The Goals Change

THE Western economies seem to be approaching a decisive historical turning point. The paramount goals of these societies may be about to undergo far-reaching changes which will almost certainly involve equally far-reaching revisions to the policies, attitudes and structures of their economies. The future of private enterprise may be determined by how clearly its leaders comprehend the impending historical climacteric and how well they adjust to the new demands industry will be called upon to meet.

The previous great turning point of the free enterprise Western economies was a mere thirty years ago, around the end of World War II. A whole new set of objectives replaced those more or less tacitly accepted in the decades before the war; the free enterprise societies were confronted with the stern alternative of either meeting these objectives, or being replaced by some other radically different kind of economic system.

The new goals were Full Employment, a floor of Social Security, a more equitable distribution of income, greater equality of opportunity, Economic Growth and steadily rising living standards. In Australia we set ourselves the additional goal of a rapid expansion in Population to be achieved through a massive injection of immigrants.

Virtually three decades have elapsed and the reconstructed free enterprise systems have achieved quite extraordinary successes in accomplishing the goals demanded of them. Indeed, success has been so rapid that, in some respects, we may have failed to adjust our thinking to the realities and problems of
the new kind of society that has emerged. We have barely stopped to ask ourselves whether some modification of goals accomplished, or of policies pursued, may now be necessary. The famous American economist, John Kenneth Galbraith, recently noted, "The reluctance to accommodate to underlying social change is not new. Its consequence is that, in time of social and institutional change, the advice on practical matters which reflects the accepted economic view will often and perhaps usually be in error. The advice will relate to previous and not present institutions: the needed action, unfortunately, must relate to the reality. If it does not, it will be at best inadequate or useless and at worst, damaging".

Much of the great shift in emphasis which is now occurring revolves around the concept of Growth. In the Western societies, Growth has held the stage for the last two decades; the performance and success of their economies have been gauged, predominantly, by the annual percentage increases in Gross National Product.

Growth has been measured simply by the yearly increment in the volume of goods and services produced. Since the main determinant of growth is output per person, rapid productivity improvement has assumed central importance. (In Australia, as distinct from most other Western economies, population increase as well as the increase in productivity, has also had a significant influence on the growth rate.) Those countries, such as Japan and Western Germany, which have achieved far higher-than-average Growth have been regarded as setting an example for countries, such as Britain and Australia, whose growth rates have been near the bottom of the international tables.

The Growth objective, until recently an economic sacred cow, is now being widely and trenchantly criticised. The criticisms have a moral, emotional and intellectual content.

As standards of living have advanced and the Western societies have become more affluent, the single-minded emphasis on Growth is being attacked as a narrowly materialistic and ignoble goal for human endeavour. Even among many who may not question the moral justification of the Growth objective, there are increasing signs of unease about where we are heading. People are asking, "Where does Growth stop? Even though we may not have reached it yet, there must surely be a limit to
affluence, to the production and consumption of more and more goods and services. We can’t go on increasing affluence for ever”.

The fiercest emotional assaults on Growth come from the growing army of extreme conservationists, and from the rebellious young who display an alarming distaste for many aspects of modern Western society. However, powerful attacks on the Growth concept, on a more intellectual level, are also being launched by eminent economists and scientists, such as America’s Galbraith, and in Australia, by Professor F. J. Fenner, Director of the John Curtin School of Medical Research at the Australian National University. The latter is a strong opponent particularly of the goal of population expansion for its own sake.

Even some world figures in politics and high-level administration have raised dissenting voices. In his first press conference after assuming the office of President of the Common Market Commission, Sicco Mansholt surprised his audience by saying, “Gross National Product in all our member states, and also in the United States and Japan has been thought of as something sacred. But GNP is diabolical. We must think, instead of our people’s happiness”. Pierre Trudeau, the Prime Minister of Canada, has on a number of occasions queried the single-minded pursuit of Growth. Our real problem he has said, is “how to maximise human dignity and the quality of life”.

What is to be said in face of this multi-pronged attack on the hitherto generally accepted central dogma of the Western economies?

It is impossible to deny that Growth is giving rise to an alarming accumulation of frightening by-products which were not foreseen even so late as ten years ago. The rapid inroads into world reserves of natural resources, the pollution of air, water and land, the destruction of plants and wild life, the increase of noise, the growing human frustrations of urban living and the congestion of people and traffic, are among them. Many scientists see an imminent threat to the whole balance of natural forces upon which Man is ultimately dependent for his very survival.

Two schools of thought seem to be holding the floor on the Growth debate.
(1) Those who say that Growth has become an unmitigated evil which, unless restrained, will eventually undermine the life supports of the human species: in other words, that in the unqualified pursuit of Growth, Man is engaged in a process of ultimate self-extinction. Some exponents of this school of thought assert that the only sensible policy, particularly for a country such as the United States, is Zero Economic Growth and Zero Population Growth.

(2) Those who claim that the remedy for the ills attendant on Growth is still faster Growth, for the disturbing side-effects of Science and Technology, more Science and Technology. This school argues that only out of continued Growth will it be possible to provide the resources necessary to eradicate pollution, to preserve the environment, to solve the crisis of "the big city", to feed the exploding millions.

As is invariably the case in human affairs, the path of wisdom and common sense would seem to lie somewhere between the two extremes at present engaged in an uncompromising, rather absurd, confrontation.

It must be clear by now that the time is rapidly approaching, if it is not already here, when we must look at the Growth objective much more critically. It should hardly, for instance, these days be regarded as a national calamity if the Growth rate for a single year fails by a few decimal points to achieve the target which has been set as the desirable aim. Only the purblind can still believe that Growth and Progress are synonymous and that GNP is a reliable index of the community's welfare and happiness. Economists now need to widen their sights and devise a less misleading, more convincing measure of progress, even narrow economic progress, than the annual increase in GNP. It is surely the highest order of naivety to imagine that the Kingdom of God on Earth and a better life for all will follow as an automatic consequence of ever-lasting Growth.

The Western economies will clearly now need to devote a far higher proportion of their resources to the cure and prevention of the bitter consequences of unrestrained industrialisation and urban expansion. In Australia, for instance, the policy of bringing in more and more immigrants to add to the mounting discomforts and frustrations of our two major cities will have to be looked at much more critically. The idea,
which has dominated our economic thinking for two decades, that the numbers game in things produced and in population expansion leads to progress will have to be replaced by deeper, better balanced goals. The quality of life, as distinct from the quantity, must now take over as the paramount objective, the main concern of economic and social thought.

In Japan, it is worth noting, an almost revolutionary change in attitudes has taken place in the last 12 months: official policies are now placing primary emphasis on the correction of the environmental disorders which have accompanied the almost miraculous economic progress of the last decade.

