No Time To Increase Taxes

STATEMENTS by the Prime Minister and the Federal Treasurer have made it clear that the forthcoming Budget will aim at restraining the inflationary forces at present at work in the economy. This objective would be supported by at least 90% of the community.

Confidence in the budget as a decisive weapon of economic control has, however, rather waned as a result of experience in recent years. The old idea—and one still held in some quarters—was that the budget could be used as a powerful instrument to beat back inflation by drawing off purchasing power from the community. This was to be achieved by the expedient of a "budget surplus". The government would simply ensure that its total receipts from all sources—mainly taxes and public loans—would exceed its total expenditure. The "surplus", which would represent a deduction from the purchasing power available to the community and thus from total demand, would somehow be "frozen away" and not permitted to return to circulation. For various reasons this is technically anything but easy to do, but, apart from that, the demands on the public purse in the expansionary economies of the post-war world are so urgent and insistent, that a government finds it almost impossible to resist them. In the present-day economic environment, the pressures for increased government expenditure are proving to be virtually irresistible.
This is especially true in the economic and political setting of Australia today. On the one hand, the rapid pace of development gives rise to well-nigh unlimited demands for government spending on community needs, all of which are regarded by their advocates as “essential”. On the other, there is the special political problem which arises in a federal system where the states are reliant on the central government for the bulk of the moneys they require to meet their own expenditures. In Australia the States have to bear a main part of the burdens of development. It is not surprising that they are forever on the Commonwealth doorstep clamouring for more money to spend on the lagging services for which they are responsible. In this situation a budget surplus becomes little more than a pious aspiration.

The Prime Minister no doubt had these difficulties well in mind when he announced last February that the Government must do everything in its power to avoid deficit finance and that this would be the greatest task of the 1960 Budget. He went on to say that this task (i.e. the avoidance of deficit finance) would be anything but easy. In other words, what the Prime Minister seemed to have in mind was that the Budget should aim at avoiding pouring additional fuel on the fires of inflation by resorting to Treasury Bill finance. No mention was made in the Prime Minister’s statement of a budget surplus. This might be taken to imply that the best the Budget could do was to avoid giving further encouragement to inflation; it could not hope to be, in a real and positive sense, disinflationary.

It would be a grave error, however, to jump to the conclusion that a budget which achieves a balance between receipts and outgoings, is, necessarily, non-inflationary. Everything depends on how the balance is achieved.

As soon as any serious inflationary tendencies appear in the economy, there is a school of thought which immediately proposes increased taxation as a “remedy”. This is what happened, most notably, in 1956, when eight leading University economists urged the Commonwealth Government to raise taxes to realise an additional £100 million a year. The view that increased taxes exert a disinflationary influence, however, is now being vigorously disputed. This challenge
to traditional thinking is of particular significance at the moment. Preparations for the 1960 Budget must at present be well under way and there is little doubt that the Government will be urged by some to impose increased taxes as part of the resistance to the rising trend of costs and prices. This view should be rejected.

It can be stated categorically that if the forthcoming Budget provides for increased taxation, the net impact will be inflationary. And this applies no matter whether the Budget were balanced or even whether a theoretical surplus were achieved. The one thing the next Budget should avoid doing, if it is not to give a further stimulus to inflation, is to raise taxes.

The idea that increased taxation is necessarily anti-inflationary is based on a peculiarly static view of the economic process. It assumes that if the government imposes higher rates of taxation or additional (new) taxes, the extra revenue represents money extracted from the community and to that extent the community's spending is reduced. But this approach ignores entirely the dynamics of the matter—it ignores entirely how the community is likely to react to the additional taxation which it now finds itself compelled to pay. The community does not submit passively to higher taxation. It finds the increased taxes irksome, and the natural irritation which it feels is translated into a desire to do something about it. In one way or another the different sections of the community eventually take action to counter the effects of the increased taxes on their own pockets. And this activity inevitably gives rise to inflationary consequences.

Let us suppose that the increased taxation takes the form of higher rates of personal income taxation, designed, in the main, to reduce consumer expenditure. The wage or salary-earner finds his pay packet lighter; the private businessman his profits lowered; the professional man his income reduced. They do not take this "lying down". They seek round for ways to circumvent the impact of the higher taxes on their incomes. In the case of the wage and salary-earner this will soon result in a "build-up" of pressure for higher-wages-or
salaries; the professional man may decide to raise the scale of his fees or charges; the businessman will endeavour where possible to lift his prices so as to maintain his profits intact.

Nor would these consequences be avoided if the increased taxation took the form of higher indirect taxes on items of consumer expenditure. Apart from the undesirable direct effect of such taxes in raising prices, the higher living costs will give rise to a similar series of consequences as the various sections of the community adjust themselves to the new situation and endeavour to maintain their real incomes intact.

On the other hand, if company tax is increased, the tendency of companies will be to treat the additional tax as a cost and raise their selling prices in order to maintain their profits. For instance, companies engaged in constructional work, which look for a given profit on jobs they quote for, will almost certainly raise their quotes to cover the additional tax. If the jobs are government jobs, the practice will increase the cost of capital projects and involve governments in additional expenditure.

One of the great laws of economics which Keynes propounded—but which has somehow been mislaid by many of his followers—is that people develop an habitual standard of life which they do not willingly or easily relinquish and which they strive to maintain. Keynes never forgot—indeed how could he—that the primary raw material of economics, in its practical sense, consists of human beings and that natural human reactions to given measures of policy could be ignored only at the possible cost of rendering the measures abortive. With too many economists today economics has become a kind of exercise in simple mathematics, of addition and subtraction, so that if you subtract so much from this form of expenditure and add it on to that, total expenditure is unaltered and balance is maintained. This ignores human reactions to the measures undertaken and makes of economics a far simpler thing than in fact it is.

Keynes applied his concept of an “habitual standard of life” to his analysis of the effect of a change in income upon the spending and saving of the income recipient. He argued
that, faced with a reduction in income, a man would tend to reduce his savings rather than his customary expenditure on consumption. This is not without relevance to the problem we are considering.

An increase in taxes designed to reduce expenditure on consumption will be nullified, at least in part, by the fact that people will call upon their savings in order to maintain their spending on their everyday needs. Increased taxation will thus mean a reduction in voluntary savings.

It might be argued that while increased taxation would have little or no effect on spending for consumption, the drawing down of savings will mean that less money will be available for private investment. As a consequence investment expenditure will be reduced and this will have at least some deflationary effect. But, in an environment of full employment and rapid economic development and expansion of markets, it is hardly likely that businessmen will submit tamely to this situation. They will strive to obtain their funds from other sources, by additional borrowing or, if that is denied to them, by competing for some of the savings going into government and semi-government investment; or by raising prices to provide additional finance from their own earnings. All these responses would intensify inflationary pressures—the first and third obviously, the second, by forcing the government to seek other avenues of finance to maintain its own expenditure.

