

CEDA at fifty – the EPO at thirty

An audit of three eventful decades



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Introduction

This edition of the *Economic and Political Overview* (EPO) introduces CEDA's fiftieth anniversary year. For nearly thirty of these fifty years, the EPO has been the flagship research report, launching each New Year with a survey of the economic and political outlook.

Although 2010 opens with a domestic political outlook that is perhaps uniquely volatile, there will need to be an extraordinary upheaval if the upcoming year is to prove the most significant. So far, that accolade belongs to 1983.

This anniversary year is an occasion to look back at some of the highlights of three remarkable decades. Over this period Australia's economic orientation has been transformed and our external environment transfigured. This anniversary is also a good opportunity to revisit the forecasting capacities of our distinguished commentators, who included John Niewenhuysen, Marina Wyn-Williams, Pat Weller, Barry Hughes, Chris Caton, Dean Jaensch and Ken Wiltshire.

The 1980s

1983 can claim to be the year in which the most significant domestic change occurred. It witnessed the election of the Hawke-Keating government, marking the abandonment of the socio-political strategy that had guided Australia's economic development since Alfred Deakin's prime ministership during 1906–09. Guided by Deakin's framework, Australia's secondary economy had been largely insulated from the rest of the world. Manufacturing developed to serve primarily a domestic market and surpluses from rural and resource exports were used to fund wages and tariffs. By contrast, the post-1983 strategy sought to open Australia's economy much more directly to the global economy while boosting productivity, wealth and exports through beneficial competition.

Economic deregulation and financial liberalisation were rapidly implemented. Our 1982 and 1983 editions of EPOs anticipated this need although they did not predict that the Hawke-Keating government would act with such speed or determination. Nor did they anticipate the political base of this change. All the central measures received bipartisan support; undoubtedly the most powerful reason for rapid change.

1983 introduced a broad economic strategy, which succeeding governments have followed. This was clearly the approach of the Howard governments and (despite Prime Minister Rudd's *Monthly* article) this framework continues broadly unchanged.

Australia had embraced globalisation. But this has proved a more dynamic process than originally anticipated. Financial liberalisation in 1983 constituted one pole of this shift and the global financial crisis of 2008 another. Meantime, wholly to Australia's benefit, globalisation has also mediated a significant shift of gravity towards emerging economies in Asia. But that is getting ahead of the story.

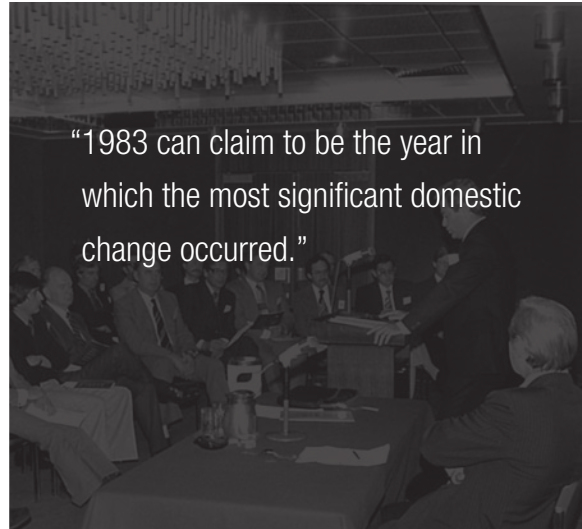
The EPO was launched in June 1982. Earlier that year, Andrew Peacock had unsuccessfully challenged Malcolm Fraser for the prime ministership and in the resulting turmoil, John Howard was elected deputy leader. Fraser rebuffed increasing pressure from 'dry' members of his own party to switch economic gears. Our commentator also noted the dysfunctional state of federal-state relations and lamented the extent to which parliament was dominated by the executive. Some things don't change.

The tone of the next two editions was exceedingly downbeat. The Australian economy was weighed down by drought, inflation and a world recession. Also in 1983, the environmental movement staged its first major campaign, to stop Tasmania's Franklin Dam. Labor had just been elected. But our commentator thought the early days of the Hawke government recalled the scandal-plagued and inexperienced Whitlam government. How wrong he proved to be!

By 1986, EPO confidently predicted another win for Labor and pointed to Treasurer Paul Keating's dominance of economic policy. The Tax Summit was over and Keating's proposed GST buried. Although the government's capacity to deliver benefits in return for wage restraint was eroding rapidly, the Accord remained the centre-piece of Labor's anti-inflation strategy.