When all this is said however, as it should be said, the vast majority of the community will, for some considerable time yet, be seeking and demanding further improvements in their personal material standards of living. This is where the proponents of Zero Growth lose touch with reality. "The affluent society" is after all a relative concept. Today's Western societies, it is true, are marvellously affluent by comparison with those that have preceded them. This does not mean, however, that the majority living in these societies think of themselves as affluent. They will still be looking for further improvements in their material conditions, further opportunities to indulge their tastes for the good things of life, greater economic security for themselves and their families. Any Government that ignored this over-riding ambition would not remain in office for a day. These are hard, practical considerations which the more starry-eyed conservationists overlook. There is a measure of irony in the fact that some of the most eminent advocates of the virtual cessation of Growth have themselves already acquired a living standard far above that enjoyed by the great majority. It seems a bit ungenerous of those who have reached the top of the ladder to suggest that the ladder should now be kicked away so that nobody else will have the opportunity of climbing up.

What is needed now is not so much a complete rejection of long-established goals, as a change of emphasis. Nevertheless, the change needs to be no minor one. Insignificant and painless adjustments to present attitudes and policies will not suffice. Western society is confronting momentous issues, and nothing less than a revolution in our way of thinking, both on the national and international planes, will meet the situation.
If the massive population, social, environmental and urban problems facing Western societies are to be resolved, business and the community will have to pay the price, and the price will be heavy. There is no escape from that. In straight economic terms, it means that there will have to be a large-scale diversion of resources from the improvement of personal living standards and from economic development to the new imperative demands. How this diversion can be accomplished within the free market economy will need to be worked out by political and business leaders and their advisers. To ignore these demands by continuing blithely on our present path would assuredly, in due course, run us into a crisis of the utmost magnitude in which our democratic Western way of life would be imperilled. Ecologists would no doubt go further and say that Man's survival itself would be threatened.

Those who see the solution to our current dilemmas in Zero Growth are wrong. We still need Growth, but Selective Growth, Growth of a different order from the concepts we have come to accept over the last quarter of a century.

We still need Productivity, but Productivity channelled, at least partly, to different ends and purposes from those of the Consumer, Admass Society. The diversion of resources needed will be brought about either by massive intervention by governments, with all that that means in terms of taxes, bureaucracy and interference with the free market; or, it will be brought about largely through business, and particularly by the large strategic corporations accepting new responsibilities for the good of society. A leading American economist, Henry C. Wallich of Yale University, pointed out in the March 1972 "Fortune", "Everybody will benefit if more of the work of improving the world is handled by business and less by government. The job will get done at minimum cost instead of with maximum bureaucracy. The ultimate menace of Big Brother (in Washington) will be pushed back".

Thirty years ago thoughtful, far-sighted businessmen recognised the need for an attack on the shortcomings of Western capitalist society. It was partly due to their intervention, and its expression at government levels, that the worst evils were overcome and that liberal free enterprise was preserved as the major ingredient of the Western economic system.
The very successes of the last three decades, however, the unprecedented advances in standards of life and general affluence, have been to some extent responsible for the dilemmas which Western society is facing. As was the case thirty years ago, business leaders will now need to turn their attention to the solution of the new crop of grievous problems which has emerged. While they cannot afford to take lying down the extreme, emotional assaults on the modern business system and on Science and Technology, they also need to realise that the single-minded and self-centred pursuit of Growth no longer makes sense.

At the core of the whole crisis of Growth is not merely Man’s viability but Man’s essential dignity. We are re-learning, through bitter experience, the ancient truth that the dignity of the individual, which is at the heart of liberal philosophy, can not only be destroyed by Poverty, but can also be subtly corrupted by an unthinking affluence.

Affluence can never be more than a means to the end of a higher and nobler life for the human species: when it tends to become the end itself, Man is launched on the downward path of self-destruction. The Youth of the World, so wrong perhaps in many things, are undeniably right in discerning that only through an ever widening and deepening sense of brotherhood can the human species find salvation.

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IPA Review — April-June, 1972
Inquiry into Taxes

There is mounting concern about Australian taxation. In broad essentials the tax structure has remained intact for a quarter of a century. The Commonwealth Government has at last decided to institute a full-scale inquiry into the operation of the tax system.

No doubt because of constitutional reasons the terms of reference of the Committee of Inquiry are restricted to the Commonwealth field thus leaving out State and local taxation. The Committee also presumably has no authority to examine the growing practice of government business undertakings to set charges for their services at rates which will finance not merely their operating costs but also large-scale capital extensions; these charges are, in principle, no different from taxes imposed by governments to finance public works. The Committee of Inquiry would thus seem to have no power to consider the all-important matter of the impact of the Australian tax system, in its entirety, on the economy.

The Institute of Public Affairs ever since its formation has been concerned with the shortcomings of Australian tax policies.

In August, 1945, the I.P.A. published a booklet, “Taxation in the Post-War Years" and since that time many articles have appeared in “Review" advocating changes in taxation policies. The 1945 booklet said that the tax system should be reviewed in its entirety; taxation should be looked at not merely as an instrument for raising government revenues, which seemed to be the dominant consideration at the time, but from the standpoint of its effects on post-war production and employment. As the following extracts from material published over the past 27 years will show, we have continued to be concerned not only with these effects but also with the tax contribution to chronic inflation.

Taxation extends to every corner of the economic structure, it influences directly every business decision and enterprise, it enters into practically every economic calculation as a factor of major importance.

The ultimate source of all taxation is personal endeavour. Over-high taxation must tend to weaken this endeavour and therefore to destroy the source of its own creation.

An equalitarian society in which men are rewarded primarily according to their needs, and not according to their skill and efforts and achievements, will be a stagnant, dormant society with death at its heart.

The crucial argument against higher taxes is that, no matter what form they take, they will sooner or later give rise to increased incomes and thus to higher costs and prices.

In one way or another the different sections of the community eventually take action to counter the effects of increased taxes on their pockets. And this activity inevitably gives rise to inflationary consequences.

At current rates taxation is hitting middle and upper-middle incomes in Australia more severely than any other country. An overhaul of the income tax scales is an urgent priority.

It is often claimed in academic and other circles that Australia is one of the most lightly taxed countries in the world. This view is based on macro-economic measures which show that tax revenues as a proportion of GNP are lower than in most Western nations.

A simple percentage ratio of total taxes to GNP fails to take into account the widely differing incidence of various forms of taxation. The table, at the top of page 33, which dissects taxation into its components enables a much better comparison to be made than the bald percentage of total taxes to GNP.

The table shows that the level of personal income tax (as a percentage of GNP) in Australia is about average — excluding Sweden — and certainly not the lowest among Western countries. We are similarly about average for indirect
### Taxes as Percentage of GNP — 1968

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* approximate

**Source:** United Nations' National Accounts Statistics.

Taxes, and clearly among the top countries in the incidence of company tax relative to the GNP.