Advocates of increased taxes could profitably study an important article in the April number of “Lloyd’s Bank Review”. Writing on British budgetary prospects over the next five years, the author, Mr. F. A. Cockfield, makes the following comments: “There was at one time a tendency to regard balancing the national accounts as essentially a matter of book-keeping: if the four main components in national expenditure—namely consumers’ expenditure, capital expenditure, government expenditure and the foreign balance—appeared likely to exceed the national income which would be generated at stable prices, all it was necessary to do was to increase taxes. Usually the chosen victim was the consumer.
The consumer, however, proved to be singularly unco-operative and unwilling to toe the line if he could find any avenue of escape. The degree of inflation we saw between 1945 and 1952 was in no small measure a reflection of the excessive level of taxation during those years."

And again: "If the level of government expenditure is too high it is useless trying to balance the economy simply by increasing the taxes on the private sector. To do so leads to further inflation as both the consumer and industry seek to find means of countering the effects of the increased taxes. One grave danger of raising taxes in an attempt to damp down an excessive upsurge is that later on, when the danger is over and taxes could and should be reduced, there emerge all sorts of other claimants on the Budget surplus. If the surplus is allowed to be absorbed in increased government expenditure, the final result is an ever-increasing level of taxation exerting a continuous inflationary effect."

Mr. Cockfield has had a close working experience of the matters of which he writes. He served with the British Treasury, being Director of Statistics and Intelligence on the Board of Inland Revenue from 1945 to 1952. In 1951 and 1952 he was a Commissioner of Inland Revenue.

* * *

If the 1960 Budget is to avoid giving a further stimulus to the chronic inflationary movement which has plagued the economy since the war, it must at all costs refrain from increasing taxation.

This may require some change in the approach and philosophy of the budget-makers. Too often in recent years—and this applies not only to Australia—the starting point seems to have been from the side of expenditure. Governments decide what they want to spend, or what they consider they must spend, and then proceed to impose the necessary taxes which (in conjunction with the moneys they expect to obtain from borrowing) will provide the finance to cover their outlays.

This time, could not the start be made from the revenue side? In other words the Government should assess what
revenues it can expect to obtain without imposing new taxes, or raising rates of existing taxes, and adjust the total of its expenditure accordingly. This is, of course, no more than the approach the wise individual applies to his own finance and the Government might well follow suit.

If the Government is to play its part in preventing, or at least curbing, the apparently inevitable inflationary drift, then the great need is for it to limit its own spending. Higher taxes under present conditions must inevitably mean more inflation.

The Prime Minister recognized this need when in his address at the Melbourne session of the International Congress of Scientific Management in February last he said:—

"The first task is to slow down the massive upward movement of Government expenditure, which in the case of the Commonwealth, has been rising at the rate of something like £100 million a year."

---

**Mr. Harry Hey**

The I.P.A. records with deep regret the death of Mr. Harry Hey on 11th April, 1960. Mr. Hey had been a member of the Institute's Council since 1951.

Mr. Hey was a distinguished metallurgist. His technical knowledge and experience contributed greatly to the mining and metal industries of Australia. At the time of his death, he was Chairman and Managing Director of Electrolytic Zinc Co. of Australasia Ltd. and a director of I.C.I. of Australia and New Zealand Ltd., Associated Pulp & Paper Mills Ltd. and other companies.

Mr. Hey had a deep understanding of human relations gained from a life-time spent in mining and metal extraction.

He will be greatly missed by his wide circle of friends in business, by the employees of the Electrolytic Zinc Co. and, not least, by the Council and staff of the I.P.A.
The I.P.A. has just published a new illustrated booklet. It deals in a simple and popular way with the pressing subject of inflation.

The booklet discusses:
- Why inflation is bad for Australia.
- How it unfairly penalises certain sections of the community.
- Who is to blame.
- How rising costs affect Australia's export industries, hindering our efforts to compete in world market.
- Why it is vitally important to increase our efficiency and productivity.
- Why it is everybody's business to fight inflation.

The I.P.A. is inviting companies and other organisations in all states of Australia to purchase copies of the booklet, for wide distribution among their employees and associates, at 1/6 per copy:

20 copies £1 10 0
50 copies 3 15 0
100 copies 7 10 0
500 copies £37 10 0
1000 copies 75 0 0

Copies of the booklet will be sent on request—free of charge—to schools and other educational institutions.

Some of the interesting facts brought out by the booklet are the following:

The Australian £. is now worth 6/8 or one-third of its pre-war value. This decline in purchasing power of our currency compares unfavourably with many other countries, viz.:—
Purchasing Power

Today as a % of Pre-war

<table>
<thead>
<tr>
<th>Currency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Swiss franc</td>
<td>55%</td>
</tr>
<tr>
<td>The German mark</td>
<td>52%</td>
</tr>
<tr>
<td>The U.S. dollar</td>
<td>49%</td>
</tr>
<tr>
<td>The N.Z. £.</td>
<td>42%</td>
</tr>
<tr>
<td>The British £.</td>
<td>37%</td>
</tr>
<tr>
<td>The Australian £</td>
<td>33-1/3%</td>
</tr>
</tbody>
</table>

The booklet shows that because of the rise in prices during the last decade, all goods and services sold in 1958/59 cost the community £3,500 million more than they would have had prices remained stable.

A chart shows in graphic form who received the extra money resulting from higher prices:—

- 46% went to wages and salaries.
- 20% went to farmers, professions, small business and property owners.
- 12% went in indirect taxes.
- 12% went to company profits and depreciation.
- 10% went in higher import prices.

Production is vital in keeping down the cost of living. More production means lower costs, cheaper goods and increased prosperity. To beat inflation wages and other incomes must not rise more rapidly than production.

The Australian standard of living and future development depend on increased exports. Inflation is the arch-enemy of the exporter because high costs make it difficult for him to compete in world markets.

The battle against inflation is a job for everybody. Management and employees must strive unceasingly for higher productivity. It is the duty of governments to keep their spending down to what the community can afford.

If taxes are too high the incentive to produce is weakened, savings are discouraged and inflation is encouraged.

Governments must guard against the temptation of trying to make the economy do more than our available resources will permit.
Manufactured Exports

The fact that 200 of the leading financial and industrial figures in Australia saw fit to take the best part of a week off from their everyday tasks to attend the recent National Export Convention at Canberra, underlines, as nothing else could, the paramount importance of exports to the economy. The Convention, organised by the Export Development Council, was possibly unique in Australian economic history.

