serious study. It does not by any means always follow that because a man has proved his genius in the promotion or the management of large-scale business enterprises, that he is well qualified to pronounce on the virtues or defects of government policies. Let him be as vigorous and outspoken as he wishes once he has grasped the problems at issue, but he should make it his business first of all to obtain a proper comprehension of what is at stake.

* * * *

The mixed economy, in which a large degree of government control is associated with a much larger degree of private business enterprise is likely to be with us for a very long time to come. It is time both business and government started to give some hard thought on how to obtain the best results from the mixture.
Australia's reserves of sterling and foreign currencies are at present in excess of £500 millions, but they are little more than what is needed to pay for one year's imports at present prices.

THE BALANCE OF PAYMENTS

The overseas balance of payments is possibly the most revealing, although not the most fundamental, of all the indicators of economic health and prosperity. It is here that underlying internal weaknesses and instabilities eventually manifest themselves most clearly. This is especially true of those countries in which international trade comprises a large proportion of all trading activities. For instance the final test of the success or failure of Britain's dramatic struggle for economic survival is whether she can balance her overseas accounts by achieving a sufficient volume of exports to pay for the food and raw materials essential to her existence. The attention of governments and economists in Britain has been, therefore, over the last few years, unremittingly focussed on her balance of payments, and particularly on her balance with the dollar countries.

But overseas trade also looms very large in the Australian economic picture, and the trend in the Australian balance of payments should be a matter of live interest and concern to business and trade unions as well as to governments. Relative to its population Australia is a large exporter and importer, selling very big quantities of a very small number of products and purchasing a wide range of raw materials, finished goods and capital equipment needed for home industry and for direct consumption by the people.

THE BALANCE OF PAYMENTS—WHAT IT IS

The balance of overseas payments is the surplus or deficit remaining after our overseas expenditure on imports and other items have been balanced against our overseas receipts from exports and other sources. Imports and exports are by far the largest entries in our overseas accounts; the difference between them is known as the balance of trade, as distinct from the balance of payments which covers all receipts and expenditure from overseas transactions—not merely those arising from exports and imports.
In addition to paying for our imports, we have to pay interest on the Australian national debt held abroad, dividends on overseas capital invested in this country, and for such services as shipping and insurance; and in addition to overseas receipts for our exports, we receive funds by way of new capital invested by overseas people in Australia, the expenditure of overseas tourists in this country, and from other sources. When receipts from all sources exceed expenditure the result is reflected in an increase in our overseas funds (these are held almost solely in London and are popularly known as London Funds) which are held mainly by the Commonwealth Bank.*

Exports are the means by which we pay for our imports. Prosperous times in Australia have usually been associated with a high level of exports, which have meant that we have ample funds to finance the volume of imports necessary to our industrial development and a rising standard of living. On the other hand when exports have been low we have usually been forced by one means or another to contract our imports with unhappy effects on expansion and standards of living within Australia. The classic means of reducing imports, where there has been a decline in exports, is by internal deflation which has reduced spending power in Australia—and thus expenditure on imports—and which has in the past been accompanied by unemployment.

RECENT MOVEMENTS

A comparison of trade figures for the financial year, 1948-9 with 1949-50 reveals that whereas imports have increased by £122m., exports have increased only by £74m., a rise of £87m. in wool exports covering declines in other exports. (Exports of wheat and flour have fallen by £10m.). As a consequence of these changes our favourable balance of trade (not payments) for the twelve months dropped from £127m. to £79m.

* The way in which exports increase our overseas funds is as follows:—

The Australian exporter who sells say £100 of goods in the United Kingdom receives in exchange £100 in sterling. As he wants his profit in Australian money, he exchanges this claim on sterling for £125 Australian. The bank which conducts the transaction credits his account with £125 Australian and in return receives the £100 sterling which it holds in London as an addition to its London sterling funds. In this way the transaction both increases deposits and spending power within Australia and also increases the sterling funds held in London by the banking system. The reverse process operates in the case of imports. Australian trade with all foreign countries is mainly financed through London. Transactions may be negotiated in sterling, or in the currency of the countries concerned. In the latter case, surplus holdings—e.g. French francs, may be sold for sterling, or conversely where holdings are inadequate, e.g. American dollars, they are allocated to us under the Dollar Pool arrangement and paid for in sterling.
Whilst the deficit with U.S.A. and Canada was reduced from £12m. to £6m., a favourable balance of trade with the United Kingdom of £20m. has been turned into a deficit of £40m. Our overall favourable balance is being maintained by heavy sales of wheat to India and the Far East, and of wool to the continent of Europe, particularly France and Belgium and to Russia and Japan. Should for any reason these exports fall off in the near future, then the balance of trade would most certainly turn against us.