The methods of raising tax revenues should not be disregarded in comparing the tax burdens of different countries. An even more important consideration is how the money is spent. Most great tax authorities of the past were accustomed to stress that the true burden of different scales of taxation could not be properly assessed without reference to the ways in which the taxes were used. Dr. Hugh Dalton, a former Labour Chancellor of the Exchequer, in a well-known text-book on public finance, said that the benefit of services rendered to individual taxpayers was equally as important as "ability to pay" in assessing the equitable distribution of the direct money burden of taxation. The modern school of economists with their emphasis on economic aggregates seem to have lost sight of this fundamental principle. Admittedly, Dalton and other authorities were here concerned with the distribution of the tax burden as between sections of the same community. The same principle must, however, clearly apply when endeavouring to assess the comparative burden on their peoples of the tax systems of different countries.

A high proportion of tax revenues may be expended in a manner which has no immediate impact on the standard of living of the community, considered as a whole. On the other hand, a large part of the tax yield may be spent in ways which involve quite a substantial sacrifice in current living standards. Social security taxes or contributions are clearly in the first category. Expenditures on capital works, particularly works needed to absorb large additions to the population, are equally clearly in the second. The real burden on the community of social security taxes is obviously far lighter than those taxes which are raised for the purposes of financing outlays on public projects. This crucial distinction has been consistently ignored by practically all economists and press commentators in comparisons of the burden of taxes in different countries.

The table above shows that social contributions — usually on a flat rate basis — are the major reason for the high ratio of total taxes to GNP in many overseas countries. In these countries a large part of tax collections is spent on the provision of more or less immediate improvements in the standard of living of the retired, the young and the other major recipients of government services and
benefits. In Sweden, for example, social service benefits and education take about half of all taxes — a far greater proportion than any other country. The scale of social service benefits in Sweden is certainly the highest in the Western world — there is no means test — and education is entirely a State function.

In Western Germany all workers are guaranteed 75 per cent of their most recent earnings on retirement. This pension is automatically increased after retirement in step with subsequent movements of an index of average earnings. In addition to the high level of cash benefits, the German Government also pays heavy subsidies (financed out of taxation) to keep down the prices of home-produced farm products to the consumer. If the cost of these subsidies is added to the social security payments and the total deducted from all tax collections the tax burden falls from 36½ per cent to 21 per cent of GNP. In France the situation is similar. After deducting social security payments and subsidies, the tax burden is reduced from 37½ to 18 per cent of GNP. If the same principle were applied to Australia (i.e. deducting the tax revenue applied to social service payments) the tax burden would fall from 28 per cent to 21 per cent — about the same as Germany but above France.

In Australia, there is an entirely different approach to social welfare from most other Western countries where the State has become supreme in about the entire range of social services, including health, education and housing as well as cash benefits. In Australia quite a large part of retirement benefits, medical and other social welfare services, about 20 per cent of education expenditures, and about 95 per cent of housing expenditures are left to the disposition of the individual rather than that of a paternal State. The private provision that many people make for services such as these could be regarded, in effect, as the equivalent of social welfare taxes paid in other countries.

When considering the burden of taxation, moneys raised to finance current welfare are of a very different order from taxes spent on capital works, most of which take many years to complete and yield their benefits. The former represent no immediate subtraction from the standard of living of the community taken as a whole; the latter clearly impinge on current living standards, especially where they mainly arise from a rate of population growth, unique in the Western world.

In Australia 30 per cent of taxes go to education and social welfare. Another 30 per cent are spent on public works. In fact, over 90 per cent of the entire cost of capital works in Australia is financed by the taxpayer. In this respect there is a marked contrast between Australia and overseas countries and one of great significance for the economic analyst. It has, however, so far as we know, been ignored in discussions of economic policy at both official and unofficial levels. Over the past decade government capital expenditures have averaged nearly 10 per cent of GNP in Australia compared with only 2 to 4 per cent in most other Western countries. The capital component of Australian public expenditure is also easily the highest in the Western world — about 33 per cent, compared with 21 per cent in the United Kingdom, 20 per cent in France and 19 per cent in Canada. A major reason for this difference is the migration programme. Estimates by Dr. Max Neutze, Australian National University suggest that over a quarter of all fixed capital expenditure by governments in Australia is directly attributable to the cost of servicing migrants. The average Australian is thus paying a higher proportion of his income to the government in direct taxes than any other country except Sweden and is getting back less in current benefits than the people of any other Western nation.

Another flaw in aggregate tax comparisons (apart from the way the money is
spent) is that they take no account of the differing levels of real income or standards of living in the various countries. This is clearly seen by reference to the incomes of individuals. A man with an income of $20,000 a year can be taxed at an average rate of 50 per cent and still be left with a net income of $10,000. But if a man with an income of $5,000 a year is taxed at 50 per cent, he would be left with a mere $2,500. It doesn’t need much imagination to see that the burden on the second man is far greater than on the first. This factor is of particular importance when comparing the tax burden in the United States with that in other countries.

The Commonwealth tax inquiry will no doubt be studying the increasing tendency in modern tax systems to shift the incidence from direct taxes on income to indirect taxation: for example, by the introduction of the Value Added Tax, as a major part of their tax systems, in the European Common Market countries and now Britain. In the past this policy has been strongly opposed on the grounds that it penalises the lower incomes and is regressive, thus offending against the principle of equity. However, it has been argued recently that such taxes represent a heavier burden on the higher income earners who spend much more than the lower incomes on those commodities likely to draw the lion’s share of indirect taxation. Today less than two-fifths of consumer expenditure is devoted to household essentials such as food and housing, which are either exempt or lightly taxed.

The principle of taxing spending rather than income is also claimed to have less adverse effects on enterprise and work and thus on progress in the community’s living standards. Where income taxes are exceptionally heavy, as is the case in Australia, those who do the most important work of the community are unduly penalised, and particularly those with little capital compared with those who, for various reasons, possess substantial capital resources. Where taxes on incentives tend to be punitive, shrewd people will seek out ways of tax avoidance. This is easier for people with capital resources than for the majority and offends against the principles of equity and fairness which should be the hallmark of a good tax system.

Another great question the inquiry will need to answer is how much of the community’s income can be appropriated by public authorities through taxation without giving rise to a serious in-built bias towards inflation. Years ago Dr. Colin Clark put the figure at 25 per cent of the national income. In Australia and most other Western countries it is now over 30 per cent. He has yet to be proved wrong.

Because of continuing inflation, there is a massive movement of people, almost every year, into higher tax brackets. Twenty years ago when the present scale of progressive taxation was set, $7,500 a year was a relatively high income enjoyed only by executives and professional men near the peak of their careers; a marginal tax rate of 44 cents in the $ may have been defensible. But this no longer applies. Today $7,500 is barely the salary of the younger, middle-income manager or senior supervisor. The average male wage and salary earner (now on $5,000 a year) with a wife and two children pays away 16 per cent of his income in tax, compared with only 4 per cent twenty years ago. In 1968/9 the $4,000-8,000 income bracket paid $858 million in taxes, in 1958/9 a mere $140 million.