The simple truth—and the raison d’etre of the Convention—is that the continuance of large-scale development, along with the maintenance of living standards, will depend entirely on our ability to achieve a rapid increase in export income. The 1960 decade will provide the test. The magnitude of the task, now generally accepted, is that an increase of at least £250 million a year in export income (some would say a very much higher figure) will be necessary by 1965. That this represents a rise of 30% or more over present export levels highlights the enormity of the problem. Of course, a big and fortuitous and sustained lift in the price of wool would overcome all difficulties, but this is something we could hardly count upon. Unless this increase can be achieved, the rate of development will almost certainly have to be substantially reduced.

The air of the conference was, naturally enough, thick with suggestions as to how exports might be increased but, generally, they all boiled down to two—hard, very hard, selling abroad and hard, very hard, endeavour at home to raise efficiency and lower costs.

The Export Development Council has warned that we can no longer rely on the primary industries to the extent that we have done in the past, and greatly increased attention will have to be devoted to the export of manufactured and semi-manufactured products. Whether the Australian economy is sufficiently tough to achieve a reasonably rapid and reasonably substantial increase in exports of manufactured goods, only time will show. But we are up against some pretty hard and experienced competitors whose economies impose sterner conditions on management, labour and governments than do our easier-going arrangements in Australia.
It may be that success in the drive for exports will eventually be achieved not mainly in the field of highly fabricated manufactures but in that of basic metals and materials such as copper, iron ore, coal and alumina. Nevertheless, the full weight of our national ingenuity and competence must be applied to the effort to secure increased outlets abroad for the products of the expanding manufacturing industries.

It is four years since the Minister for Trade, Mr. McEwen, impressed upon manufacturers that they must develop an export consciousness and earn exchange if their growing requirements for imported materials and capital goods were to be adequately met.

In these years the Commonwealth Government has pursued a vigorous campaign of export promotion. The Trade Commissioner Service has been extended; a number of special trade missions have been sent abroad; and an export guarantee insurance scheme has been established.

What success has been achieved by the drive to expand markets for the products of secondary industry? How large a contribution is manufacturing now making towards the earning of export income?

Various answers have been given to these questions, depending on the definition of manufactured exports adopted. On the reasoning that every item which at some stage passes through a factory is manufactured, it can be shown that factory products constitute nearly 40% of all exports. Other commentators, applying a narrower classification of manufactured exports used by the Commonwealth Statistician, dismiss as relatively unimportant the contribution of the manufacturing industries to overseas earnings. (This classification does not include processed primary products such as flour, butter and canned fruits in manufactured goods). Dr. Coombs, Governor of the Reserve Bank, has stated that overseas exchange being obtained from new investment in manufacturing and from manufacturing exports is barely sufficient to cover purchases of equipment and the remittance of profits and service charges.
The truth lies somewhere in between these two views. It is clearly overstating the position to include the total export value of flour mills, butter factories, wool scourers and metal refineries when the great part of the value of the output is made up of the cost of the raw materials originating in the primary industries. On the other hand the actual value added by processing in these factories may be reasonably attributed to secondary industry.

A Department of Trade analysis of exports, using the wide definition, classifies all processed primary products under the category of "factory" output. This gives the following picture of manufactured exports over the years 1946/7 to 1958/9—

<table>
<thead>
<tr>
<th>Year</th>
<th>Rural &amp; Foodstuffs</th>
<th>Basic Metals</th>
<th>Iron &amp; Petroleum, Other</th>
<th>Total</th>
<th>% of Total Exports</th>
</tr>
</thead>
<tbody>
<tr>
<td>1946/7</td>
<td>102</td>
<td>14</td>
<td>5</td>
<td>2</td>
<td>36</td>
</tr>
<tr>
<td>1949/50</td>
<td>163</td>
<td>22</td>
<td>2</td>
<td>3</td>
<td>23</td>
</tr>
<tr>
<td>1954/5</td>
<td>184</td>
<td>32</td>
<td>7</td>
<td>7</td>
<td>39</td>
</tr>
<tr>
<td>1955/6</td>
<td>181</td>
<td>38</td>
<td>7</td>
<td>14</td>
<td>40</td>
</tr>
<tr>
<td>1956/7</td>
<td>189</td>
<td>45</td>
<td>27</td>
<td>17</td>
<td>48</td>
</tr>
<tr>
<td>1957/8</td>
<td>172</td>
<td>30</td>
<td>23</td>
<td>24</td>
<td>54</td>
</tr>
<tr>
<td>1958/9</td>
<td>174</td>
<td>31</td>
<td>25</td>
<td>23</td>
<td>50</td>
</tr>
</tbody>
</table>

Overall there has been little change in the export value of processed rural products in the last decade. A substantial rise in the export of cane sugar has been counter-balanced by a substantial fall in flour exports. Over the ten years, exports of butter, cheese, processed milk, tinned fruit and most other items have remained fairly steady in money terms; similarly with scoured wool and tops. But, in aggregate, processed rural exports are at present below the levels of the mid-'fifties. There has been a solid rise in exports of refined metals such as copper, lead and zinc, although they are currently much below the 1956/7 peak largely because of lower prices and American import quotas on metals.

It is clear from this table that the increase in the value of manufactured products that has taken place over the past few years is attributable mainly to an expansion in the ex-
port of non-primary products (columns 3 to 5 in the table above). However, even here, the actual increase in volume (i.e., when allowance is made for price rises) is very slight except in the case of petroleum products and iron and steel. In these industries a substantial increase in productive capacity has made possible a sharp rise in exports to markets in New Zealand and other areas in the Australian “sphere of influence”.

For many people the really critical item in the table on page 44 is that described as “other factory products” (column 5), for it gets closest to what they would regard as manufactured exports proper. This is where the factory process is more or less involved and where the value added by manufacturing is a substantial proportion of the value of the final finished product. A more detailed break-down of column 5 shows the following trend—

**EXPORTS OF “OTHER” MANUFACTURED GOODS 1946/7 TO 1958/9**

<table>
<thead>
<tr>
<th></th>
<th>1946/7</th>
<th>1949/50</th>
<th>1956/7</th>
<th>1958/9</th>
</tr>
</thead>
<tbody>
<tr>
<td>VEHICLES &amp; PARTS</td>
<td>2</td>
<td>1</td>
<td>8</td>
<td>9</td>
</tr>
<tr>
<td>MACHINERY</td>
<td>5</td>
<td>6</td>
<td>12</td>
<td>13</td>
</tr>
<tr>
<td>OTHER METAL MANUFACTURES</td>
<td>4</td>
<td>1</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>CHEMICALS</td>
<td>5</td>
<td>3</td>
<td>6</td>
<td>7</td>
</tr>
<tr>
<td>TEXTILES</td>
<td>11</td>
<td>3</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>RUBBER &amp; LEATHER</td>
<td>3</td>
<td>2</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>BOOKS, STATIONERY, PAPER</td>
<td>1</td>
<td>1</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>ALL OTHER</td>
<td>5</td>
<td>6</td>
<td>7</td>
<td>6</td>
</tr>
<tr>
<td>% of all exports</td>
<td>11</td>
<td>3</td>
<td>5</td>
<td>6</td>
</tr>
</tbody>
</table>

The expansion in exports of motor vehicles and parts which has followed the establishment of the local car industry, could almost be described as spectacular. The main market is New Zealand but bright prospects are also held for Malaya, Thailand and Africa.

