POLICY FOR INFLATION

THE following comprises the full text of a policy to cope with inflation prepared by the Editorial Committee of the I.P.A. It was issued to the Australian press on September 30, 1950, *and was published by various daily newspapers in more or less abbreviated form. The policy is now reprinted here in full in order to provide a permanent record of the Editorial Committee's views on the measures necessary to arrest inflation at the time the policy was prepared. While the statement represents the majority opinion of the members of the Editorial Committee, it does not necessarily represent the views of individual members of the Institute's Council.*

1. There is mounting public agitation about the rapidly declining value of the Australian pound. But it is necessary to recognise that the rise in prices within Australia is in part a natural and inevitable response to a world expansionary economic situation, and to economic policies being followed within Australia which are generally approved. These policies relate particularly to increasing our population through large-scale immigration and to raising the nation's productive capacity through long-range developmental programmes.

The continued rise in prices should therefore not be regarded as wholly unhealthy. Nevertheless, the position has been reached where some positive measures to bring this rise more within conscious control are essential. This necessity has been strengthened recently by the impact of two new inflationary factors; the increased expenditure on defence made imperative by the Korean war, and the record wool prices obtained at the new season's wool sales.

However the Australian people must face up frankly to the fact that it will be impossible to arrest the inflationary drift unless all sections are prepared to accept the necessary disciplines and sacrifices involved. Any national programme designed to achieve this end must aim at imposing these disciplines as equitably as possible among the different sections of the community. It must be remembered that the sacrifices required will be as nothing to the toll which will be exacted should the inflationary trend get out of control.

2. An effective policy to arrest inflation must have regard to the basic causes. Inflation occurs when the pressure of demand for finished and semi-finished goods, raw materials, capital equipment and labour is too great to be met from the prevailing levels of production and supply. There are, at present, three main sources of this excess pressure.

(a) The high level of export income brought about by extraordinarily high prices for Australia's main exports, particularly wool. High export incomes give rise, by a cumulative process, to heavy spending throughout the Australian economy. Rising world prices for export commodities mean in general high prices for the proportion of these commodities consumed in Australia.

(b) The abnormally heavy investment programmes of both private industry and governmental authorities. Governments on top of their normal capital expenditures are engaged in vast developmental projects and on heavy commitments for defence, while private industry is endeavouring to expand its productive capacity at a rate unprecedented in Australian history. The fact that there is insufficient production of essential materials and equipment and inadequate resources of labour to satisfy all these investment projects is leading to competitive bidding for the short supplies with higher prices and high labour costs. The large discrepancy between award and actual wage rates is clear evidence of this inflationary pressure. The crux of the inflationary situation at present probably

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lies in over-investment in relation to the current artificially restricted level of production.

(c) Rising internal costs of production brought about by rising prices for imported materials and by higher money incomes—particularly wages as a consequence of increases in margins and of cost-of-living adjustments.

These three causes, of course, are closely inter-related.

3. In order to meet this situation we propose the following measures: (These measures are supplementary, one to the other, and have been designed to distribute, so far as possible, the burden of controlling or correcting inflation equitably between the main economic groups of the community).

i. The Australian £ to be appreciated by 10%.* This would mean that £112½ (Aust.) would equal £100 (sterling), compared with the present position where £125 (Aust.) equals £100 (sterling). The broad effect of this measure could be to reduce export incomes and import prices (in Australian £s) by something of the order of 10%. The former would tend to reduce the pressure of spending throughout the economy; the latter, which would mean lower prices for imported raw materials and capital equipment, would tend to reduce Australian costs and thus selling prices. Moreover, once the external value of the Australian £ had been definitely fixed, the large flow of "hot money" entering Australia for speculative investment purposes (estimated by the Commonwealth Bank to total £300m.), would abate and some of it might possibly be withdrawn. This "hot money" is an aggrava-

*** IMPORTANT—This recommendation comprised one part only of an inter-related plan, an essential feature of which was a strong effort directed toward the stabilisation of internal costs (See point X). Subsequent to the publication of the plan on the 30th September the decision of the Commonwealth Arbitration Court in the basic wage case has overthrown any possibility of the immediate stabilisation of internal costs. For the time being then, and at least until the full effects of the wage increase are clear, an appreciation of the exchange should not be considered.**

ting factor in the investment boom in the exchange and property markets, and appreciation of the £ would therefore help to introduce stability into these markets.

