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Forum

The Impact of Wages and Industrial Policies on the Performance of the Agricultural Export Industries

Policy Forum organized by the A.C.T. Branch of the Australian Agricultural Economics Society, and held at the Australian National University, Canberra on 30th September, 1986.

Official Opening Speech

John Kerin*

Thank you for the invitation to officially open this first Annual Policy Forum of the A.C.T. Branch of the Agricultural Economics Society. The agricultural economics profession has contributed enormously to rural policy debates in this country. The importance of this contribution is highlighted by today's topics, which cover two of the most important issues facing the agricultural export sector.

The theme I would like to adopt for my remarks today is that an economic environment that benefits agriculture is precisely the same environment that benefits the economy as a whole, and vice versa. Both agriculture and the economy generally need maximum competitiveness, maximum economic growth, and minimum inflation. In current circumstances, this means we need to hold and build upon the competitiveness gains from the currency depreciation. An important element in maintaining our competitive gains is continued restraint on nominal wages growth. This will contribute to lower inflation and thus strong economic, employment, and productivity growth.

Wages Policy—Recent History

It is obvious that the rate of increase in average nominal wages in this country was too high in the decade before the Hawke Government came to power. The major wage explosions coincided with the absence of an effective Commonwealth wages policy, first in the mid 1970s and again in the early 1980s. Wages growth has slowed substantially since the present Government implemented the Accord strategy—from 12.7 per cent in 1982–83 to 6.4 per cent in 1985–86. More importantly, this slowdown was achieved at a time of very strong economic and employment growth. As the Prime Minister pointed out to the Business Council, this is the first time in the post-war period that real wages declined during an economic recovery.

Research conducted within the Bureau of Agricultural Economics (BAE) shows that the Accord has resulted in a reduction in real wages of some 5.5 per cent below what earlier experience would have indicated. And all this in a climate in which average time lost through industrial disputes has fallen to less than half the level of the Fraser years.

Policy Alternatives

These recent successes result from the co-operative, centralized approach between the Government and the trade union movement formalized in the Accord. On the Government's side, we agreed to support the maintenance of real incomes over time consistent with economic conditions, income restraint generally across the community, and measures

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related to the social wage and industry policy. In return, the trade union movement has agreed to wage restraint in line with the economy's capacity to pay.

The chief alternative strategy being proposed is typified by that of the National Farmers' Federation (NFF)—I don't think the Opposition's proposals stand up as either an alternative or as a strategy. I think it is fair to characterize the NFF strategy—without being accused of creating a "straw man"—as being based on industry capacity to pay, as determined by free negotiations at the industry or enterprise level by employers and employees.

Today I would like to very clearly set out why I support the Government's approach, and why I oppose the NFF's alternative. With the presentation of the Government's Economic and Rural Policy Statement in April, and the NFF's response thereto, the areas of disagreement between the rural sector and the Government have been both narrowed and clarified. Wages policy is the major area of difference.

First, I should make it clear that we do not have rigid wage indexation in Australia. We have achieved a 5 per cent real wage reduction through the current discounting process. The purpose of the Accord is to allow wages growth to adjust to economic conditions. The terms of trade decline imposes very severe economic conditions—which is precisely what the Accord is designed for. And it has worked. Any changes should build on the success of our strategy to date. In the light of this success, any alternative proposal must be treated with great caution.

In fact, we have one of the most flexible wage systems in the world at the macro-economic level. While our real wages fell by 5 per cent, United States of America real wages fell by only 1 per cent, and rises of 4 per cent occurred in West Germany, almost 6 per cent in Japan, and a massive 10 per cent in the United Kingdom. This international comparison gives the lie to those who suggest that the wage slowdown

we have achieved under the Accord would have occurred in any event. The United Kingdom figure is particularly notable. Mrs Thatcher has run the economy into the ground and created 13 per cent unemployment, but even with strong anti-union measures cannot stop annual real wage growth of 5 per cent. Here we see once again the absolutely disastrous effects of a government without a wages policy.

So we do not have an inflexible system. The debate, therefore, boils down to whether we can, and should, have more flexibility in relative wages—that is, in wage relativities across industries, as distinct from the average wage level. I believe that we cannot, that we should not try, and that other aspects of flexibility are more important.

I note in passing the absolute contradiction in the position of those who advocate both a deregulated labour market and a wage freeze. The two are fundamentally incompatible. A wage freeze is both unnecessary and counter-productive. Wage growth this year is expected to be close to the average of our trading partners—after our currency depreciation, we do not need it to be several percentage points lower. And trade union adherence to the "no extra claims" commitment has been remarkable.