Australia has a long-established export trade in machinery—especially farm implements and mining equipment in and around the Pacific area. The steady progress achieved over the last decade is expected to continue and could even accelerate if manufacturers of machinery in North America decided to use Australia as a base for Asian and Pacific exports.
Vigorous efforts being made to expand exports of other metal manufactures are bearing some fruit. For instance, particular success has been achieved with exports of louvre windows which have risen by over 50% since 1956/7. Although handicapped by high costs, chemical exports over a broad range have increased in recent years, especially in the pharmaceutical field.

On the other hand, the textile industry, which has suffered badly from rising costs, has lost ground in export markets, particularly since 1946/7 when local producers could easily undersell those overseas. Part of the explanation of the high export earnings by the textile trade in 1946/7 lies in the general world shortages of the early post-war years. In total, "other" manufactured goods now constitute a larger share of all exports than in 1949/50 and slightly more than in 1956/7. But the record still compares unfavourably with 1946/7 when Australia was able to capitalise on immediate post-war shortages and costs were much lower.

The export of industrial "know-how", a commodity of which Australia buys a lot but sells little, provides possibilities. A few Australian companies have achieved marked success in selling technical ideas to other countries and this prospect could be explored more widely.

A tabulation of manufactured exports since 1955/6, taken out by the Commonwealth Statistician using the narrow definition, largely bears out the Department of Trade analysis of manufacturing exports proper. These figures include iron and steel, but exclude petroleum, presumably on the grounds that the final value consists largely of the cost of crude oil.

<table>
<thead>
<tr>
<th>Year</th>
<th>£ m.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1955/6</td>
<td>46</td>
</tr>
<tr>
<td>1956/7</td>
<td>74</td>
</tr>
<tr>
<td>1957/8</td>
<td>73</td>
</tr>
<tr>
<td>1958/9</td>
<td>71</td>
</tr>
</tbody>
</table>

In a footnote to his table, the Statistician warns of the arbitrary character of the line necessarily drawn between primary produce and manufactures in his classification which
has resulted in the virtual exclusion of all processed primary products. The Bureau of Census and Statistics has not attempted to calculate the value added by manufacturing in exports of processed primary products. However, useful unofficial estimates have recently been made by Mr. G. R. Webb, a lecturer in the Faculty of Economics at the Melbourne University. Using data from the Secondary Industries and Oversea Trade Bulletins published by the Commonwealth Statistician, Mr. Webb has prepared estimates of the value added by factories in processing primary products and in refining imported crude oils. These figures give a virtually complete assessment of the contribution of secondary industry to export income.

Mr. Webb’s figures are set out below—

<table>
<thead>
<tr>
<th>Year</th>
<th>Prim. prods.</th>
<th>Mining materials</th>
<th>Petroleum materials</th>
<th>Total</th>
<th>% value attributed to secondary industry to total exports</th>
</tr>
</thead>
<tbody>
<tr>
<td>1946/7</td>
<td>33</td>
<td>6</td>
<td>-</td>
<td>73</td>
<td>24</td>
</tr>
<tr>
<td>1949/50</td>
<td>49</td>
<td>9</td>
<td>-</td>
<td>81</td>
<td>13</td>
</tr>
<tr>
<td>1953/4</td>
<td>65</td>
<td>12</td>
<td>-</td>
<td>127</td>
<td>16</td>
</tr>
<tr>
<td>1954/5</td>
<td>59</td>
<td>12</td>
<td>1</td>
<td>119</td>
<td>15</td>
</tr>
<tr>
<td>1955/6</td>
<td>64</td>
<td>14</td>
<td>2</td>
<td>131</td>
<td>17</td>
</tr>
<tr>
<td>1956/7</td>
<td>62</td>
<td>20</td>
<td>3</td>
<td>164</td>
<td>17</td>
</tr>
<tr>
<td>1957/8</td>
<td>59</td>
<td>13</td>
<td>5</td>
<td>154</td>
<td>19</td>
</tr>
<tr>
<td>1958/9</td>
<td>59</td>
<td>12</td>
<td>5</td>
<td>151</td>
<td>19</td>
</tr>
</tbody>
</table>

The most significant column in the table above is column 4 which covers exports of manufactured products in the strict sense. For the 3 years 1953/4 to 1955/6 exports of these goods remained fairly constant around £50 million a year. Then, in 1956/7, there was a big jump by £28 million lifting the total export figure to £79 million. Since then exports have remained around this figure.

This striking rise in 1956/7 is almost wholly attributable to an increase in exports of iron and steel of about £20 million and of motor vehicles and parts of £5 million. If these are
disregarded there has clearly been no increase of any note in exports of manufactured goods over the last three or four years—that is, since the Minister for Trade, Mr. McEwen, drew attention to the need for a much greater export of manufactured goods.

All in all, the figures suggest that moderate progress has been made in increasing exports of manufactured goods over the 1950 decade. The progress, however, has not been spectacular.

Australia confronts many obstacles in breaking into new export markets for manufactures. In a sense we are starting from behind scratch. Not only have the older industrial countries established commercial connections in many markets, but they also have an accumulation of knowledge and experience which Australia necessarily lacks. Australian industry, however, enjoys some advantage, because of its comparatively equable climate.

But, fundamentally, the greatest problem is that of comparative costs. This difficulty has been aggravated by the 1959 wage increases. Average hourly male wage rates in manufacturing in Australia are now over 10/- an hour. This compares with 7/6 in U.K., 2/6 in Japan and 5/- in West Germany. Export markets for manufactured goods in the face of such a labour costs’ disadvantage are anything but easy to win. Further increases in labour costs would diminish hopes of making even modest headway towards that increase in manufactured exports which well-informed opinion regards as imperative if development is eventually to be maintained. As Sir John Allison recently put the matter to a meeting of the Export Development Council: “Failure to meet the cost challenge would seriously impair our ability to continue as a nation at our present rate of growth. The problem of our export costs getting out of hand was still the ‘Achilles heel’ in our national economy.”

Future progress in expanding exports of manufactured goods will be watched closely. It may be not too much to say that the continuance of the large-scale industrialisation of recent years may finally hinge on the success achieved in this vital part of the economy.
The second quarter of 1960 has been a period of "wait-and-see" for the economic commentator.

