The Impact of Wages and Industrial Policy on the Performance of the Agricultural Sector from an ACTU Perspective

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> "The estimation in which different qualities of labour are held comes soon to be adjusted in the market with sufficient precision for all practical purposes, and depends much on the comparative skill of the labourer and intensity of the labour performed. The scale, when once formed, is liable to little variation. If a day's labour of a working jeweller be more valuable than a day's labour of a common labourer, it has long ago been adjusted and placed in its proper position in the scale of value".
>
> (D. Ricardo, *The Principles of Political Economy and Taxation*, Everyman's Edition, London, 1973).

Thank you for the opportunity to address this inaugural annual policy forum of the Agricultural Economic Society. The impact of wages and industrial policies on Australian economic performance is a matter of some importance, and it is appropriate that the effects of those policies on the agricultural sector be assessed in a balanced and professional way. I hope this forum contributes to a raising of the standard of debate on these issues above the cant which has characterized much of the populist pseudo-professional debate of late.

I confess at the outset that I have no particular expertise in agricultural economics and the operation of agricultural markets. This being a meeting of the Agricultural Economic Society, I defer to your better knowledge in those areas. But in similar vein, labour economics was not high up the league table of popular course options when I was at university, and this may help explain why full (or even satisfactory) appreciation of the peculiarities of labour market processes is not widespread. However, the impact of wages and industrial policy on the performance of the agricultural sector cannot fully be appreciated without a clear understanding of those peculiarities.

The direct and primary impact of wages policy is on the labour market; the effects of wages policy on product markets are indirect and induced. This is especially the case for Australian agricultural products markets where wages comprise only about 12 per cent of on-farm costs but up to 50 per cent of off-farm costs, with off-farm costs constituting up to half of farm gate returns.

In this light I wish to outline the theoretical rationale which underpins current wages policy, and in so doing I shall focus as sharply as possible in the short time available on the arguments advanced for deregulation of our wage fixing arrangements. I shall then briefly address what is meant by "industry policy", and the linkages between wages policy and industry policy under the Accord. This discussion will, I hope, provide the context for a rational assessment of the impact of wages and industrial policy on the performance of the agricultural sector, which concludes my paper.

The present government has adopted a prices and incomes policy approach to economic management, the framework of which is set by the Accord. Under the Accord, a centralized system of wage fixation—or if you like, wage regulation—is the vehicle by which appropriate aggregate labour cost outcomes are sought.

It is, today, an article of faith amongst most economists that regulated markets produce outcomes inferior to those

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generated by unregulated markets. This Pauline beacon of insight guides those blinded by it to advocate all-round deregulation, no matter what the nature of the market in question. The benefits cited by the proponents of labour market deregulation fall essentially under two distinct heads, both of which are micro-economic in character. These are:

- allocative efficiency gains; and
- productive efficiency gains.

Superior macro-economic performance is then thought to ensue from either or both of these improved micro-economic foundations.

Consider first the allocative efficiency argument for labour market deregulation. The orthodox, neo-classical market model of economic theory says resources are attracted to their most productive uses through the signalling function of the price mechanism. When demand exceeds supply, prices tend to rise, and vice versa. When wages—as the price of labour services—are regulated, as occurs through decisions of the Arbitration Commission, the free functioning of the signalling mechanism in the labour market is impaired and inefficiencies arise in the allocation of labour resources. By deregulating wage fixation, it is alleged, allocative efficiency gains will arise.

Orthodox economists have been harping on this theme for many years. In 1930 the noted Australian economist Edward Shann wrote:

> Fluctuating wages have a social function, to perform in minimizing unemployment and sending labour to Sydney or the bush. (Shann, quoted in Hancock 1985, p. 8)

The Australian Treasury, under Secretary Stone held a similar view in the late 1970s and early 1980s, as can be seen from Statements No. 2 of the Budget Papers in those years. Having freed himself of the shackles restraining comment by public sector bureaucrats, Stone asserted:

> . . . there has been in Australia an unwillingness to view the workings of labour markets like other markets—in terms of supply, demand and price. (Stone 1984)

More recently, Professor Michael Porter, in an affidavit tendered as an exhibit to the last National Wage Case, asserted:

> The most fundamental of economic arguments and principles firmly establish that a system of awarding across the board wage increases which ignores the capacity of various sectors to pay is inconsistent with the achievement of the maximum well being of employees and employers, and frustrates economic growth.
>
> It is the most basic lesson regarding economic growth that resources must be attracted into those sectors capable of employing them in the most productive manner, and any wage mechanism which reduces the signalling value that wage relativities can perform necessarily reduces the capacity of the economy at large to productively employ labour. (Porter 1986, pp. 3–4)

As noted above, this signalling role of relative wages has long been cited by those who argue against centralized wage fixation. Moreover—and this really *is* the point—it has been tested empirically *ad nauseum.* Numerous studies have focussed on the structure of wage relativities—the existence of wage differentials by age, sex, industry, occupation, and geographic location—with international comparisons and time series studies being conducted, often with subtle econometric specification and diagnostic testing, of the linkages between changes in wage relativities and employment.