The tax cuts in the 1970/71 budget (10 per cent on all incomes below $10,000 a year and progressively diminishing thereafter on income up to $32,000) did something to rectify this situation. Unfortunately, policy attitudes seemed to change in 1971/2 when tax
Inquiry into Taxes (continued)

rates were again increased. With rapid inflation and sharp wage and salary rises, virtually all the concessions gained in 1970/71 by middle and upper-middle income earners have been lost.

Present company tax rates of 47½ cents in the $ on public company profits (42½ cents on private company profits over $10,000) have been steadily creeping up since 1955 when public company rates were 35 cents (private 30 cents). Some relief seems indicated here, particularly on private companies which are also obliged to pay an additional 50 cents in the $ on retained profits unless they distribute up to half of their income to shareholders.

Hailed as an instant spur for production, profits and employment, the revolutionary British budget introduced last April should provide the inquiry with ammunition to support a swing away from excessive taxation on effort and thrift. Income tax rates have been cut substantially (mainly through higher personal allowances) and also on small companies earning less than $30,000 a year. The loss of revenue is partly to be made good (as from 1973) by a Value Added Tax on all domestic spending other than food, fuel, fares, petrol and new buildings. Crushing estate duties are to be replaced by an inheritance tax assessed according to individual bequests to legatees and not the total value of the estate as hitherto.

Finally, there is the dilemma of how to curb government expenditure and hence taxation in the face of demographic, social, environmental, economic and political considerations all pointing in the direction of greater expenditures.
The Treasury Paper on Overseas Investment

The Treasury Paper is unlikely, of itself, to lead to any major alterations to present policies on overseas investment. If significant changes are made they will have their source in political rather than in economic motives: their object would be to gain political advantage from the prevailing public sentiment towards foreign investment. Narrow national pride and ignorance of the bigger issues are the main reasons behind hostile attitudes.

When the Treasury published its White Paper on Overseas Investment in 1965, the main question disturbing the public mind was the eventual effect of unrestricted capital inflow on the balance of payments. This was the chief consideration, for instance, in the thinking of the Vernon Committee. It was feared that the cost of servicing overseas investment would impose an increasing and eventually menacing burden on the external payments' position. The 1965 White Paper argued that these fears were unwarranted because they stemmed largely from failure to take account of the huge addition to exports (and, to a less extent, the import replacement) which would result from the investment of foreign capital, particularly in the resources field. Today, with overseas reserves in an embarrassingly healthy state, little is heard about the threat to the balance of payments and the focus of public attention has shifted to other aspects, particularly increasing overseas ownership and control.

The new Treasury Paper has been criticised on the grounds that it avoids giving definite answers to crucial questions and refrains from making positive policy recommendations. However, a careful study of the final chapter (Chapter 6) of the Report — and it does need careful study — should leave only minor doubts where the Treasury stands on the major issues. These issues are:

1. The destabilising effects of certain types of capital inflow on domestic economic management.
2. The problems posed by exchange rate speculation.
3. The increase in foreign ownership and control.
4. Overseas take-overs.
5. The effects on the balance of payments.

On the first issue the Treasury Paper points out that large inflows of capital funds, such as have occurred in recent years, can lead to an increase in bank deposits and liquidity in Australia and thus to an expansion in demand and economic activity. Moreover, this could take place at a time when, for reasons of internal economic management, the authorities were endeavouring to pursue a restrictive monetary policy. The purposes of domestic policy could thus be frustrated. The Report recognizes this danger, but says that despite the size of capital flows in recent years, they have not, because of a certain conjuncture of circumstances, “represented a significant impediment to the execution of policy”.
Should the effect of these capital movements run counter to the purposes of internal monetary management, the Treasury favours action to avert or control the flows rather than measures to offset their effects after the event.

These problems, as well as the vexed question of foreign take-overs, would clearly be exacerbated by an undervalued exchange rate. The Treasury insists, in several places, that it is essential "for any country to get its exchange rate right". This does not mean, however, that a country should yield to speculative pressures arising from the mere existence of a healthy state of overseas reserves, where the exchange rate is already appropriate.

The third issue, foreign ownership and control, is the most highly charged because it is tied up closely with nationalistic emotions. The Paper seems to leave little doubt where the Treasury stands. After pointing out that foreign ownership of companies has risen from 20 per cent in 1948/9 to around 35 per cent in 1970/71 (measured by company income payable abroad as a proportion of total company income), the Paper says, "from a purely economic viewpoint such a rise in the ownership ratio need not pose any threat".

The Paper generally rejects the contention that policies of overseas companies seriously conflict with Australia's national interests. Criticisms frequently heard are that management opportunities for Australians are limited because the top jobs are reserved for expatriates from the parent company; that production and exports can be curtailed to suit the global strategies of multi-national corporations; that purchasing policies may discriminate in favour of the parent company's country; and that research and development is carried out at headquarters so limiting these activities in Australia.

The Paper states that management opportunities for Australians appear to have been greatly expanded by the establishment of overseas-owned enterprises. On restriction of exports, it says, "As far as it is possible to tell franchise limitations are not nowadays inhibiting unduly the exports of foreign-affiliated companies". The Paper states that there is no conclusive evidence that United States' subsidiaries discriminate against Australian suppliers in their purchasing. On research and development it concludes, "A recent survey of research activity in Australia indicated that overseas companies . . . undertake more research and development work (in Australia) than locally owned companies".

While conceding that non-economic considerations and nationalistic aspirations may weigh heavily with governments and the Australian people, the Paper points out, astutely, that constraints on the expansion of foreign ownership could detract from the pursuit of other aims and policies which themselves may arise from national sentiment. The Treasury considers, and virtually rejects, the solution to increasing foreign ownership and control, frequently proposed, of providing for a minimum local equity participation. The Paper points out that this may only result in spreading Australian equity more thinly over a wider number of companies and not increase it in total. It also states that a minimum equity requirement may have little effect on overseas control because it would not necessarily mean that local investors acquire an effective voice in the running of the enterprise. The reduction of the growth of foreign ownership and control may also detract from the benefits to the Australian economy arising from the acquisition of new technology and managerial know-how. The Paper further notes that greater local participation might result, paradoxically, in tighter export franchises.

On the matter of take-overs, the Treasury concedes that they do appear to generate strong hostility on non-economic grounds. However, it reaches the conclusion that whether or not take-overs
run counter to Australia's economic interests depends on the circumstances of each case. This may suggest that the right policy — and the one that seems about to be followed in Canada — is that government approval should be sought for all take-overs of any significance.