Sufficient time has not yet elapsed for the inflationary consequences of the 1959 wage decisions to be fully assessed; it would be premature to draw any conclusions from the comparatively moderate 3/- rise in the cost of living in the first quarter of the year. Nor is it yet possible to do more than guess at the effects of the removal of import restrictions last February on the flow of imports and the balance of payments. Moreover, the 1960 Budget, which will be the most important for some years, is still a month or more away. In the meantime the critic must possess himself in patience until the course of government policy is made plain. All that can be said at the moment is that the present is no time to increase taxes.

The lack of issues of immediate public interest, however, affords an opportunity for some observations on three matters likely to be of continuing importance for the Australian community for some years ahead.

One of these is inflation. Even when last year’s wage rises have been fully accounted for in the price structure, few people really believe that we will have done with inflation. And this is a feeling held not merely by the financial and economic expert, but by the ordinary man in the street, whose instinct in these matters is, at times, astonishingly accurate. Why, then, is this so, despite the recently expressed determination of senior Cabinet Ministers that prices and costs must be stabilised?

For one thing, the dice seem to be strongly loaded against the Government. To some extent the Government is at the mercy of its own wage-fixing machinery, and the wage-fixing-
authority at the mercy of its own methods. The present system of an annual review of the basic wage, coupled with separate inquiries into margins for skill, makes it difficult indeed for the Commonwealth Arbitration Commission to refrain from granting additions to wages which will not out-run the very modest average annual increments in national productivity which are all that can realistically be expected. The present system of wage adjustment is strongly biased in favour of inflation.

But much more fundamental than the method of wage-fixing, is the scale of the investment programme. Doubts must be growing whether, in a free economy, it is possible to divert 25% of total national expenditure into investment purposes without a continuing tendency toward inflation. Probably in no other country outside Russia, is the ratio of investment to Gross National Product so high as in Australia.

Even in the wealthiest countries, resources are "scarce" in relation to all the demands made upon them. An investment programme which is extra-heavy, must inevitably come into conflict with the natural impulse of the community toward rising standards of consumption. This impulse can be curbed, but in a free economy, as contrasted with the "police" economy of Russia, the means for doing this are limited. Indeed, the one decisive weapon open to a democratic government for restricting consumption and thus for making resources available for investment, is that of inflation itself.

The government, of course, need not consciously indulge in inflation for this purpose. But having set its targets for investment, it may find that in order to realise the targets it is often forced to undertake measures—for example, higher taxes or budget deficits or higher charges by government instrumentalities to finance capital expenditure—which inevitably have inflationary consequences. Whether a government recognises it or not—and very often it does not—the necessary restriction of consumption and of current living standards to free sufficient resources for its investment objectives, is brought about through the agency of rising prices. These prices serve to cut back standards of consumption by reducing the purchasing value of the incomes of many people
in the community—though not of all—below what it would otherwise be.

Private business can also unwittingly aid and abet this process by raising prices and thus acquiring additional finance which they can devote to expanding investment in their own enterprises. This is a perfectly legitimate and necessary means of financing capital additions, but in an inflationary environment the higher prices charged tend to compel some restriction of real consumption on the part of the community.

Here is the great dilemma which faces Australia in its efforts to stop inflation, and it is a dilemma which has not yet been finally resolved:— Is some inflation—perhaps only a little inflation—desirable in order that the pace of development and economic expansion can be maintained? Or is it better to settle for a slightly slower pace of development for the reward of stable prices?

In the 1950's the decision was clearly in favour of the first alternative. But whether this alternative would be wise—or indeed practicable—in the years ahead is open to question. In any case, what is clear is that most sections of the Australian community, have not yet finally made up their minds on the right course to pursue. Despite the Government's pronouncements on inflation, it is hard to escape the feeling that there is still a gap, although a narrowing one, between intention and will. Certainly the Australian people and the Commonwealth Government are much more strongly opposed to inflation than they were through the 1950's. But it has yet to be proved that they would be prepared to carry their opposition to the point where the enemy was not just seriously weakened, but beyond all doubt conquered.

LAST April, Professor F. A. Bland, former Chairman of the Commonwealth Public Accounts Committee, declared that democracy in Australia had been defeated and bureaucracy was triumphant. This, in our opinion, goes much too far. Nevertheless, Professor Bland has drawn attention to a development to which we have become dangerously indifferent.
The growth of the bureaucratic machine to its present giant proportions is largely a result of the modern planned and regulated economy, and to the increasingly complex range of functions undertaken by governments in response to insistent public demand. It is a development by no means confined to Australia, but world-wide. There are today in Australia around 150,000 public servants (i.e., employed in administration and not in government activities such as transport, education, police, post office, and so on)—more than twice as many as before the war. There is now 1 public servant to every 70 people as against 1 to every 100 pre-war.

Not only have the day-to-day administrative functions of the public service grown enormously, but the powers of government departments and of top officials over national policy have become very much greater than they were even twenty years ago.

In theory, the public servant, in policy matters, is no more than an adviser; in practice, his influence on policy is frequently decisive. The senior departmental official today exerts an authority over matters of high national policy far in excess of the ordinary elected representative of the people in Parliament, and often greater than the Cabinet Minister who, by comparison with the full-time expert official, cannot often help being little more than an intelligent amateur in the matters of his department.

There is, of course, no putting the clock back. As Sir Winston Churchill said years ago, you can’t solve unemployment by a show of hands in Parliament, but only by taking the right action, and the right action is usually a complex amalgam of many ingredients, which, in turn, are themselves frequently complex.

The drift of great political power to the full-time expert official is something made inevitable by present-day government and our modern conception of how it should serve the community. But while recognising its inevitability, we should also be constantly alive to its dangers. The lesson of history is that no section of the community can safely be entrusted with an excess of authority; and the modern bureaucratic
machine cannot claim exception from this basic democratic principle.

In fairness it must be said that the senior personnel of the public service have shown exceptional competence in performing their duties, and Australia has reason to be grateful, not only for their ability but for the sense of dedication which they bring to their tasks. To criticise "bureaucracy" is not to criticise individuals, but a growing tendency, in other countries as well as in Australia, toward government by permanent officials rather than by those elected by and responsible to the people.

There is no simple means by which this tendency can be reversed or even halted. The solution, if there is one, will have to be sought along many channels. One or two observations can be made.

The public has a right to expect that its Cabinet Ministers will not be over-awed by the expertise of their departmental advisers. Again, it is not suggested that this actually occurs, but it is true that there is probably no more effective safeguard against bureaucratic tendencies than the able, strong-willed Minister not afraid to exercise his own judgment.

Another safeguard is to be found in intelligent and continuing comment on Government policies from responsible critics. The operative words are "responsible" and "intelligent". Irresponsible criticism, of which there is too much, by arousing contempt among those at whom it is directed, probably only serves to give rise to the feeling that "we know what is best". But it is difficult for criticism to be "intelligent" unless it is well-informed, and the public is entitled to insist on full explanations and justification of proposed policies or of governmental actions. The practice of the departmental White Paper (issued under the authority of the Minister) is one way in which intelligent criticism can be assisted, and could, with advantage, be much more frequently resorted to.