Time precludes a review of this empirical literature, but Appendix II of the Hancock Report provides a ready introduction for those interested, and that particular appendix has been described by Professor Max Corden as "excellent" (Corden 1986, p. 105). The fact is that hard evidence supporting a major allocative role for wages in the labour market is just not there to be found. As the INDECS team of economists observed in *State of Play 4*:

> It is the experience in many countries of a degree of uniformity of wage increases for different types of labour, rather than between different firms, that is suspiciously inconsistent with the competitive model. It is this type of finding that has diminished labour economists' enthusiasm for the competitive story as an explanation of reality, if not as an ideal. Moreover, an Australian study has found that the size of one's over-award pay tends to depend normally on the firm worked for rather than the occupation engaged in, a result which is the opposite of that predicted by competitive theory. In the labour market the invisible hand may be all thumbs. (INDECS 1986, p. 20)

I would stress at this juncture that the Australian Council of Trade Unions (A.C.T.U.) does not quibble over the direction of the effect which relative wage movements may have on quantities demanded and supplied. All else equal, a rise in the wage rate for one category of labour relative to all others will tend to decrease the demand for and increase the supply of that type of labour. Rather, it is the ability to achieve a sustained change in relativities, and the magnitude of any subsequent response which is at issue and which brings the allocative efficiency argument seriously into question. To achieve a sustained change in relativities requires the agreement of other affected labour market participants, and such agreement will in general only be forthcoming if the proposed changes are perceived by them to be "fair". In any event, the employment response is characteristically extremely weak. For example, the marked change in male to female wage relativities following the equal pay decisions of 1969 and 1972 is noticeable by its absence from the consequent relative employment performances of these two groups; it should also be noted that the equal pay decision was widely perceived to be "fair".

These propositions are not in dispute amongst specialist labour market economists. As the noted labour market economist and proponent of labour market deregulation, Professor Richard Blandy said at the recent Conference of Economists:

> In the past twenty years . . . accumulating evidence and a variety of theoretical developments have led to a sense that labour markets do *not* work in any simple neo-classical way. (Blandy 1986a, pp. 1–2)

In concluding, Blandy observed:

> . . . Australian economists have given undue emphasis to the issue of relative . . . wage flexibility as the touchstone of efficiency in the labour market. There are good economic reasons everywhere why wages are sticky. (Blandy 1986, p. 14)

(As my opening quote from Ricardo suggests, the observed stability in relative wage structures is not a recent phenomenon.)

The "theoretical developments" to which Blandy refers include segmented and internal labour market theory, and implicit contract theory, and his paper outlines those developments accurately. To this list can be added search theory and bargaining theory.[1] These theoretical advances help explain the lack of labour market evidence supporting the simple neo-classical model, and from the standpoint they provide it can be seen why long-term job attachment—a feature of all developed economies—is economically rational for employers and employees alike.

Considerations such as these underlie the Hancock Report's conclusions that:

> The structure of wages and salaries in Australia is consistent with the provision of broadly indicative signals, rationing scarce talents and acquired skills. We do not believe, however, that relativities are a sensitive signalling device. This comprehends both the following statements: (1) wage

[1] A sound exposition of all these theoretical developments can be found in Okun (1981). The seminal article on search theory is Stigler (1962). For a recent treatment of bargaining theory, see McDonald and Solow (1981).

relativities do not respond readily to changes in the underlying conditions of demand and supply; and (2) the allocation of labour is insensitive to changes in relativities between the wage levels of major categories of labour. (Hancock 1985, p. 29).

From the available evidence and on the basis of current labour market theory, it seems that relative wage flexibility is not a *necessary* condition for labour market quantities to adapt to changed circumstances and to reflect allocative efficiency. Neither is it a *sufficient* condition. It follows that few if any allocative efficiency gains could rationally be expected to ensue from labour market deregulation. This leaves the argument based on productive efficiency.

In essence, the productive efficiency argument sees economic gains arising from improvements in workplace industrial relations and in that respect it acknowledges the fact that economic and industrial relations considerations are inextricably intertwined. The productive efficiency argument says that workers' motivation, application and ultimately output will be higher to the extent that they perceive themselves to have a stake in the well-being of the enterprise for which they work. If workers are intimately involved, in decision making and administrative processes of the organization, not only will output be higher but product and process innovation will be improved. Such an enterprise will be better equipped to adapt to change in a dynamic and uncertain world than will be the organization structured in the traditional, hierarchical, rigid way.