Characteristics of the Labour Market

The fundamental problem with arguments for labour market "deregulation" is that labour markets are not like the product markets agricultural economists are used to dealing with. This is because of the long-term nature of most terms of employment, the heterogeneity of labour, barriers to mobility and disparities in bargaining power. Similarities in employees relate to occupation, not necessarily industry. Workers also hold very deeply held equity beliefs that one person's wage rise should be passed on to others. These beliefs are not unique to Australia. Australia's relative wages have not been shown to be noticeably more rigid than those overseas—in the United

States of America what we call "comparative wage justice" is called "pattern bargaining." Nor are they unique to employees. Farmers, for example, do not mind using equity arguments when it suits them, such as, the misleading comparison of BAE farm income estimates with Average Weekly Earnings figures.

As a result, relative wage movements are a poor adjustment mechanism in the labour market. For example, where there are labour shortages, employers are reluctant to offer higher wages, as this flows to existing employees. Other adjustment mechanisms, such as overtime, reorganized workloads, capital investment, and training are often more attractive. Similarly, employees can organise collectively to prevent wage reductions, while employers will be reluctant to reduce wages for fear of losing their best employees, who have often been trained at great expense to the employer. In his address to the 1986 Annual Conference of the Ricegrowers' Association, the President of that Association warned against a wage cut in the industry because the resulting loss of workforce morale would threaten the productivity gains that the industry has achieved. Consequently, wages tend to operate as an adjustment mechanism only in those relatively small sections of the labour market where these factors operate with less force.

By and large, it is efficient at the micro-economic level for the labour market to adjust through quantity, rather than wage changes. And, in quantity terms, Australia has one of the most mobile workforces in the world.

Effects of Wage Decentralisation

Attempts to decentralize wage setting would, therefore, have some inevitable, highly adverse, consequences. There would be a repeat of the 1981-82 wage explosion—the last thing Australia needs. This implies a resurgence in inflation and the erosion of the competitiveness gains from the currency depreciation. As a nation, we would be locked-in to a permanent cycle of inflation and depreciation, and slow economic growth.

Farmers would end up trading a slightly lower direct wage bill—which is only about 10 per cent of total farm costs—for a greater increase in other costs. They would be worse off.

A fully decentralized system could not prevent pockets of exploitation—that is, people receiving well below the going rate for their labour. This would set up pressures for remedial regulatory action—which is partly how our system developed in the first place. Pure market forces would equalize wages within occupations, which is very different from a wage system based on "industry capacity to pay," so many of the alleged problems with the current system would remain. It would inevitably be easier to increase wages in good years than to reduce them in bad years, so more volatile industries would face above-average wage bills over time. Agricultural export industries would be obvious losers—as the sugar industry has already found out. Decentralization based on "industry capacity to pay" means that a wage hike could occur every time a firm, or an industry, improved its productivity and competitiveness. This would severely retard innovation and economic growth. Real wages tied to overall, as distinct from industry, productivity is a major way of distributing the benefits of economic growth throughout the community. I have no in-principle opposition to profit sharing, productivity bargaining, or other ways of encouraging employee initiative. But these cannot be allowed to undermine the macro-economic imperative of wage restraint. If we had learnt these lessons before the "resources boom" of a few years ago, and not attempted to "deregulate" wage fixation at that time, Australia would be much better off today.

Wages and Industry Policies

As Andy Stoeckel has been at pains to point out in recent months, it is not labour costs per se that matter to the economy, but *unit* labour costs. We can pay any level of real wages we like *as long as* they are justified by productivity levels. Productivity improvement provides the

real opportunity for greater flexibility, so this is where we are directing our attention. The present government has always been determined to lift Australia's productivity performance. Our priority on coming to office was to re-establish economic growth, which is both a cause and a result of productivity growth. We then broadened the approach to include reform of excessive regulation and protection. Now that we are well down that track, we can go further and address the impediments to productivity improvement right across the board.

We have heard a lot in recent weeks about restrictive work practices. Some employers have apparently found the responsibility of the trade movement difficult to stomach—a responsibility that has resulted in a dramatic reduction in average time lost through industrial disputes. So some have decided to provoke disputes themselves on the issue of work practices. This may have been less objectionable if real wages hadn't fallen by 5 per cent in the last three years while a survey showed that remuneration of senior management increased by 12 per cent last financial year. Restrictive work practices are not new, and have not been getting worse. They are not always the fault of unions—management bears at least equal responsibility. Many practices—such as at Robe River—arose in consent agreements. Nevertheless, changed work and management practices provide a major opportunity to lift productivity levels. I do not detect much resistance by trade unions—problems mainly occur when management makes unilateral changes that impose costs on some individuals without offering any apparent offsetting benefits.