In addition to this volume of overseas trading, sums of money must constantly be transferred between Australia and other countries in payment for services rendered (or received)—for tourist expenditure, freight and insurance on imports, the transfer of dividends, interest on public loans raised abroad in earlier years and the like. The gross total of these payments and receipts reaches large figures but official estimates are given only on a net basis; the final balance which had to be paid by Australia on account of all these items in 1948-9 was about £80 million. This payment was in addition to that required to meet the cost of actual goods imported amounting to £415 million. As the total value of our exports reached approximately £548 million, Australia had a surplus of a little under £50 million in the 1948-9 financial year.

This surplus comes to us in the form of additional reserves of sterling—or other foreign currencies—and was partly responsible for the rise in the grand total of these reserves from £A274 millions in June, 1948, to £A452 millions in June, 1949. The remainder of the increase presumably arose from a substantial inflow of private capital into Australia from abroad; from the pre-payment for some goods exported from Australia; and from delays in the payment by us for quite a range of commodities purchased from abroad. A large addition to overseas currency reserves of this kind exerts a strong inflationary effect inside Australia for it represents the acquisition of a substantial volume of money by Australians unaccompanied by any corresponding inflow of goods.

AN UNFAVOURABLE BALANCE?

On the basis of this year’s figures it appears that we will have an unfavourable balance of payments on current account for the first time since the abnormal conditions of World War II. Total exports for the year have attained the record level of £615m., but imports also reached an all-time high
with £536m. The net payment to be made by Australia on account of all the "invisible" items will probably rise to £90m. because of higher costs and prices. This would mean that Australia would have to meet a total expenditure on current account of £626m. with a total income from exports amounting to £615m. If these figures prove to be reasonably accurate, there will be a deficit of about £10m. to be met from our reserves of sterling and foreign currencies. Our reserves would continue to rise, however, if there is a continuance of capital inflow, from investment.

This position is no cause for alarm; it would be wrong to think that we can or should achieve a surplus on our current overseas payments at the end of every twelve months. But there is need for caution. The export industries are on the whole not well equipped to expand production to meet any decline in prices, particularly wool prices. Because of public works programmes we have heavy commitments for imports, and we will still need large quantities of rubber, cotton and motor vehicles, petrol, tobacco, and other products essential to the Australian economy.

HIGH STERLING RESERVES A DELUSION?

By editorial comment and as a result of expressions of opinion by public men from time to time, the press has given considerable prominence to the size of Australia's reserves of sterling and foreign currencies, which at present stand in excess of £500 millions. Often this figure is compared with the pre-war average level of around £60 millions and, perhaps naturally enough, it is concluded that the increase which has taken place means that our position is now secure beyond possible doubt.

This is a mistaken view.

It needs to be remembered that in the pre-war years we were importing at the rate of only a little over £100 millions a year, whereas today goods are flowing in at a rate exceeding £500 millions a year; also the pre-war level of our sterling reserves was uncomfortably low for they were not sufficient even to meet the costs of one year's imports. But today the position is not greatly different for these reserves are still not much above the total value of one year's imports. Because of dollar restrictions imports of some items, particularly cotton and newsprint, are lower than last year, but, great increases
have taken place in imports of other raw materials such as steel and coal, machinery and in everything associated with motor transport—motor vehicles, petrol and rubber tyres. Imports of tobacco and tea and cocoa are also on the upgrade with the result—indicated above—that the 1949-50 trade year will almost certainly see the elimination of the surplus on account of current transactions. Incidentally, it is a thousand pities that overseas funds are now being adversely affected by the importation of large supplies of coal and steel when such vital commodities could and should be produced at home in adequate quantities. Imports of iron and steel have risen from £10m. in the twelve months ended June, 1949 to £25m. for the twelve months ended June, 1950.

A most important aspect of the whole balance of payments position is that at present our sterling reserves are being considerably augmented by large transfers of private capital into Australia, associated both with British monetary investment here and with the stream of immigrants entering the country. These cannot be expected to continue on the present scale; in fact a change in Australia’s economic circumstances might put in process an embarassing movement in the opposite direction. The terms of trade which have tended in favour of Australia over the post-war years must now be expected to move against us. A recession in Australia, brought about by a decline in export income following a fall in overseas prices, would probably reduce inflows of capital from investors and immigrants, just as in the early 1930’s. Considerable sums of “hot money” which were transferred here in expectation of an appreciation of the exchange rate, as means of obtaining “easy profits” for speculators, would no doubt be repatriated. It is difficult to estimate the effects of these influences on the Australian balance of payments position, but the last report of the Commonwealth Bank indicated that overseas reserves might easily be reduced by £100 million by the resumption of normal arrangements for the payment for exports and imports.