On the fifth issue, the effects of capital inflow on the balance of payments, the Paper concludes "there seems little reason to expect any problems of a purely balance of payments kind to emanate over time from the continuing large-scale inflow of capital from abroad".

The special value of the Treasury Paper is that by helping to clarify these issues, in their economic aspects at least, it leaves little excuse for misplaced or short-sighted judgements which could harm the economy. However, the immediate impact of the Paper on public thinking may be less than its authors no doubt hope. The Paper is essentially an esoteric work of reference rather than a succinct statement of the issues for the layman. Only a small number of people are likely to read it in its entirety, and an even smaller number may be prepared to give it the painstaking study necessary to its understanding. The Paper has the serious disadvantage of being difficult to read, not only because of its exceptional length, but also because of the obvious concern of the authors to achieve a full and accurate expression of the complex technical intricacies of the subject matter. This they have done, for the most part, admirably. Most, although not all aspects of foreign investment, are explored with superb intellectual acuity and insight.

While the Treasury Paper studiously avoids the making of definite policy recommendations, it nevertheless leaves no doubt where the Department stands on the over-riding issue. On economic grounds at any rate, the Treasury experts would clearly view with disfavour any radical interference with the free flow of overseas funds into this country. In this they are undoubtedly right. There is no shadow of doubt that the inflow of overseas capital — along with the technical and managerial know-how accompanying it — has made a major and indispensable contribution to the development of Australia over the last two decades, and to the fact that the Australian economy is now so well equipped to face the future. Indeed, without that contribution much of this development would clearly not have been possible; one hesitates, indeed, to contemplate the backward, primitive state of the economy in its absence. For one thing, the great immigration programme could not have been carried through. For another, the massive and rapid development of our rich mineral wealth since the mid 1960's, which has now become the essential lynchpin of the economy, could not have occurred.

Opponents of overseas capital are accustomed to ignore these momentous considerations. They also frequently compare Australian policies towards foreign investment with policies in other countries such as Japan and France whose situations bear no similarity with that of Australia.

There is an interesting parallel in Canada. At the beginning of the 1960's the greatest issue exercising the Canadian mind was the increasing ownership and control of the Canadian economy by the United States. There were widespread demands that strong measures should be taken to halt the invasion. Ten years later, after numerous reports and inquiries, little has been done, basically because, when the chips were down, it was seen that any strong restrictive action would have dire consequences for the development of the Canadian economy: all this in spite of the fact that the extent of overseas interest in the economy was somewhere about twice as great as that in Australia and that this interest was
dominated by one country, the United States. Admittedly, the Treasury Paper indicates that, very recently, steps have been taken to provide for a greater degree of local control. But the reforms do not appear to be of a very far-reaching nature; the most important one involves a closer scrutiny of foreign take-overs.

The over-riding criterion by which overseas investment should be judged is the contribution it makes to the standards of living and the welfare of the great mass of ordinary Australians. The question of who owns the shares in this company or that, weighed against this criterion, is not of great significance. Shareholders are, after all, a peculiarly self-centred breed, concerned almost exclusively with their own personal financial advantage. Certainly the majority have little if any feelings of loyalty to the institutions in which they invest. Nor are they greatly concerned with questions of national pride. They will sell out their shares just as eagerly to overseas as to local buyers if there is a good profit to be gained. The majority of shareholders take remarkably little interest in the appointment of those who represent them on Boards of Directors. Only when they feel that the company in which they have an interest has been woefully mismanaged do they attend annual meetings — and not always then.

Thus it seems rather hypocritical and inconsistent for Australians to deplore the fact that the proportion of foreign ownership is increasing. In any case this is virtually inevitable in a young country with unusual opportunities for rapid development.

It is, of course, certain that, on occasions, Australian public opinion will be outraged by some particular manifestation of foreign investment — it may be a take-over of a modest and apparently efficiently run local enterprise by an overseas giant, or the unduly high profits of an overseas-owned company. However, we should not allow our natural vexation at such instances to distort our judgement on the overall balance of advantage of the economics of overseas capital.

Few things in life are, after all, an undiluted good: with most there are offsetting disadvantages to be weighed against the benefits. The crucial question is whether the benefits on balance outweigh the costs. While we should try to maximise the benefits and minimise the costs, it is surely a mistaken idea to imagine that we can have the best of all worlds.

Some of the most heated opposition to overseas investment has come — in the past at any rate — from various business interests. Essentially this opposition derives from the belief that increasing foreign participation in the Australian economy reduces the opportunities open to Australian business either in the establishment of new enterprises or the expansion of existing ones. In fact, for the most part, the exact opposite is the case. The vast influx of foreign capital over the last 20 years has enormously expanded business opportunities for Australian enterprises, big and small. This has occurred not only directly for firms engaged in the constructional field or in the supply of equipment and materials required by overseas controlled enterprises but also, indirectly, by the very fact that the economy has expanded at a far greater rate than would otherwise have been possible.

In 1948 when General Motors-Holden launched the Holden car it had 7,500 employees and a payroll of $8 million. Since then $324 million has been spent on land and buildings, plant and equipment, much of it locally. The number of employees has grown to 26,000, payrolls to $123 million a year, and payments to suppliers to $260 million a year. G.M.H. buys from over 3,000 Australian-owned firms, many of which did not exist or were small backyard concerns thirty years ago. G.M.H. exports have grown
from nil in 1948 to over $40 million a year. Total employment in the motor vehicle industry, excluding General Motors, has risen from 50,000 in 1947/8 to 150,000 and the number of factories in the industry from 5,000 to over 15,000. In 1971, the company paid dividends approaching $20 million, about half of its export income.

Another substantially overseas owned concern, Hamersley Iron, has spent $450 million (up to 1971) with Australian firms on capital works and expects at least 70 per cent of its $150 million export income (in 1971) to be retained in Australia through payments to employees and local suppliers and shareholders.

Perhaps the most serious omission of the Treasury Paper is its failure to attempt any broad assessment of the immense secondary benefits of overseas investment to the internal economy and to business opportunities for Australians.

Of all countries, Australia, because of its geographical immensity, its small population, its dependence on highly capital-intensive resource industries, its need to take advantage of world technological developments, is probably the least suited to adopt restrictive and self-centred attitudes towards overseas capital. If we were to satisfy sentiments of narrow national pride by imposing severe constraints on foreign investment we would surely be cutting off our nose to spite our face. In any case, where does true national pride lie: in retaining an overwhelming preponderance of local ownership and control, with all that would mean in terms of retarded growth, lower living standards, and a much weaker and more insecure economy? Or the reverse?