The optimism of 1986 had reversed by 1987. That edition of EPO opened: '1986 was a horror year for the Australian economy.' Our author even noted how far all forecasts (including his own) had been off-beam. He hoped the government would continue with structural adjustment, but in an election climate doubted it would be able to resist special interest pressures. In the event, this prognosis also proved





wrong. Labour was re-elected in 1987 and pressed on more determinedly with its structural adjustment program. This was the setting for Keating's bravura 'banana republic' declaration.

The 1990s

By 1992, Bob Hawke had lost his job. He succumbed to a combination of forces including high unemployment, a weak recovery and an ambitious Treasurer. On the Coalition side, the Howard-Peacock tensions seemed to be over with John Hewson as the new Opposition leader and *Fightback* just unveiled. The EPO noted that 1991 witnessed the implosion of the Soviet empire, an event whose outcomes it declared too early to predict – except for immediate gains for Australia's wheat industry!

1993 was the year of the *Fightback* election. Both parties embraced fiscal activism as a way of stemming unemployment. However, our commentator also noted the extent to which financial markets now constrained such possibilities. He worried that their judgements would focus excessively on current account trends to the exclusion of beneficial longer term forces. Keating won the election but survived only for three years. Howard replaced Hewson in January 1995 and thereafter the Coalition's fortunes turned. After 13 very significant years for Australia's economic structure, the Coalition was returned in 1996.

In retrospect, Howard's eleven-year tenure as prime minister was not marked by the same roller-coaster as the preceding Labor years. Basic structural reforms were mostly in place, contributing to a new burst of economic prosperity. Three big structural issues remained: the Telstra sale, the GST and Work

Choices. The first two were successfully settled, though not without considerable political effort. Succeeding editions of EPO record the pressures Howard was under, starting with the Hansen, One Nation episode. Aware of how much Howard had earlier been bloodied by the Joh-for-Canberra campaign, our commentator noted the political dangers in the One Nation upsurge. Howard stared down this threat and after its initial success in Queensland, the One Nation party drifted on to ultimate implosion.

The EPO noted the obstacle course impeding adoption of a GST. In the 1998 campaign, the government managed to keep the focus on the broad design of the tax system. However, by 2001 this proved much more difficult. The GST election of 2001 was a very close call for the Howard government, fortuitously saved by the arrival of the Tampa.

The Howard governments did not enjoy the benefit of bi-partisanship. Whereas the major changes enacted after 1983 were rapid on account of (mostly tacit) bi-partisan support, the GST and Telstra sale continued to attract fierce opposition, despite the fact that both measures had earlier been supported by senior Labor figures.

For much of the Howard term, Labor disarray meant politics played second place to Australia's economic performance. The 1998 edition of EPO notes the new flexibility that the Australian economy displayed through the 1997 financial crisis.

The 2000s

By the early 2000s, the fall in productivity was attracting attention. Then the resources boom took off and the economy basked in the glow of its windfall revenue gains.

By 2007, the EPO had mutated from a severe black-and-white production with two essays and masses of statistical tables into a much more user-friendly publication. Now, photos broke the austerity of text-only pages and graphs were deliberately designed to be understood by the non-specialist. Moreover, a number of additional essays were included so that the whole publication grew to 60 pages. The traditional EPO analyses were supplemented by essays on public policy issues (water policy, the financial system and broadband). Ivan Deveson also reported on CEDA's 'Big Issues' survey.

The February 2007 edition was launched nine months before the federal election. At that stage, the outcome looked far more open than subsequently proved to be the case. John Howard was then moving rapidly to match Kevin Rudd's surge in the polls. The

latter had sought policy leadership on a variety of issues, including global warming, water management and broadband. In the light of current developments, these essays merit a second look.

In one of the supplementary essays, the noted economist, John Quiggin, surveyed issues surrounding the management regime for the Murray-Darling Basin and the development of a tradable market in water rights. Despite the fine sentiments of federal and state politicians, Quiggin lamented the generally dismal outcomes. The cap imposed in 1995 had led to an immediate increase in water run-off as the holders of unexercised rights moved to actualise their entitlements. Thereafter, the cap had achieved some positive benefits but its impact was muted by unsolved political conflicts. Under National Party pressure, perhaps the most vexed amongst these was the failure to allow city water authorities to enter the market for water. Other unresolved issues included trade between catchments and the purchase of water rights by government authorities. Overarching all these dilemmas was the dysfunctional state of federal-state relations, an issue which the Rudd government had promised to attack, so far without much apparent progress. This issue is also a core promise of Opposition leader Abbott. Indeed it is the centrepiece of his book, *Battlelines*, published earlier this year (Melbourne University Press, 2009).