In fact, productivity gains can offer the workforce a great deal in terms of job security, career opportunities and improved work environments. Effective action can only be taken through consultation and co-operation. Work practices are too complex, too subject to the actions of everyone involved, for a confrontationist approach to hold out any hope for major change.

Last week's Conference of employers

and trade unions began the process of a general, detailed review of restrictive work and management practices. This initiative is not a case of jumping on a bandwagon. Restrictive work practices have been a major focus of EPAC's¹ work, for example, for some time, while our industry policy approach has always included action in this area. We have now extended this more generally throughout industry.

Farmers, and others, are paying increased attention to productivity in the off-farm sector—both in processing and transport. Some of this has been focused in a narrow-minded way on individual issues such as the tally system. I am neither wedded to nor antagonistic to the tally system—what I want is the best possible arrangement. But all issues need to be addressed—not just this one.

The Government has already shown its commitment to change. I hope, and expect, that all parties in the off-farm processing and transport sectors will constructively participate in the examinations we have set in train.

Protection and Regulation

Protection has always been the major focus of industry policy debate in this country, to the neglect of other issues such as productivity. I hope the current debate represents a redressing of this balance. The two are, of course, inter-related—improvements in industry competitiveness require both reductions in excessive protection and regulation, and improved productivity.

Farmers have consistently sought reduced manufacturing protection because it undoubtedly hurts exporters. This is only one of the adverse effects of protection. Probably the major effect is resource misallocation within industries and reduced innovation within individual firms. The overall result has been to restrain productivity growth. Along with wage policy failures, this has boosted inflation, and so has reduced economic and employment growth.

¹ Economic Planning Advisory Council

Farmers should not think that protection is the cause of their problems. Manufacturing protection in Australia stopped increasing decades ago, so all the adjustments in agriculture—a higher currency level, a higher cost structure, and lower land prices—also occurred decades ago. But farmers, along with all Australians, can benefit from reduced protection, so we have started this process.

But we need to make sure that protection reductions are sustainable—there is no point in a repeat of the mid 1970's when a one-off tariff cut was overwhelmed by political opposition and subsequently eroded. This means that politically, as well as economically and socially, we need to reduce protection at a rate that avoids undue hardship to individuals.

The complete absence of retrenchments under our steel and motor vehicle plans is enhancing the prospects for protection reductions elsewhere. Chemicals, paper products, and textiles, clothing and footwear are currently under review, and we will be seeking to reduce reliance on high levels of protection in these industries. We have replaced tariffs on a number of agricultural inputs with bounties. While this assists farmers, the same is not true of tariffs on items other than inputs. From the point of view of exporters, it does not matter whether protection is provided in the form of tariffs or bounties. The Budget decision to reduce most bounty payments by 20 per cent should therefore be welcomed as a reduction in protection. The list of deregulatory measures taken by the Government is becoming too long to recite. Further measures are under constant consideration.

The other major point I want to make to the rural sector is that it is not exempt from this approach. We have inherited a legacy of ad hoc regulatory responses to rural problems from our National Party predecessors. This is to the disadvantage of the more efficient agricultural exporters.

Protection of any industry, whether it be primary, secondary or tertiary, hurts any export industry. For example, a more appropriate regulatory environment must encourage productivity improvement in the grain transport system. This is one of the aims of the Royal Commission. Reform of the dairy marketing arrangements is encouraging improved performance in the dairy processing sector. The elimination of export pooling is the major achievement, but the reductions over time in the product levies are also important.

We have heard a lot about “privatization” over the past year or so. This is a red herring—what counts is the efficiency of public sector organizations and elimination of unnecessary regulation. My Statutory Marketing Authority reforms are all about this issue of improving commercial performance. I could go on, but the point is that excessive protection and regulation are of as much relevance to agriculture as to manufacturing. As is the question of productivity. Farmers have every incentive to maximize their own productivity, but there remains wide differences in productivity between farms. With no immediate end in sight to the world trade crisis, and agriculture facing a long-term decline in its terms of trade, productivity improvements on-farm are of crucial importance.

As a government, we have shown our credentials on tackling the issues of protection, regulation, wages policy and productivity. We are prepared to act on any problem brought to our attention. Experience indicates that our approach is the only one with a future. The only approach promising lower inflation and retaining the competitiveness benefits of the currency depreciation. And the only one that takes our inheritance, both good and bad, and adapts it to our current difficult circumstances.

I have much pleasure in officially opening this Forum.