But the subject is a big and portentous one, and much more is certain to be heard of it in the years ahead.
The third problem concerns the growing inadequacy of the roads to cope with the almost terrifyingly rapid increase in the number of motor vehicles. Each year something like a quarter of a million motor vehicles are being added to the multitudes which already crowd the Australian roads.

Over the 1930 decade the average yearly addition to the motor vehicle population was a mere 30,000. Some conception of the magnitude of the problem can be gained from the fact that 350 motor vehicles, bumper to bumper, would fill up over a mile of single-track highway. 250,000 vehicles would take up 750 miles.

In the years immediately before the war we were spending on road maintenance and construction £25 million, or £4 per head of population. Today we are spending £120 million or £12 per head of population, which is little or no more than before the war, after allowance is made for the fall in the value of the £. But today we are adding nearly as many motor vehicles to the roads in one year as we did in ten years during the 1930's.

It is clear that we are shortly going to need entirely new perspectives on this problem and the sooner we get them the better it will be, not merely for the motorist, but for the general comfort and safety of living in Australia.

Although it has been said, almost to the point of tiresome repetition, that we live in a “motor-car” age, that does not make it any the less true. Whatever is done about improving facilities for public transport, increasing numbers of people are going to insist on having their own cars. If they cannot use them in reasonable convenience and safety, the cumulative anger arising from widespread frustration could be terrible indeed.

At present the roads do not, generally, provide for rapid and comfortable travel by the motorist; the pleasant Sunday afternoon drive, for instance, is little more than a memory. Nor do they provide for safe travel, and how much of the awful toll of accidents is attributable directly to the glaring inadequacy of the roads, we will never know. But it must be considerable.
The economic wastes in loss of time because of hold-ups and excessive vehicle maintenance caused by rough surfaces must be enormous. (It is estimated that delays due to traffic congestion alone are costing the economy £200 million a year.) Unless drastic steps are taken soon, the whole position could rapidly degenerate into near-chaos. Better roads, allied with adequate parking facilities, are something the people will continue to demand and a democratic free economy must find ways of meeting that demand.

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Although it may, at first sight, seem that these three matters are entirely separate and distinct, strangely enough they are all inter-connected. In an economy suffering from the disease of chronic inflation, there is a constant insufficiency of resources with which to meet basic national requirements and community demands. Shortages crop up, often in the most unexpected places, and many essential needs remain unsatisfied.

In this situation there is, of course, much more for the public service to do. Problems constantly arise; the facts must be uncovered; reports prepared; special committees, and often even departments have to be created. For instance, for most of the 1950's we had a large department of public servants to deal with the licensing of imports. The acute problems posed by the roads has led to the establishment of a National Roads Council. With rapidly rising costs, government authorities, such as the Tariff Board are overwhelmed with work. And so it goes on.

All things in economics are inter-connected. With some, the thread that connects them may be obscure to the point of being invisible, but it is there if we search hard enough for it. Present-day thinking is over-prone to treat apparently different problems as isolated entities. As in medicine, so in economics, many superficially diverse ills often arise from a root basic cause, which can be uncovered if we dig down deeply enough.
A Note On Productivity

IN recent years the concept of "productivity" has become of great importance in economic analysis and in the fixation of wages.

The concept itself is not difficult. Productivity is simply the efficiency with which goods and services are produced.

The measurement of productivity, however, is exceedingly complex and its development is still in a comparatively early stage.

Indeed, most statisticians would agree that the measures so far produced are so crude, that they should be used sparingly for practical policy decisions. But the reservations which the statisticians apply to their own measurements, have not prevented the use of these measures, sometimes to an unwarranted extent, in economic analysis and even in the fixation of incomes. This practice could lead to conclusions and to decisions which are seriously in error.

A brief and clear statement of the limitations of measurements of productivity was given last March to the National Association of Manufacturers Institute on Industrial Relations in the United States.

The authors of the statement, Bernard G. Rogers and Roger H. Fulton, are attached to the Industrial Relations Division of E. I. du Pont de Nemours & Co. We republish the statement here:

"During the past few years there has been much public controversy with regard to the relationship of wage increases to inflation, and inevitably, these discussions involve the subject of productivity. The term 'productivity' has been used so frequently that it has acquired an impressive and acceptable stature with the public.

This is unfortunate because the productivity concept is still in its infancy and careless application of the measure to wage problems may result in financial losses to employers as well as dislocations to the economy."
Industrial management is so well aware of the seriousness of "wage inflation" or "cost-push" inflation that documentation of this fact seems unnecessary. However, the pitfalls of relating productivity to wages and its consequences upon profits and prices are apparently not as well understood.

Stated simply, productivity is a measure of the efficiency with which resources are converted into goods and services that the people want. If the nation experiences a rise in productivity or the efficiency with which it utilizes its resources of land, labour and capital, its standard of living is thereby improved. Looking at it from a slightly different viewpoint, productivity changes also affect such things as profits, prices and wages.

In theory, productivity is simply a measure of the change in the ratio-output divided by input. The output term represents all goods and services having market value. The input term represents all resources which contributed to the output. While this measure is simple in concept, many problems arise when attempts are made to undertake specific measurements. In fact, the experts on productivity take great pains to qualify the accuracy of their results.

Contrary to widely held opinion there is currently no precise measure of national productivity. Not only is output in the economy difficult to measure but statistics relating to the input which made the output possible are still in the formative stages of development. This lack of data caused economists to seek a short-cut to the problem of measuring productivity trends. Estimates of national output were divided by the labour input because figures relating to man-hours worked were available. This, in effect, was the origin of the output per man-hour measure.

Output per man-hour, in the case of the national economy, ignores the use of land, natural resources and most importantly capital. In the case of industries and firms, it also ignores intermediate materials and services purchased outside the unit. Yet, without these inputs, no output would be possible.

The proposition that output per man-hour provides an exact measure of productivity is sheer nonsense. It assumes that changes in efficiency are based solely upon the relation-
ship of changes in output and changes in man-hours and that the improvements in productivity would be the same regardless of whether a 10% or a 100% increase in capital expenditures were required to achieve the improvement in output.

Obviously capital is not available for the asking. Capital inputs such as machinery and equipment which provide the basis for most increases in efficiency are no more a free commodity than is labour—if they were, unlimited capital would be available to everyone. Because it is not free and the owner must earn a return on his investment, capital should also be considered as an input resource in order to obtain a measure of true productivity savings. The output per man-hour measure does not take account of this basic fact in our economic system.