A second supplementary essay in the 2007 edition was by Reserve Bank of Australia (RBA) Governor Glenn Stevens. Writing before the global financial crisis, Stevens pointed to the role of the credit boom as an important contributor to the prosperity of the Howard years. He reported that as a matter of prudence, the RBA, in conjunction with the Australian Prudential Regulatory Authority, had participated in an IMF-led stress test of the Australian financial system. High marks were awarded.

However, his caveats are noteworthy. Stress tests assumed that Australia's reverse was not part of a general international recession. In addition, the modelling assumed that an economic recovery would occur. Stevens noted that the confidence that this will happen, can not be taken for granted – yet confidence about the likelihood of recovery is vital to its actual occurrence. The global financial crisis has since demonstrated his point.

Finally, Joshua Gans of the Melbourne Business School entered the lists on broadband. Gans wrote as the national broadband network debate was gaining momentum. In his view, a national focus was wholly misplaced. Amongst the variety of options for going the last mile in delivering broadband, fibre-to-the-node (FTTP) was only one possibility. Gans noted the many alternatives and argued for a much more locally



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based approach. The Rudd government has since announced its \$43 billion roll-out. Since this is to be opposed by Opposition leader Abbott, this issue too is far from resolution.

This brings us to the most recent editions of EPO. Writing in February 2008, our economic commentator sought absolution for his forecasts. ‘There was not one word in the 2007 Economic Overview about the Shanghai stock market or about sub-prime mortgages. I prefer to believe this doesn’t mean I’m a bad forecaster; rather it means that in any one year there will be unexpected events.’ No doubt developments

later in the year, as world financial markets threatened to implode, would count in the latter category.

Presciently, the 2008 edition focused on another chronically unresolved matter, the state of Australian federalism. Ken Wiltshire presented a critique of existing political arrangements and explored the alternatives. By contrast, Jonathan Pincus defended the existing broad distribution of powers. He argued that ‘...contrary to received wisdom, Australia has got most of the big things right in the financial relationship between its states and its central government.’

This edition also strayed beyond economics and politics to look at social trends. Hugh Mackay reflected on Australia's changing aspirations. In his view, for much of the past thirty years people had been trying to defend themselves against 'constant upheaval'. Reform fatigue had been ubiquitous. Australian's had narrowed their attention to their own domestic space, which remained in their control. Now however, society has emerged from what Mackay labels its 'dreamy' period and he forecasts more social activism and more community engagement.

Conclusion

Mackay also noted the very large changes in social patterns that have occurred over the past 30 years. For example, 30 years ago almost everyone was married, indeed 90 per cent by age 30. Today, fewer than 50 per cent are married by that age. Similarly, birth rates have plummeted and the age at which a first child is born has advanced to beyond age 30. Wanting to keep their options open, young people now avoid commitments. For their part, young women regard their mother's 'liberation' sceptically. More likely, 'enslavement'. Mackay also sees a new generation of men completely at ease both with their own gender and with the equal expectations of women.

So what general themes might emerge from this thirty-year retrospective? One concerns orientations. The style and approach of EPO suggests the extent to which domestic economics and politics remain dominant. Despite globalisation, the underlying assumption of EPO authors continues to be that our future is in our own economic and political hands. Australia's prosperity was no doubt partly the result of the 1983 changes as well as sound fiscal management. But the credit boom and the rise of China have also figured.

This retrospective suggests that in reviewing the pace of the emissions trading scheme and national broadband, broad bipartisanship on general economic strategies remains. But this is often masked by the incentive structure of adversarial politics. To what extent is this responsible for failure to progress issues such as water, the Murray-Darling, Indigenous policy etc? Too often it seems that political incentives and the needs of policy making are misaligned, with the costs ultimately born by the whole community.

The EPO also shines a light on our forecasting capacities. In relatively stable contexts, forecasting tools do seem to offer some purchase on the near future. But stable contexts have been the exception not the rule these past thirty years. There seems little

prospect of their return. As Nassim Nicholas Taleb put in his celebrated study¹, this remains a world of black swans. Internationally, China's turn to a more market-oriented economy, the collapse of the Soviet empire and the rise of militant Islam were three unpredicted events. And had they been predicted, who would have believed the forecaster? Indeed, the 'tech wreck', the financial crises of the early 1990s, the Asian financial crisis and then the 2008 global financial crisis suggest that despite the sophistication of all our tools and instruments, uncertainty is chronic. It is salutary that the global imbalances that contributed to the 2008 financial crisis remain unresolved.

So the need for an EPO will not diminish. Weighing our thirty years in comparative perspective, Donald Horne's older judgement – Australia as the lucky country – seems still to have explanatory power.

Endnotes

- 1 Taleb NN 2007, *The Black Swan: the impact of the highly improbable*, Penguin Books Edition, London