Tasmania's No Tiger, But Why?

JEFFREY RAE

OVER the 1980s and 1990s, Tasmania's economic performance has consistently been inferior to that achieved in the rest of Australia. The shortfall in performance is significant and has occurred right across the key indicators of economic performance—economic output, productivity and investment—as well as labour market outcomes, including job creation, participation in the labour market and unemployment.

Over this period, Tasmania's relative economic performance compared with the rest of Australia has deteriorated, particularly since the recession of the early 1990s. Again, the State's slide in relative performance has been evident right across the key economic indicators.

The Tasmanian Government is making serious attempts to turn around the State's dismal economic performance. It is, however, too early to say whether the economic development initiatives that it has put in place will be able to stabilize, let alone close, the performance gap and how long it might take to do so.

HOW BADLY HAS TASMANIA PERFORMED?

Over the last two decades, Tasmania achieved only about one-third of the growth in economic output posted by the rest of the country. Moreover, the 'output gap' was even greater compared with Queensland and Western Australia, where output grew faster than the national average.[1] More recently, the 'output gap' between Tasmania and the rest of Australia has narrowed somewhat. Nevertheless, since the recession of the early 1990s the Australian economy has grown at two-and-a-half times the rate of Tasmania.[2]

The rate of growth in productivity in the Australian economy as a whole—as measured by the value of output per head of population—grew by more than one-and-a-half times that of Tasmania over the most recent economic cycle. Tasmania's performance was the worst of all the States and was even considerably worse than South Australia, the next worst performer. As the ABS has pointed out, the differences were significant.[3]

The rate of investment in Tasmania has been lower than the rest of Australia and appears to be declining. Given the critical role that investment plays in output and productivity growth, the State's investment performance suggests that the longer term prospects for the Tasmanian economy are, at best, subdued.

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Participation in the State's labour market has been lower than the rest of Australia, unemployment is higher than the rest of Australia and there has been no growth in full-time employment in the State. The few new jobs that have been created, have been part-time ones. Overall, these labour outcomes strongly suggest that the State's labour market is performing very poorly and that the impediments to better performance are both extensive and deep-seated.

The subdued and deteriorating prospects for the Tasmanian economy have encouraged increasing numbers of Tasmanians to leave the State and seek their fortunes elsewhere. Those leaving are concentrated among the State's young adults and those with tertiary qualifications—in other words, those with the potential to make the greatest contribution to the State's economic development. Those leaving the State have done so despite the fact that significant income redistribution due to Commonwealth fiscal policy has helped cushion the impact of Tasmania's poor economic record on household incomes.

Tasmania has not been an attractive place for either interstate or overseas migrants to settle permanently. Moreover, the numbers of those from outside the State who have settled permanently have not been anywhere near sufficient to offset the numbers of Tasmanian residents leaving the State. As a consequence, the State's population has been declining. The population decline is expected to continue for the foreseeable future.

WHAT'S WRONG IN THE APPLE ISLE?

There are two remarkable features of Tasmania's poor economic performance compared with the rest of Australia. The first is that its dismal performance has been evident for so long that it has acquired the well-worn status of the 'Tasmanian problem'. The second is that the causes and consequences of the 'Tasmanian problem' have been examined extensively and regularly since Federation.

Since Federation, there have been over 75 reports on the 'Tasmanian problem'.[4] The latest was a joint State–Commonwealth inquiry conducted by Peter Nixon, which reported in 1997.[5] The major inquiries before that were by Sir Nicholas Lockyer in 1926,[6] Sir Bede Callaghan in 1977,[7] the Centre for Regional Economic Analysis at the University of Tasmania in 1987 [8] and Charles Curran in 1992.[9]

All of these inquiries have pronounced adversely on the State's economic performance. All have diagnosed a common set of causes. None has led to comprehensive microeconomic reforms.

Tasmania's small size and its remote location have clearly contributed to its dismal economic performance over recent decades. That said, they are not the only causes of the 'Tasmanian problem'.