**APPENDIX — FACTS ABOUT FOREIGN INVESTMENT**

I. **ANNUAL RATE OF OVERSEAS INVESTMENT IN COMPANIES IN AUSTRALIA 1947/8 TO 1970/1**

<table>
<thead>
<tr>
<th></th>
<th>Undistributed Profits</th>
<th>Direct Investment</th>
<th>Portfolio Investment and Institutional Loans</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$ million</td>
<td>$ million</td>
<td>$ million</td>
<td>$ million</td>
</tr>
<tr>
<td>1947/8 to 1951/2</td>
<td>15</td>
<td>43</td>
<td>3</td>
<td>61</td>
</tr>
<tr>
<td>1952/3 to 1956/7</td>
<td>33</td>
<td>46</td>
<td>5</td>
<td>84</td>
</tr>
<tr>
<td>1957/8 to 1961/2</td>
<td>52</td>
<td>79</td>
<td>30</td>
<td>161</td>
</tr>
<tr>
<td>1962/3 to 1966/7</td>
<td>61</td>
<td>157</td>
<td>52</td>
<td>270</td>
</tr>
<tr>
<td>1967/8</td>
<td>229</td>
<td>315</td>
<td>417</td>
<td>961</td>
</tr>
<tr>
<td>1968/9</td>
<td>280</td>
<td>339</td>
<td>402</td>
<td>1021</td>
</tr>
<tr>
<td>1969/70</td>
<td>295</td>
<td>445</td>
<td>285</td>
<td>1025</td>
</tr>
<tr>
<td>1970/1</td>
<td>322</td>
<td>655</td>
<td>516</td>
<td>1493</td>
</tr>
<tr>
<td>1947/8 to 1970/1</td>
<td>115</td>
<td>208</td>
<td>105</td>
<td>428</td>
</tr>
<tr>
<td>Percent of Total</td>
<td>26.8</td>
<td>48.7</td>
<td>24.5</td>
<td>100.0</td>
</tr>
</tbody>
</table>

**WHERE THE MONEY COMES FROM**

II. **ANNUAL RATE OF INFLOW OF PRIVATE INVESTMENT 1947/8 TO 1970/1**

<table>
<thead>
<tr>
<th></th>
<th>$ million</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>United Kingdom</td>
<td>190</td>
<td>44.4</td>
</tr>
<tr>
<td>U.S.A. and Canada</td>
<td>166</td>
<td>38.9</td>
</tr>
<tr>
<td>Other</td>
<td>72</td>
<td>16.7</td>
</tr>
<tr>
<td>Total</td>
<td>428</td>
<td>100.0</td>
</tr>
</tbody>
</table>
WHERE THE MONEY GOES

III. INDUSTRY (INCLUDING UNDISTRIBUTED PROFITS) 1970/1

<table>
<thead>
<tr>
<th>Industry</th>
<th>$ million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mining and Oil Exploration, etc.</td>
<td>339</td>
</tr>
<tr>
<td>Metal Industries</td>
<td>119</td>
</tr>
<tr>
<td>Oil Refining and Chemicals</td>
<td>56</td>
</tr>
<tr>
<td>Other Manufacturing</td>
<td>82</td>
</tr>
<tr>
<td>Finance and Property</td>
<td>196</td>
</tr>
<tr>
<td>All Other</td>
<td>185</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>977</strong></td>
</tr>
</tbody>
</table>

IV. OVERSEAS CONTROL

In manufacturing, overseas interests control 4 per cent of factories which produce over a quarter of all production and employ a fifth of all factory employees.

V. INVESTMENT INCOME PAYABLE ABROAD 1964/5 TO 1970/1

<table>
<thead>
<tr>
<th>Year</th>
<th>Undistributed Profits</th>
<th>Dividends and Interest</th>
<th>Total $ million</th>
<th>Undistributed Profits</th>
<th>Dividends and Interest</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1964/5</td>
<td>124</td>
<td>241</td>
<td>365</td>
<td>4.8</td>
<td>9.4</td>
<td>14.2</td>
</tr>
<tr>
<td>1970/1</td>
<td>322</td>
<td>439</td>
<td>761</td>
<td>7.6</td>
<td>10.5</td>
<td>18.1</td>
</tr>
</tbody>
</table>

VI. PROPORTION OF PRIVATE INVESTMENT EXPENDITURE FINANCED BY OVERSEAS CAPITAL — 1948/9 TO 1969/70

<table>
<thead>
<tr>
<th>Year</th>
<th>Per cent</th>
</tr>
</thead>
<tbody>
<tr>
<td>1948/9</td>
<td>25</td>
</tr>
<tr>
<td>1964/5</td>
<td>24</td>
</tr>
<tr>
<td>1969/70</td>
<td>31</td>
</tr>
</tbody>
</table>

VII. NET SHARE PURCHASES BY AUSTRALIAN AND OVERSEAS SHAREHOLDERS

<table>
<thead>
<tr>
<th>Year</th>
<th>Australian</th>
<th>Overseas</th>
</tr>
</thead>
<tbody>
<tr>
<td>1955/60</td>
<td>Individuals</td>
<td>$21</td>
</tr>
<tr>
<td></td>
<td>Pension Funds and Life Assurance Companies</td>
<td>$36</td>
</tr>
<tr>
<td></td>
<td>Other Corporate Investors</td>
<td>$62</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>$119</td>
</tr>
<tr>
<td></td>
<td>Overseas</td>
<td>$77</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>$196</td>
</tr>
</tbody>
</table>

Incomes Policy: 
A Red Herring

by

MICHAEL JEFFERSON

Michael Jefferson was educated at University College, Oxford and the London School of Economics. He is now Deputy Director of the Industrial Policy Group, and was previously Assistant to the Managing Director of a merchant bank and Managing Consultant with an economic consultancy.

Mr. Jefferson has written numerous articles and broadcasts upon economic affairs, although his main preoccupation is in the preparation of the Papers published by the Industrial Policy Group.

Some of the most influential men in British industry form the membership of the Industrial Policy Group which was established in 1967 to study the causes of Britain’s economic problems and to make its views public.

INTERVENTIONIST governments have two (at least) unfortunate characteristics: a desire to take responsibility for matters beyond their proper powers and competence; and constant efforts, once that responsibility is undertaken, to shift from their own shoulders the blame which rightly belongs there. Scapegoats are invented and red herrings drawn across the trail.

One area in which governments have, in recent years and in many countries, sought to extend their responsibilities and shift the blame for subsequent failure, is that of incomes policy. Governments have sought in an incomes policy the device for softening the effects of an inflation which they have deliberately created and maintained by other means.

‘Inflationary wage demands’ have become the scapegoat for governments, simultaneously increasing the money supply with absurd prodigality (at an annual rate reaching over 20 per cent in Britain in recent months). Analysis of cost-push inflation in terms of the monopoly powers of large trade unions has led, not to direct action to reduce or remove those monopoly powers, but to the prescription of an incomes policy of little relevance to the problem.