The A.C.T.U. does not have great problems with this argument so far as it goes. We have no doubt that workers can and do contribute materially to the dynamic well-being of the enterprises to which they are engaged, expecially where management attitudes have progressed past those of last century.

However, those advocating deregulation of wage fixation on productive efficiency grounds go further, and seek to attribute poor workplace relations between employers and employees to the presence or potential presence of a third party—namely, the arbitral tribunals. It is alleged that workplace co-operation and identification of commonality of interests is suppressed whenever either direct party to the employment contract can turn to a third party for resolution of disputes. It is asserted that the Arbitration Commission thus fosters intransigence, inflexibility, and dogmatic positions which find their ultimate expression in poor innovation, sluggish corporate performance and low productivity. Under a centralized system of wage fixation for instance, it is alleged that wage increases appear to workers as "manna from heaven" bearing little or no relationship to the circumstances of the enterprise. For those who rely on the productive efficiency argument to support a call for deregulation and decentralization, the solution is seen to lie fundamentally in the abolition of the current system and the dismantling of industrial tribunals.

The A.C.T.U. is aware of no evidence (as distinct from conjecture) which supports the proposition that the Arbitration Commission fosters poor workplace industrial relations. There is no necessary inherent conflict between good workplace relations and the Commission's existence. Indeed, there are numerous examples where, for instance, the development and adoption of grievance procedures with the participation and support of the Commission, has been reflected in marked improvements in workplace industrial relations.

Conciliation is an important part of the current system. There are countless factors which impinge on the nature of workplace relations in every enterprise, not least our cultural heritage, including the received attitudes of management and workers. To attribute to the Arbitration Commission general responsibility for poor environments in all establishments on the basis of casual theorizing and no evidence borders on slander. It is one thing to identify scope for productive efficiency gains to be achieved. It is a logical slide to then simply assert that the Arbitration Commission is responsible for retarding that achievement. By analogy, the same argument would hold that the existence of the Family Court fosters marriage failures—and I note that the employment contract has been likened by Professor Boulding to the marriage contract (cf. Norris 1986, p. 12).

The A.C.T.U. fully supports moves to improve workplace relations and is ever ready to discuss work practices in that context as demonstrated by our constructive participation in the Conference opened by the Prime Minister last Wednesday. An agenda exists. Work practices and management practices are under scrutiny.

Whilst one could be excused for thinking that this debate had only recently arisen, the fact is that work and management practices were already being addressed in a number of areas through consultation between employers and unions and in the context of broader packages designed to improve the efficiency of industry. Whereas some employers have attempted to address work practices through confrontation with consequent dislocation and lost production through closedowns, other employers have achieved changes in work practices—through consultation with and the co-operation of unions—without fuss and without costs. The Steel, Vehicle and Heavy Engineering Plans to name a few, are testimony to that readiness, and show what can be achieved by a process of open and frank negotiation under a package approach.

Furthermore, and given the trade union movement's clear and unequivocal support for orderly, centralized wage fixing arrangements, it really behoves those who would dismantle the system of conciliation and arbitration and thereby impose a decentralized and deregulated system on manifestly unwilling parties, to show clearly how that confrontationist approach would generate consensus and foster commonality of interest at the workplace level. Is it really believed that sweetness and light would emerge phoenix-like from darkness and despair? By what process and over what time period?

As an aside, I note that Professor Blandy, whose deregulatory stance is squarely premised on the productive efficiency argument, is one of the loudest and most prominent in calling for abandonment of the Arbitration system. It would be most interesting to know how his implicit endorsement of Peko Wallsend's approach to work practices and workplace industrial relations (Blandy 1986b) is logically reconciled with his rejection of hierarchic and authoritarian management and his endorsement of employee participation (Blandy 1986a), especially given his views on story-telling and "soft science" (Blandy 1985).

The allocative efficiency and productive efficiency arguments adduced to support deregulation of wage fixing are economic in character. As far as I am aware, the only other bases for such calls rest either on political strategy—how to win votes—or on political philosophy of the libertarian kind. This being an economic policy forum, I do not now address those issues.

I have argued that the allocative gains alleged to flow from deregulation are highly dubious at best, and that productive efficiency is tenuously related, if at all, to the effects of the centralized system as distinct from our cultural heritage. In these circumstances it stretches credulity to believe that significant macro-economic gains would arise from decentralization of wage fixation, particularly compared to the macro-economic performance recorded since 1983, and given the disastrous events of 1981–82.

But even if some micro-economic advantage did exist for a single firm in doing as it pleased with respect to wage rates, it is a fallacy of composition to presume that all would be better off if all firms tried so to act. Under the force of comparative wage justice (which all informed observers agree is not unique to Australia) each firm acting independently and strictly in accordance with its own perceived interests, in conjunction with trade unions doing likewise, can quickly generate a wage round far in excess of the capacity of the macro-economy taken as a whole.