While economists have recognized the deficiencies of output per man-hour as a measure of overall productivity, the development of a better measure did not come until after World War II when the subject of productivity began to receive wide-spread attention.

As a result of studies made by men such as Hiram W. Davis, formerly of the University of Pennsylvania and John W. Kendrick of George Washington University and the National Bureau of Economic Research, a new experimental productivity measure is gaining acceptance. This measure, which is generally called total factor productivity, takes into account not only labour but all pertinent inputs such as capital and materials and services.

Generally, estimates of productivity gain in the national economy by the total factor measure are significantly lower than output per man-hour figures for the same period of time. These differences by themselves should raise a serious question about the meaning and measurement of productivity.

Before intelligent decisions can be made with regard to productivity, a better understanding of the measure itself is required."
Mr. Horsfall has had a distinguished career in economic journalism. He is a business and financial correspondent for several journals in Australia and London.

From 1947 to 1950 he was on the editorial staff of "The Economist". He was a key figure in the establishment of the "Financial Review" (published by the "Sydney Morning Herald") of which he was the first editor.

From 1955 to 1957 Mr. Horsfall was Investment Manager of the National Securities Corporation, London.

Mr. Horsfall is a graduate of the University of Melbourne and of Cambridge. He had a distinguished career in the British Army during the war, particularly in the field of military intelligence.

Among many attainments he was Victorian sprint champion in 1932 and 1933.

In Australia's special circumstances as a country more often than not in deficit on its current balance of payments, the provision of capital to meet its long-term growth requirements is uniquely dependent on the inflow of overseas capital. This is so if only for the reason that the level of capital inflow determines the marginal increment of the country's imports.

Our degree of reliance on overseas capital is in fact a good deal greater than that conceded by some public figures who would impose more exacting conditions for its participation in Australian industry. Quite apart from balance-of-payments considerations, one reason for this is that taxation milks the stream of incomes so heavily for funds to finance public works, thus reducing available savings which might otherwise find their way into private sector investment.

Nonetheless remarkable progress has been made in the provision of capital from internal sources. Indeed, the development of machinery for the better
marshalling of investment funds has been an outstanding feature of the financial scene in recent years. By this is meant not just the widening and formalisation of facilities for the employment of short-term funds, but rather the development of the whole complex of arrangements for the finance of public works, industry, trade and commerce. This is not to say that our sophistication in this field is yet complete or that the present machinery and its out-workings are satisfactory in all respects. Maybe, looking beyond the immediate efficiency of the capital market in doing the job required of it, there is room for tightening in the legislative requirements for the raising of capital, in order to ensure that better use is made of national economic resources.

It is pretty clear, for instance, that the current speculative boom in metropolitan real estate is in some respects to be deplored. People contemplating marriage are finding it impossible to buy land without paying the earth for it and incurring a debt to finance companies out of all relation to their earning capacity. The interest element on the debt is usually formidable enough without counting in capital repayments. Yet, thanks to the free-for-all in raising money at very high rates of interest, speculation in real estate has inflated prices to such an extent that genuine buyers of land lots have no alternative but to accept the terms. Ultimately when the boom collapses and such buyers see the value of their land fall heavily, they will still have to shoulder the debt and, putting two and two together, are likely to take a jaundiced view of the situation which made the speculative land boom possible.

Possibly less clear to most people is the likely fate of genuine savings lured by glowing advertisements into purchases of land trust units, for in most of these there is no security at all for an individual buyer. All may be well while the boom lasts; the prospects of capital appreciation may seem to be coming good; promises of high dividends, cash at any time and the rest may be all honoured so long as more and more gullible citizens are brought into the net. But, if the boom bursts, the holder of a land trust unit will find that the whole process goes into reverse and that he is likely to get his fingers badly burnt. It has happened many times before. And it could happen again.

The problem is to try and stop this sort of thing without impeding the free functioning of the capital market to serve the interests of genuine development. This is a ticklish one because so long as competitive forces in the market are unfettered, the interest rate structure will be determined by the strength of those forces. This will in turn condition their success in drawing funds from the market and so dictate the disposition of the capital resources available to the community.

Of course, the bulk of the capital required by industry is financed directly by companies themselves through their depreciation provision and undistributed profits. These funds do not flow directly through the public capital market though some of them may find their way there while awaiting investment and play a considerable role as intermediary support both for Government loans and other company financing.

The proportion of private investment funds found from these two sources has risen appreciably in recent years. Total private investment increased from £580 million in 1949-50 to £1,141 million last year or by about 97 per cent. While, between the same years, undistributed profits rose from £89 million to £201 million or by 126 per cent, and depreciation increased from £145 million to £439 million or by as much as 200 per cent.
It is understandable that companies should prefer this method of finding funds. It costs them nothing and shareholders don't seem to mind either—as is evident from the low yields on the shares of companies most noted for ploughing back.

Naturally all companies would like to see higher tax allowances for depreciation. However, the Federal Government is reluctant to go as rapidly down this particular path as industry would certainly like to lead it.

All and sundry among industrial companies have been obliged to come to the capital market during the '50's—or at least to the periphery of it, as when their appeals for more capital are addressed only to shareholders. The most notable exceptions to this are the affiliates of overseas concerns whose expansion is often financed by parent companies abroad. These are the companies which Mr. A. A. Calwell would like to see at least 49 per cent owned by Australians, a suggestion which seems to fly in the face both of the limited savings available to industry from indigenous sources and also of the usefulness, to put it no higher, of the capital and know-how these companies bring into the country. However the Leader of the Opposition's oft-repeated theme never fails to find a spirited response in certain circles. Most of the other exceptions are private companies. These companies are precluded from raising capital from the public anyway and must confine themselves to indirect routes for dipping into the general pool of savings. Private companies have found it increasingly difficult to meet their capital needs in the present era of rapid expansion and many have solved the problem by taking on public status and through amalgamations.

The high proportion of new capital now raised in the form of issues to shareholders, either by way of prior charges, such as the ever-widening range of notes, or issues of preference (comparatively rare these days) and ordinary shares, is really outside the public capital market proper and more or less a family affair for individual companies. The most striking—and puzzling—thing about it for one with experience in overseas capital markets is that practically all new issues to shareholders in this country are on highly preferential terms which bear little relation to the market value of the issuing companies' securities. This seems to make nonsense of at least one of the early precepts on the "raison d'être" of stock exchanges. For it means in effect that in making an issue at par, for companies whose shares are standing at a premium the main benefit from the premium accrues directly to the shareholder rather than to the company. The only advantage to the company is that a high price on its existing securities is virtually a guarantee that a new issue at a price well below it will be successful. But by making issues at prices related closely to the market prices of existing securities, new capital could be raised much more cheaply and by issuing fewer new shares. On the other hand the adoption of premium issues would probably result in income yields taking a bigger part in investor's calculations and this would tend to make for a lower level of share prices. As matters stand the dissipation of premiums in the hands of shareholders through the sale of rights to new issues could represent an unwarranted waste of capital resources.