The problem, then, of incomes outpacing rises in productivity and its continuance is largely one of governments’ own making. Incomes policies as traditionally defined (incomes policy one as Gottfried Haberler would call it) will not alleviate that problem, at least not
for long. If we look at the post-war history of advanced industrial nations, we find that in spite of the many attempts to implement incomes policies none have succeeded for long, and most have had severe adverse consequences in the longer run. The most remarkable feature of all this experience, however, is the continued efforts of governments to play with the control of incomes despite their deplorable course record.

Incomes Policies Do Not Work

After 1945 great interest was shown in the maintenance of incomes policies (generally wages policies) in peacetime. Some experiments, such as Britain's in the late 1940's and in the United States during the early 1950's, collapsed ignominiously. But throughout the 1950's attention was drawn to the Netherlands and to Sweden where, it was said, incomes were regulated and inflation controlled. The first was allegedly the cause of the second. Recent surveys have shown that incomes policies have not worked successfully for long anywhere. As one study put it, the lessons of European experience have been that "no incomes policy can halt inflation; without inflation no incomes policy is necessary".

Recent American Experience

Quite apart from their failure to curb inflation effectively, incomes policies encourage governments to take more and more interventionist and self-defeating measures in an effort to save face. In the United States, for instance, Phase Two of the Nixon Administration's programme for the control of inflation has become increasingly discredited since its introduction in November 1971. The Prices Board lowered the maximum average price increase permitted for companies with $100 m. or over in annual sales from 2 per cent to 1.8 per cent in March 1972, and introduced an 8 per cent maximum ceiling for specific products. The "moral" pressure, which was exerted on companies by the Administration before the 90-day wage-price freeze of August 1971, also continues. The Chairman of the Prices Board called Bethlehem Steel's decision in April 1972 not to raise prices on most of its products "an example of responsive leadership in the nation's fight to stop inflation".

The effects of such pressure are to undermine profits, and therefore the major source for new savings and investment. Economic growth is impeded. But where the funds are available for investment purposes, there is every encouragement to go for more capital-intensive methods of production. This is particularly the case where incomes moved ahead faster than prices, which is what the U.S. Pay Board has allowed to occur, and to a degree well in excess of the 5.5 per cent pay 'standard'. Such a policy, then, is a sure prescription for raising unemployment as well as reducing profits and growth. There is a serious danger that the United States will fail to heed the warning of George Shultz, Director of the U.S. Office of Management and the Budget, that the second phase of inflation policy should not be too rigorous or exact too great a toll from the economy "to avoid pressures that stop production or distortions in the prices-wage structure and seriously impair efficiency".

The immediate reasons for the adoption of the recent prices and incomes policy in the United States do not, however, lie with the inflationary demands of union leaders or price increases by manufacturers. They lie with a dollar over-valued on the foreign exchanges, and the largely external reasons for that, as well as U.S. domestic monetary policy. And the appropriate measures to deal with those problems were a change of the dollar parity and closer control of the money supply. The incomes policy was and is a red herring, and unionists and manufacturers were convenient scapegoats for governmental failure to adopt the appropriate monetary policy and desire to maintain an unrealistic rate of exchange. As an American economist has

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observed:

“During the late 1950’s and in the last few years, the economy has experienced lagged inflation. Conceptually all an incomes policy can do, therefore, is to delay a lagged inflation further. If this analysis is correct, the effect of the wage-price freeze and of the subsequent stage II will be to postpone price rises which would have taken place earlier. Eventually when controls are lifted, prices will rise to their equilibrium level”.

**Experience in Britain: 1948-1964**

Recent American experience is all too familiar to those of us in Britain. Throughout the period since 1945 both Labour and Conservative governments have appealed for restraint of wage demands. The joint restraint of wages and dividends, under Sir Stafford Cripps in 1948 resulted in the restraint of dividends, whereas wage rates rose more rapidly during the year of restraint than they had done in the previous year. And little more was heard of such experiments for a decade.

But the seeds of decay had already been sown, for in August 1957 the (Cohen) Council on Prices, Productivity and Incomes had been appointed. In 1958 it produced an excellent First Report, in which reference was made to the suggestion that from time to time a percentage figure should be announced by which average money wages could increase during the year without damage to the national interest. The Council stressed the serious practical objections to such a proposal, and continued:

“There would always be industries in which there were good reasons for the advance in wages to exceed the average; others in which much less good reasons for it to do so could be thought up; very few in which the case for lagging behind the average would be readily conceded”.

Recent months have demonstrated the wisdom of that view. Regrettably, subsequent changes in the Membership of the Council (notably the resignation of Sir Dennis Robertson) coincided with a decline in the quality of the Reports produced. They were finally to point the way to price and income controls and “indicative” planning. The National Economic Development Council, set up in 1961, rapidly went further along the same road. There will be a need, the Council wrote in a 1963 Report: “for policies to ensure that money incomes (wages, salaries, profits) as a whole rise substantially less rapidly than in the past”.

Again, as in 1948, profits have been restrained while wages and salaries have risen rapidly in money terms. During the 1960’s the share of profits in Britain’s national income steadily declined. In manufacturing industry income from employment almost doubled; total net profits increased by less than one-fifth. As a proportion of income from employment, net profits declined in consequence from approximately one-third to under one-fifth. Such movements are an important factor in explaining Britain’s low rate of economic growth in recent years. As a recent study put it:

“Thus, in times of crisis, the plea for economic restraint or sacrifice invariably goes along with a stern demand for the control or restriction of profits, even though the lack of profits may lie at the very heart of the crisis — tantamount to throwing away the lifebuoys in order to lighten the ship”.

**Experience in Britain — 1964-1969**

To return to our historical narrative, however. The incoming Labour Government in October 1964 offered an unprecedented degree of collaboration with organised management and labour in formulating economic policy, and hoped that this would ensure voluntary co-operation on prices and incomes as a condition for accelerated economic growth. The expression of this hope was the Joint Statement of Intent on Productivity, Prices and Incomes of December 1964, signed by representatives of Government, employers’ organisations and the Trades Union Congress. The signatories undertook to give “effective shape to the machinery that the Government intend to establish for the purpose of keeping under review the general movement of prices and of money incomes of all
kinds”. The following year saw the most rapid rise of wage rates and money earnings there had been since 1945.

As a result of the Joint Statement, the National Board for Prices and Incomes was set up in April 1965. For the first fifteen months a voluntary policy was in operation, under which the parties concerned were free to accept or reject the Board’s findings. But from July 1966 the policy was imposed with increasing severity and degrees of compulsion, and accompanied by swingeing fiscal and monetary measures as well as irritating erosions of personal liberty (such as a £50 Travel Allowance), in an effort to maintain the parity of an over-valued pound sterling. The policy was continued until the end of 1969, but the prospect of a General Election, the inflationary effects of devaluation, and the growing bitterness of relations between some Government Ministers and union officials encouraged its abandonment.