An appreciation of the £ of these proportions should not be seriously injurious to most sections of the economy and may serve to inject a desirable measure of increased competition. Insofar as some special sections might be over-severely affected, they could be assisted by subsidies, tariff adjustments, or by other means.

ii. The above measure would cut possibly 10% off all export income (in Australian £s), but this would not be sufficient with wool receipts. These should be treated as a special case. In order to "freeze" temporarily a proportion of these receipts, an adequate wool equalisation scheme should be established.

iii. To prevent the influence of abnormal world prices for wool entering into the cost of local woollens a subsidy should be paid to the local manufacturer sufficient to enable him to maintain his selling prices at around present levels. This should be financed out of consolidated revenue.

iv. There should definitely be no budget deficit in the current financial year. Indeed, in spite of its heavy commitments for defence, development, and social services the government should make every effort to achieve budgetary equilibrium. Some of the measures proposed below, particularly those directed to reducing overall investment expenditure should help toward this end.

v. The Commonwealth Government should ruthlessly cut its developmental programme and should confine expenditure in these fields to those projects which can expect to assist production in the more or less immediate future. Those projects of a long-range character which offer no early support to production should be postponed.

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vi. The Commonwealth Government should make an intensive effort to prune its expenditure and effect economies wherever reasonably practicable, thus setting a much-needed example of economic administration to the community.

vii. In the current financial year the Commonwealth Government should endeavour to raise the maximum possible amount of money through intensive loan campaigns. As an aid to this objective, it should institute a system of savings certificates of small denominations (say £10).

These certificates should carry the highest practicable rate of interest and the total holding of any individual should be limited. They should be launched with an intensive savings publicity campaign and the government should enlist the assistance of business concerns to encourage their employees to make small deductions from their weekly wages or salaries to be placed to their credit for the purchase of these certificates.

viii. A special "spending tax" should be placed on luxury and semi-luxury goods and services. This tax would provide increased revenue for the government, and at the same time help to curb investment in the less essential industries and thereby release resources for the expansion of essential production. The expansion of basic production is a necessary component of any plan to arrest inflation.

ix. As an emergency measure an investment authority should be constituted for the purpose of reducing the volume of private investment in non-essentials (which is a potent cause of present inflationary movement) and thus making additional resources available for the basic forms of production. As to what is and what is not "essential" this authority could be guided by the new National Resources Board which the Government proposes to establish. This authority could, for instance, assist essential private industries to obtain their capital requirements without the embarrassment occasioned by less essential industries being able to offer more attractive terms to investors. It should include one or two people of wide practical business experience. This authority should be disbanded as soon as inflation is brought under control. It would then no longer be necessary.

x. *Internal Costs.* Every effort should be made to keep rises in money incomes within strict limits. As soon as the Arbitration Court has given its judgment in the basic wage case, the Government should endeavour to reach an agreement with the trade unions to avoid unnecessary increases in wages over and above the new levels set by the Court. The unions could for instance, agree to postpone all applications, actual or pending, for marginal increases. Some agreement might also be reached about the future operation of the cost-of-living index. The Government should also endeavour to reach an official understanding with employers that they will explore every possible means of effecting price reductions and of restraining any unavoidable increases in prices to the absolute minimum. This would imply, except in special cases, no increase above prevailing dividend levels.

xi. A policy of this kind for controlling or arresting inflation could best be initiated by a national conference called by the Commonwealth Government, at which representatives of all the main economic sections of the community should be asked to attend.

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