Another very popular method of acquiring new capital outside the normal market channels continues to be for companies to take over other companies. In these transactions the vendor company takes as consideration either shares of the purchasing company or a combination of shares and cash. Of course, this method doesn't involve any net
addition to the supply of capital in the country. Nor does it mean that the motives for taking over other companies are necessarily concerned with the provision of more capital. Sometimes one company wants to get another out of its competitive path; sometimes the motive is to achieve economies of scale by the integration of plants producing the same things; sometimes one company takes over another in order to extend the range of its activities or to employ its surplus funds more effectively . . . and so forth.

Take-overs have become part of the everyday scene in this era of vigorous industrial growth. For the most part they result in a greater degree of rationalisation in industry and a more efficient use of the country’s resources. And inasmuch as they revivify capital in the less efficient and unenterprising firms by putting it in the hands of the efficient and enterprising ones, it is all to the country’s good.

On the other hand they provide scope for activities opposed to the national interest, particularly in the manipulation of share values in advance of information being made public. Though it is often difficult to pick the genuine as distinct from the merely ingenious sort of take-over, some people suspect that a take-over can sometimes mean gratuitous capital benefits for insiders. The stock exchanges now demand to be informed of take-overs and bids before insiders have the opportunity to operate in the market. But the exchanges may have to consider further safeguards in order to minimise the possibilities of making money by this method. The free enterprise system will be strengthened if the possibilities for acquiring quick gains by those in a position to beat the gun through advance information are curtailed.

In the capital market proper, where companies make new issues direct to the public, the tendency has been to swing away from direct issues of ordinary shares in favour of high-interest coupon notes. These notes are often convertible into ordinary shares within, say, a five year period, they usually carry the same rights as ordinary shares to both bonus issues and issues for cash. From a company’s viewpoint the principal advantage of this method of raising new capital is that interest on notes is deductible for taxation purposes. On the other hand, dividends, and allocations to depreciation above the maximum permitted by allowances, come from taxed profits.

This method also enables companies to compete more effectively with the growing number of high-interest short-term media of which there is an increasing proliferation, issued in the main by hire-purchase, finance and real estate development companies. This is all very well, but the general adoption of convertible note financing in preference to straight issues of equity capital offends the basic principle that, unless it is required for funding short-term debt which has been used for building up the earning power of an enterprise, new capital cannot, by the very fact of it not being represented by productive assets, immediately pay its way. And, after all, when you have to start paying 7 or 8 per cent on new money from the word go, this is a heavy and unwarranted burden on any enterprise—except perhaps one that has suddenly struck oil. The sooner we get back to a sounder balance between genuine risk capital and fixed interest capital the better. But to do this it seems essential to eliminate much of the competition for new money represented by the growing number of attractive short-term media issued by what are primarily finance companies.
It was to the latter that Mr. C. H. Hoskins seemed to be referring in his chairman's address at the recent annual meeting of the Australian Mutual Provident Society. Mr. Hoskins said that he found it difficult to believe that "all these media are well based or performing a useful function". He suggested that while some of these have provided valuable additions to our capital market mechanisms, "some of the financial ventures seeking funds from the public may do little if anything useful for the economy and at the same time offer quite insufficient safeguards for the savings of those who have entrusted funds to their keeping". He went on to say that "the legislation affecting companies and other financial institutions was written long before some of the new forms of investment and savings appeared, and hence the degree of supervision is very meagre indeed. Genuine enterprise should not be impeded by harsh controls but at the same time the savings of the people should never be imperilled by laxity on the part of the authorities".

This puts succinctly the general view of responsible people in the community. There seems no doubt that provision of capital for sound industrial enterprises would be made very much easier if competition from unsound and over-optimistic finance companies were softened. In such an event there would also most likely be a salutary return to the more orthodox method of financing industrial expansion by new direct issues of ordinary shares. It goes without saying that we would then get far better value from the limited capital available to the economy.

Nor must it be forgotten that high interest rates offered on the widening range of short-term investment media, including facilities for investing money at call for returns of upwards of 3½ per cent (one company is currently offering 5 per cent for call money) has also had adverse repercussions on the financing of public works. The country's capital needs for public works are now of the order of £550 million a year. A high proportion of this is actually found from taxation, rates and other authority charges and so presents no difficulty. But to raise the remainder the authorities have had to make some drastic changes in their approach in recent years.

There have, of course, been the skilful variations in methods of financing what may be called the credit element in public works finance; for instance in the switching about from Treasury bill to bank credit. But though very relevant to the overall problem of the availability of capital (in so far as there are limits to the amount of credit that should be used in any given state of employment of the country's resources), this doesn't directly affect the capital market.

More pertinent is the Federal Government's resort to short-term bonds bearing higher interest rates and having an element of capital appreciation in them, if held for certain periods, in its endeavour to fill its loan targets. Doubtless, the introduction of attractive short-term investment media of this sort by the authorities is meant to counter the competition of the kind Mr. Hoskins was referring to, as well as recognising the fact that the real value of bonds is eroded by inflation.

But the most striking development in the capital market—and one incidentally that has greatly assisted in the provision of funds for public works—is the establishment of the short-term money market. This market has not only revolutionised facilities for dealing in bonds. It has also imparted some sorely needed flexibility to the whole capital market. Previously the market's facilities at the
short end were very narrow. Now companies and others with surplus liquid funds to employ for short periods know where this can be done with absolute security and with perfect facility. At the same time, in aggregate, the liquid funds flowing through the market make a very valuable contribution to the pool of capital available for both industry and governments.

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THE subject of short-term financing can only be lightly touched on here. Of course the banks, including in these Commonwealth and State Government credit institutions as well as the private banks, are pre-eminent in this field as they always have been. But several new fields of financing have been greatly widened in recent years and the banks have been at pains not to be left out. And, at least, as in Britain, the private banks have departed dramatically from their traditional role by entering whole heartedly into hire-purchase financing by buying into hire-purchase companies proper. Commonwealth and some State banks have, of course, been in the hire-purchase business for longer.

Less satisfactory from the private bank’s viewpoint has been the extent of their financing of housing. In this field in which the Commonwealth banking nucleus and also finance companies not subject to equivalent regulation and restriction as to rates of interest and deposits, have made most of the running. The private banks appear to be playing just as relatively important a part in short-term financing as ever. Admittedly though many industrial companies appear to have borrowed less from them in recent years and some new types of financing, such as factoring, are coming more into the picture. By and large the banks remain the bulwark of short-term financing, though steps certainly need to be taken to create uniform conditions of operating where they compete with what is now commonly referred to as “the second banking system”.

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