How far the National Board for Prices and Incomes should be blamed for the failure of the prices and incomes policy of the late 1960’s is open to dispute. Some observers have cogently argued that the Board was largely by-passed as far as its control function was concerned, since only some national wage agreements in excess of the norm and hardly any local agreements were referred to the Board. But since the imposition of the prices and incomes policy between 1965 and 1969 bears some of the blame for the subsequent rapid inflation, it is possible to be more definite about the policy as a whole than is sometimes argued.

Econometric studies of the effects of the policy have produced varying conclusions, and all have been based on provisional and debatable techniques of analysis. Those with the greatest interest in demonstrating the policy’s success put a low figure on its effect. The Chairman of the Board, Aubrey Jones, stated: “our own econometric studies would lead us to believe that, by virtue of the existence of the policy over the last few years, the average annual increase in earnings has been about 1% less than it otherwise would have been”. John Corina believed the effect had been “rather more than 1 per cent a year” although the policy had “clearly not worked in the sense that earnings rose persistently in excess of norms and productivity estimates”. But Aubrey Jones warned that “I would not myself be disposed to attach undue credence to this or any other figures”.

The fundamental criticism of the prices and incomes policy operating between 1965 and 1969 was, however, that it introduced an arbitrary element into the determination of prices and incomes. The longer the policy was imposed and the more severe it became, the more likely it was to be called in to correct distortions of its own making. And its logical end was central economic planning on a comprehensive scale.

Another criticism was that, although after taking taxation payments and welfare benefits into account Socialists could take comfort in the greater equality of income distribution, lower paid workers and those on fixed incomes saw their earnings suffer in relation to higher paid and more strongly unionised employees. In the first four years of the policy the lowest paid industrial workers fared rather better than the average, but the marked increase in earnings of the top 50 per cent of industrial workers in the year to April 1970 reversed this result for the period as a whole. And the National Board for Prices and Incomes itself pointed out that “those not covered by collective bargaining arrangements were losing ground relatively”.

Experience in Britain since 1964

These changes in 1969 were, according to one leading study, “a new and unforeseen development”. The close relationship between increases in earnings and levels of unemployment (enshrined in the ‘Phillips Curve’) no longer seemed
to exist. Social security benefits for the unemployed and for strikers and their families, much increased and extended in 1966, indirectly exerted an inflationary pressure. The effects of devaluation also began to work their way through to prices. But, according to Professor Paish, about 80 per cent of the difference between expected and actual rises in employment incomes by late 1970 "must be ascribed wholly to 'cost-push' — the use of monopoly power by trade unions and shop-stewards." Subsequent events have deepened and confirmed this view.

The Conservative Government, faced with the legacy of strong inflation bequeathed them by the outgoing Labour Administration (whose inflationary pay settlements with public service employees in the autumn of 1969 and rapid increases in the money supply shortly before the General Election stoked up the inflationary pressures already present), attempted to bring down the rate of inflation by controlling public sector pay increases and "jawboning" private employees. This policy appeared to be working reasonably well, particularly in relation to the weak handling of other industrial matters, until the coal dispute early in 1972. But the specious arguments (particularly the so-called "adjustment factor") and inflationary recommendations of the Wilberforce Committee of Inquiry into the coal dispute has left the way open for more inflationary settlements and a reversal of the downward trend in prices.

The success of the Government's policy was also greatly assisted by the voluntary price restraint agreed by members of the Confederation of British Industry. But the dangers of such a policy, if persisted with for long, were also pointed out by industrialists. For where price controls are effective but costs, particularly wage costs, continue to rise the consequences can be serious. By throttling down profit margins, such a policy strikes at the very roots of effective investment and economic growth.

Incomes Policies Are Irrelevant

In spite of, perhaps because of, the serious inflationary pressures from which Britain is now suffering, the desirability of an incomes policy as traditionally conceived is even less obvious than in earlier years.

Some foreign commentators do not believe that Britain has had an incomes policy in recent years, since only symptoms have been treated rather than causes. Aubrey Jones, as Chairman of the National Board for Prices and Incomes, was regarded as "an overworked and harassed doctor prescribing quack medicines". There is much truth in this view, and it has led to closer attention being paid to the need for treating causes.

Gottfried Haberler has recommended what he terms incomes policy two: "an assortment of specialised measures designed to eliminate monopolistic restrictions and market imperfections in different sectors of the economy and thereby to improve the performance of a flexible, competitive free-market economy". He argues, in my view correctly, that it is not sufficient merely for governments to conduct their monetary and fiscal policy in such a way as to avoid or minimise inflation and offset inflationary wage increases. In Britain, at least, we have reached the point where, as the Chancellor of the Exchequer recently put it, the British public are being blackmailed by monopoly union power intent upon exploiting its advantage to the full. Whereas wage-bargaining has traditionally been conceived of as negotiation between two parties in reasonable balance, no such balance any longer exists in important sectors of British industry. The monopoly power of trade unions must therefore be tackled directly, perhaps on an ad hoc basis where this power is being unduly exploited in the view of an independent tribunal. National wage bargaining may have to be superseded by plant bargaining, with penalties for "leap-
frogging" where this can be shown to have occurred and has been imposed by external monopolistic pressures. And welfare benefits for strikers and their families, where the strike is found to be part of the undue exploitation of union power by the independent tribunal, should no longer be available.

It may be objected that such proposals are a serious threat to the continued existence of the trade union movement in Britain. In recent weeks the more militant unionists in Britain have been reminding us that the first thing the Nazis did on coming to power was to destroy the trade union movement. Neither the objection nor the analogy bear close examination. Within proper bounds, I am a passionate supporter of a vigorous trade union movement. However, it is not black-shirted fascists which pose a threat to democracy, liberty and prosperity in Britain today, but red-shirted fascists. If moderate, but well-directed, measures are not taken then the danger of political extremism could arise. And these fears are not likely to be allayed by the statement of the General Secretary of the Trades Union Congress in early May 1972, that the main aim of the trade union movement was not the overthrow of a democratically elected Government.

**Conclusion**

An increasing body of opinion would agree with Professor Hayek that the chief obstacle (there are many others) to the functioning of the market economy and the effectiveness of the price mechanism is trade union monopoly. There seems no good reason to disagree with the conclusions of two academic economists that:

"incomes policies in the past have not been successful in reducing wage inflation. The causes of the failure, rooted in the complexity of the labour market, have not disappeared, and it is unlikely that the imposition of an incomes policy currently would be more successful or have fewer costs than past attempts".

What is required is the treatment of causes, whereas the conventional incomes policy has always treated symptoms. And since the analysis and results of incomes policies in different countries broadly conform with each other, there seems no reason why Australia should be an exception to the general rule that incomes policies are a red-herring diverting attention from the true causes and cures of inflation, low productivity, and poor economic growth.

Mr. Jefferson has expressed his personal views. They do not necessarily represent the views of the Industrial Policy Group or those of its individual Members.