Based on a report I did recently for the New Zealand Business Roundtable, it is clear that the poor design of certain Tasmanian institutions has contributed to its dismal economic performance.[10] The Hare-Clark system of voting for the Tasmanian Lower House of Parliament tends to deliver minority government. Minority government and an Upper House generally dominated by independent members have resulted in a political reluctance to address issues no matter how urgent they became. Although a majority Government emerged from the last State election, it remains to be seen whether the recent reduction in the number of Parliamentarians in Tasmania will be enough to correct this bias over the longer haul.

Poor public policy choices have also contributed to the dismal performance of the Tasmanian economy. The bottom line is that public policy at both the State and Federal level has created an environment that is unattractive to business, even though that was never a goal of either level of government.

State regulation has generally stifled business innovation and prevented competition. Before the recent reforms by the Bacon Government, the same point could have been made about the level of State taxation. This bias is most pronounced in the environmental area. There, Tasmania has developed an image of being opposed to economic development, regardless of how well environmental impacts are, in fact, being managed. For example, the rights to object to development proposals are more generous in Tasmania than in any other Australian State.[11]

Despite generous Federal parliamentary representation, Tasmania has been unable or unwilling to prevent many Federal policies that clearly disadvantage the State.

The first example is the Commonwealth's attempt to promote industrial development through high tariffs. This policy was clearly at the expense of States such as Tasmania that were more heavily reliant on primary industries—particularly agriculture, forestry and mining.

The second example concerns Federal regulation of the labour market. The centralized system of setting wages and conditions has involved a loss of flexibility for different businesses and in different circumstances. The States with smaller and more narrowly based economies, such as Tasmania, are less able to accommodate this loss of flexibility. While there have been reforms in the Federal regime over the 1980s and 1990s, significant rigidities remain.

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The final example is cabotage—the policy of reserving coastal shipping services to vessels registered in Australia and crewed by Australian seamen. Cabotage has meant that the cost of coastal shipping services in Australia has been well above international levels. This has worked against the use of sea transport for interstate trade in those areas where Tasmania may be expected to have a competitive advantage. Given Tasmania's total reliance on shipping for moving most of its imports and exports, cabotage has had the effect of limiting Tasmania's capacity to export to both mainland Australia and the rest of the world.

WHY HASN'T THE PROBLEM BEEN ADDRESSED?

The Bacon Government has made progress on addressing some of the fundamental causes of the 'Tasmanian problem'. Since its election, the Government has moved the State budget into surplus and reduced the relative severity of State taxes compared with the other States. In this time, the State has seen some improvements in its economic performance compared with the rest of Australia, so much so that the population loss of recent years due to interstate migration has been halted, at least for the moment.

Nevertheless, much remains to be done. Most pressing is the need to reform Tasmania's regulatory burden, which has a negative effect on business and economic efficiency. This would not only have an immediate economic benefit for the residents of the State, but it would also help to counter the widespread perception that the State is opposed to economic development and activity.

Given the chronic and persistent nature of the 'Tasmanian problem', it is reasonable to ask why microeconomic reform is so long coming in Tasmania. Part of the explanation undoubtedly lies in the unique nature of the Tasmanian Parliamentary system and the political inertia it has encouraged. Such a bias, however, does not explain why the Tasmanian electorate has not demanded institutional and policy reform. It is not as if there have not been enough demonstrations of what microeconomic reform can achieve, both in the rest of Australia and elsewhere.

I have no doubt that Federal fiscal

policy has contributed to a lack of awareness in the Tasmanian electorate on the need for fundamental institutional and policy reform. There are two reasons for this.

The first reason is that the impact of Tasmania's poor economic performance on the States' households has been cushioned, to some extent, by the interplay of progressive income tax scales and targeted social welfare assistance.