**IF EXPORT INCOME SHOULD DECLINE**

And apart altogether from the unfavourable reactions on our overseas reserves of these indirect influences, what would be the direct effects on the balance of payments should export prices, and therefore export income, decline? Exports
of wool, wheat and flour for the financial year ending June, 1950, totalling £410m. are nearly twice the value for the same period in 1947-8. Prices in 1947-8 were high and so were export volumes. It is not being needlessly alarmist to say that £100m. could be clipped from our export income in the not far distant future as the result of quite a moderate decline in export prices. Failing a similar decline in import prices some adjustment to our import programme and other overseas expenditure would almost certainly become necessary, for our London Funds could not continue for long to support an unfavourable balance of payments.

Of course, imports can always be reduced (at the cost of a temporary reduction in real living standards) and if the internal deflationary process which would accompany such a reduction in export income were allowed to run its course, no doubt they would be reduced following curtailment of the purchasing power of the people. But if, as would seem more likely, internal purchasing power were artificially supported, the demand for imports might remain high, throwing additional strain upon the balance of payments. It has been suggested in the White Paper on Full Employment that a situation of this kind might be met by straight-out quantitative restriction of imports. Apart from whether action of this nature would be consistent with our obligations under the post-war trading agreements, it would almost certainly invite reprisals from other countries, which would lead to a vicious spiral of contracting demand.

The next question is how far and in what manner is Australia dependent upon imports at present?

Table II printed at the end of this article clearly indicates that over the last twenty years the composition of imports has changed; materials and capital equipment for use by domestic industry have come to occupy, relatively, a much more important place while the importance of consumers' goods has steadily decreased. And, lest anyone think that the Australian economy has become more independent of the production of other overseas countries, the proportion of imports to national income has risen steeply from 14% in 1938-9 to over 21% last financial year. It was 18% in 1928-9. Table I reveals at least one important fact; that the burden of overseas interest payments on our balance of payments is now almost
insignificant as compared with what it was in 1928-9, or even ten years ago.

Gathering together this evidence, the general conclusion emerges that any marked impairment of our financial capacity to pay for imports would be under today's conditions more than usually hurtful to the nation. A forced curtailment of imports on any scale would threaten the ability of Australian secondary industry to maintain production even at present levels and would undoubtedly end (for a time) possibilities of industrial expansion at anything like the rate experienced over recent years. It could react severely upon industrial employment and would place a most awkward obstacle in the way of the national immigration policy. And, though there would be no embarrassment as a result of the annual interest bill payable by Australia on account of government and other public authority loans raised abroad in earlier years, this problem, which caused such heartaches and bitter recriminations in the days of the last depression, might very well be replaced by another.

The new problem would be a dilemma associated with the effort to provide—in circumstances of a marked decline in our export income—domestic employment which would require, of course, that the people's purchasing power should not be allowed to fall, or at least not allowed to fall far. Any such action would keep up the demand for imports so, maybe, the interesting position will one day be reached where domestic credit expansion will replace overseas interest payments as the "villain of the piece" in any balance of payments difficulty which might confront this country.

Table I.

<table>
<thead>
<tr>
<th>COMPOSITION OF AUSTRALIA'S OVERSEAS EXPENDITURE</th>
<th>1928-9</th>
<th>1938-9</th>
<th>1948-9</th>
</tr>
</thead>
<tbody>
<tr>
<td>Imports</td>
<td>%</td>
<td>%</td>
<td>%</td>
</tr>
<tr>
<td>Freight and Insurance</td>
<td>69</td>
<td>61</td>
<td>79</td>
</tr>
<tr>
<td>Interest on Public Debt</td>
<td>9</td>
<td>9</td>
<td>8</td>
</tr>
<tr>
<td>Public Expenditure</td>
<td>15</td>
<td>15</td>
<td>4</td>
</tr>
<tr>
<td>Net Company Dividends</td>
<td>1</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td>Net Expenditure—tourists, migrants, and other services</td>
<td>4</td>
<td>8</td>
<td>4</td>
</tr>
<tr>
<td></td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

Table II.