Over the 1990s, the average Australian household paid more in tax than it received in social security benefits, and the gap has progressively increased to around 5 per cent of household income. In sharp contrast, the average Tasmanian household received in social security benefits about what it paid out in income tax. In other words, Tasmanian households make no significant contribution to the cost of the other Commonwealth services they receive—such as those of the Defence Force, the Federal judiciary and Commonwealth regulatory agencies—their costs are borne by the rest of the country. In round terms, the benefit to Tasmanian households is equivalent to around $500 million a year.

The second reason underlying the lack of awareness about the need for microeconomic reform is that Tasmania is the major beneficiary of the system of Commonwealth payments to the States and Territories.

Commonwealth payments to the States and Territories are an important source of revenue for all jurisdictions. These Commonwealth payments seek to address the difference in revenue-raising powers and functional responsibilities of the different levels of government. They also seek to equalize the fiscal capacities of the States to deliver services—through a process called Horizontal Fiscal Equalization (HFE). This refers to the difference, in per capita terms, between the cost to a State of providing a range of services common to all States and the financial resources available to it. Under HFE, the smaller States, such as Tasmania, receive a greater share of Commonwealth payments to the States to enable them to discharge their standard functions without having to impose above-average revenue-raising measures on their residents.

In 2002–03, it is expected that Commonwealth payments to Tasmania through the State's Consolidated Fund will comprise 68 per cent of total receipts. In contrast, the revenue raised by State's own taxes is expected to provide only 20 per cent of total receipts.[12] Were Tasmanians to have to pay the full cost of the services that are currently provided by the State Government, State tax rates would have to be increased nearly three-and-a-half times what they are at present. This underestimates the increase that would be necessary to sustain existing service levels, as it does not take into account the behavioural response that could be expected to the tax increase. Were the State to have to face up to this issue, we would find out whether Tasmanians really value the services in question more than what they cost to provide—at the moment we simply do not know the answer.

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The bottom line is that Tasmanians are getting, courtesy of the Commonwealth, substantial direct and indirect income transfers that are not dependent on the State performing well economically. The contrary is the case in fact. The extent of these mandated transfers will tend to increase, the worse the State performs. This tends to insulate Tasmanian living standards, to a significant degree, from the full impact of poor economic performance. In turn, this means that the electorate is likely to be less concerned about the contribution of poor institutional design and poor policy choices to economic performance than one would otherwise expect.

In other words, Commonwealth fiscal policy is, albeit unintentionally, a significant impediment to the Tasmanian electorate appreciating the urgency of the need for microeconomic reform in the State.

NOTES

1 Hon. Peter Nixon AO, *The Nixon Report: Tasmania into the 21st Century*, Report to the Prime Minister of Australia and the Premier of Tasmania, July 1997.
2 Australian Bureau of Statistics, *Australian National Accounts: State Accounts*, Cat. 5220.0, Canberra, 23 November 2000.
3 *Ibid*., page 3.
4 Nixon, *op. cit*.
5 *Ibid.*
6 Sir Nicholas Lockyer, *Inquiry into the Financial Position of Tasmania*, April 1926.
7 Sir Bede Callaghan, *Inquiry into the Structure of Industry and Employment Situation In Tasmania*, June 1977.
8 The Centre for Regional Economic Analysis, *The Tasmanian Economy: A Survey*, December 1987.
9 Charles Curran AO, *Tasmania in the Nineties*, April 1992.
10 Jeffrey Rae, *The Tasmanian Experience: Lessons for New Zealand*, New Zealand Business Roundtable, January 2002.
11 Tasmanian Department of Treasury and Finance, *The Competition Index: A State-by-State Comparison*, Government of Tasmanian, May 2001, page 31.
12 Parliament of Tasmania, *Budget Overview 2002-03*, Budget Paper No. 1, Tasmania, May 2002.

Jeffrey Rae is a director of ACIL Consulting and author of The Tasmanian Experience: Lessons for New Zealand, *published by the New Zealand Business Roundtable [www.nzbr.org.nz]*

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