COMPOSITION OF AUSTRALIA'S IMPORTS.

<table>
<thead>
<tr>
<th></th>
<th>1928-9</th>
<th>1938-9</th>
<th>1948-9</th>
</tr>
</thead>
<tbody>
<tr>
<td>Producers' Materials</td>
<td>45.5%</td>
<td>44.1%</td>
<td>43.6%</td>
</tr>
<tr>
<td>Capital Equipment*</td>
<td>23.4</td>
<td>27.4</td>
<td>29.5</td>
</tr>
<tr>
<td>Consumers' Goods</td>
<td>24.1</td>
<td>19.8</td>
<td>17.4</td>
</tr>
<tr>
<td>Fuels and Lubricants</td>
<td>6.7</td>
<td>7.8</td>
<td>8.8</td>
</tr>
<tr>
<td>Munitions and War Stores</td>
<td>.3</td>
<td>.9</td>
<td>.7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>100.0%</td>
<td>100.0%</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

* Includes small item classified in Official Statistics as "Auxiliary Aids to Production."


Table III.

EXPORTS OF AUSTRALIAN MERCHANDISE—PRINCIPAL COMMODITIES.

Australian Currency F.O.B. Prices.

<table>
<thead>
<tr>
<th></th>
<th>1928-9</th>
<th>1938-9</th>
<th>1948-9(a)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>£ mil.</td>
<td>£ mil.</td>
<td>£ mil.</td>
</tr>
<tr>
<td>Wool</td>
<td>61.6</td>
<td>42.7</td>
<td>231.7</td>
</tr>
<tr>
<td>Wheat and Flour</td>
<td>26.3</td>
<td>13.3</td>
<td>98.2</td>
</tr>
<tr>
<td>Butter</td>
<td>7.2</td>
<td>12.9</td>
<td>23.8</td>
</tr>
<tr>
<td>Sugar</td>
<td>2.4</td>
<td>4.2</td>
<td>13.3</td>
</tr>
<tr>
<td>Meats</td>
<td>6.3</td>
<td>11.8</td>
<td>29.8</td>
</tr>
<tr>
<td>Hides and Skins</td>
<td>9.3</td>
<td>4.1</td>
<td>12.2</td>
</tr>
<tr>
<td>Lead</td>
<td>3.2</td>
<td>4.3</td>
<td>22.1</td>
</tr>
<tr>
<td>Dried Fruits</td>
<td>2.3</td>
<td>2.9</td>
<td>3.4</td>
</tr>
<tr>
<td>Fresh Fruits</td>
<td>0.9</td>
<td>2.0</td>
<td>3.1</td>
</tr>
<tr>
<td>All Other</td>
<td>19.1</td>
<td>24.3</td>
<td>105.0</td>
</tr>
<tr>
<td><strong>Total Exports</strong> (excluding Gold)</td>
<td>138.6</td>
<td>122.5</td>
<td>542.6</td>
</tr>
</tbody>
</table>

(a) Subject to revision.


Table IV.

RATIO OF IMPORTS AND EXPORTS TO NATIONAL INCOME OF BRITISH COMMONWEALTH COUNTRIES AND THE UNITED STATES OF AMERICA, 1929 and 1948.

<table>
<thead>
<tr>
<th></th>
<th>Imports 1929</th>
<th>Imports 1948</th>
<th>Exports 1929</th>
<th>Exports 1948</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>18%</td>
<td>21%</td>
<td>13%</td>
<td>28%</td>
</tr>
<tr>
<td>New Zealand</td>
<td>22%</td>
<td>28%</td>
<td>33%</td>
<td>35%</td>
</tr>
<tr>
<td>Canada</td>
<td>28%</td>
<td>21%</td>
<td>25%</td>
<td>25%</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>29%</td>
<td>22%</td>
<td>20%</td>
<td>17%</td>
</tr>
<tr>
<td>United States</td>
<td>5%</td>
<td>3%</td>
<td>6%</td>
<td>6%</td>
</tr>
</tbody>
</table>

Source: United Nations Department of Economic Affairs, Division of Economic Stability and Development.
THE WAGE-EARNERS SHARE OF THE NATIONAL INCOME

Memorandum from Professor Prest.

In the March/April number of "Review" we published an article on the changes that have taken place in the distribution of the national income since before the war. The article deplored the shortcomings in the statistical data on this important subject, which is so vital to the taking of wise decisions on economic, social and industrial policy. Many questions which are at present the subject of a great deal of dispute, and which give rise to industrial unrest, would be resolved if adequate official information on the distribution of the proceeds of industry were available.

We have now received a memorandum from Professor Wilfred Prest, Professor of Economics at the University of Melbourne, which throws further light on the deficiencies and the misleading nature of statistical information relating to this important matter. We are pleased to have the opportunity of publishing Professor Prest's interesting memorandum in "Review."

Considerable attention has recently been given both in the Press and in the Arbitration Court to the concept of the share of National Income that is—or should be—paid in wages and salaries. This concept has also been used in the "Review" of the Institute of Public Affairs (Victoria) to measure the change in the wage-earners' standard of living.

Much confusion surrounds this concept and the uses to which it is put. The confusion is partly due to the failure of the Australian National Income statistics to show wages and salaries separately, so that the £1,055m. paid as "wages and salaries" in 1948/49 included, on the one hand, the earnings of juniors, women and unskilled workers and, on the other, the salaries of company executives, public servants and members of Parliament. These diverse recipients do not constitute a homogeneous class of "labourers," with a common social background and common economic interests. The I.P.A. article referred to above recognised this defect in the statistics but it is frequently forgotten or ignored.

The next largest item in personal income is designated in the National Income accounts—"Profits from Unincorporated Businesses." It comprises the incomes of farmers, shopkeepers, doctors and others who are in business either as partners or sole traders. A little reflection, however, suggests that a substantial part of these so-called "profits" could be quite appropriately regarded as wages or salaries in respect of the labour which the proprietors devote to their businesses. On this reckoning the share of National Income paid in wages and salaries would be much larger than that shown in the National Income accounts. Furthermore, the variations in the latter which the statistics reveal between different dates and between different countries can often be ascribed to variations in the extent to which people prefer to work for themselves or to take paid employment.

Still more confusion surrounds the remaining items of personal income. There seems to be a widespread assumption that rents, interest and dividends are paid to some persons other than the wage and
salary earners or the owners of unincorporated businesses. The existence of such a class of “rentiers” or “capitalists” has been taken for granted since the days of Ricardo and Marx. In present-day Australia there are no doubt some elderly retired persons, and some widows and spinsters, living exclusively or mainly on income from property; but they cannot be a very numerous group.

The whole question of “who owns Australia” is one which deserves a good deal more objective research than it has hitherto received. It seems probable, however, that today most property is held either by institutions or, as a supplementary source of income, by persons who are mainly dependent on current earnings—whether in the form of wages, salaries or profits from unincorporated businesses.

Apart from institutional holdings, the ownership of shares in joint stock companies and of Government bonds is probably largely confined to salaried workers and the owners of unincorporated businesses. However, of the various forms of property income shown in the 1938-9 White Paper on National Income, company dividends accounted for only £39m., and interest payments for only £42m., against £73m. in respect of rents (including the rental value of owner-occupied dwellings). Whatever may be the case in respect of the ownership of company shares and government bonds, there is no doubt that the wage-earner has a substantial share in home ownership. Indeed, the Census shows that about half of the householders in Australia own, or are in process of purchasing, their own homes.

Furthermore, much of the property held by institutions is in the hands of savings banks, insurance companies, friendly societies, pension or superannuation funds and trade unions. These are all institutions in which the wage earner has a large stake, so that many wage earners who hold no property personally, nevertheless do so collectively through the social institutions of which they are members.

It is not suggested that there are no considerable inequalities in the ownership of property in our present society. But it is urged (a) that the idea of an entirely “propertyless proletariat” is a dangerous myth, and (b) that property income is comparatively insignificant, being generally supplementary to some other source of income. The real importance of personal property lies in the opportunities which it provides for its owner to engage in lucrative and influential activity, the remuneration from which may, however, take the form of a “salary.”

Hence it is difficult to see what significance can be attached to the “share of National Income paid in wages and salaries.” It indicates what part of national income is paid in a particular form, not what part is paid to a particular class. For the latter purpose it would be more appropriate to consider what part of national income is paid to a particular income group, say the group with less than £12 per week; alternatively, one might consider how the average income of the lower half of the income recipients has changed compared with that of the upper half.

Unfortunately, the latest available figures of income distribution relate to 1945/6 and while they distinguish between incomes before and after tax, they do not distinguish between the incomes of women and juniors and those of adult males, nor between the incomes of employed persons and those of persons in business on their own account and they make no allowance for the cash value of social services. More elaborate and up-to-date information on income distribution is an urgent prerequisite for the intelligent discussion of, and the formulation of policy on all economic and social questions.