Under the Accord there has been no such development. The Accord is not premised on a simple neo-classical model of how labour markets function, but is clearly premised on the fact that wages impact on inflation and employment. The Accord does not rest on shaky theoretical foundations, but on direct understanding deriving from the economic and industrial realities of the past 15 years. A centralized and orderly approach to wages can and will—if it is fair—succeed on macro-economic terms without hobbling allocative or productive efficiency. For the agricultural sector, the benefits of the present approach have been manifest in the markedly reduced incidence of industrial disputation especially beyond the farm gate in industries such as transport and shipping, as well as in the much slower rate of nominal wage increase which has been achieved. In the three financial years ending 1985–86, nominal wage rates rose 16.1 per cent compared to 39.6 per cent in the three financial years ending 1982–83; comparative figures for average weekly ordinary-time earnings of full-time adults are 23.2 per cent and 47.9 per cent respectively. That is, nominal labour costs have risen half as quickly under the three years of the Accord compared to the preceding three year period (see Table 1). In real terms, award rates rose by 6.9 per cent in the three years ending 1982–83 but fell by 7.8 per cent in the three years ending 1985–86; corresponding earnings movements were +15.2 per cent and −0.7 per cent respectively.

Expressing farm sector wages, salaries and supplements as a proportion of gross farm product is a hazardous exercise because of seasonal and other erratic factors. However, bearing that in mind, farm sector wages, salaries and supplements averaged 15.5 per cent of Gross Farm Product (GFP) over the three financial years ending 1982–83, compared to 14.4 per cent over the three financial years ending 1985–86 (see Table 2). My conclusion is that both the direct and indirect effects of labour costs on the agricultural sector have been markedly lower under the Accord policies.

Part of the reason for this beneficial outcome so far as the agricultural sector is concerned derives from the overall restraint which has been exercised by the labour movement faced with a consultative rather than a confrontationist federal government. A further factor has been the potential which exists and which has been utilized within the centralized wage fixing system for the particular circumstances facing the rural sector to be taken into account when awards impacting on that sector come before the Commission for variation. Over recent years, and notwithstanding opposition

Table 1: Real and Nominal Earnings Growth

	CPI[a]	Award rates of pay	AWOTE full-time adults	Real award rates	Real AWOTE full-time adults
1980–81/1982–83	32.7	39.6	47.9	+6.9	+15.2
1983–84/1985–86	23.9	16.1	23.2	−7.8	−0.7

Source: Budget Papers, Statement No. 2 1986–87 and unpublished data from the *Consumer Price Index*, ABS Cat. No. 6401.0.

(a) All groups excluding Hospital and Medical Services.

Table 2: Farm Sector Wages, Salaries and Supplements as per cent of Farm Product—at Current Prices

	WSS Farm Sector ($m)	Gross Farm Product ($m)	WSS as per cent GDP
1980–81	964	7,071	13.6
1981–82	1,068	7,342	14.5
1982–83	1,073	5,582	19.2
1983–84	1,200	9,038	13.3
1984–85	1,296	9,053	14.3
1985–86	1,361	8,632	15.8
Ave 1980–81/1982–83			15.5
Ave 1983–84/1985–86			14.4

Source: *Quarterly Estimates of National Income and Expenditure, Australia, June Quarter 1986*, ABS Cat. No. 5206.0.

from the A.C.T.U., wage adjustments under the Pastoral Industry Award have been delayed because of economic circumstances in the rural sector. As the Government's *Economic and Rural Policy* Statement of April this year noted:

> . . . scope exists under the existing wage fixation principles for industries to mount a properly argued case based on their incapacity to pay National Wage Case decisions. Rural industries as a whole benefited from this through a delay of flow-on during the drought that ended in 1983. Individual industries have also benefited from a delay in the introduction of wage adjustments. In present circumstances, the option remains open to the rural sector to develop and argue a properly documented case. (Australian Government 1986, p. 25)

Turning to industry policy, it is important to recognize the change which has taken place in recent years in the meaning of that term. In days past, industry policy was often taken as synonymous with barrier protection. This is no longer the case. Under the Accord, "industry policy" connotes a rational approach to industry development, with the focus on developing comprehensive packages of measures to facilitate investment and growth tailored to the needs of particular sectors, with implementation proceeding on a steady and known timetable.

For example, consider the Heavy Engineering package. Its main elements are labour adjustment assistance, skill enhancement incentives, and a concessional loan funding scheme. The labour adjustment component includes retraining, wage subsidy and relocation assistance where industry restructuring leads to retrenchments. There is a management efficiency component which provides for assistance in development of corporate plans, domestic and export marketing strategies, and consultancies for advice on new management techniques.

But let me disabuse you of any embryonic notions that these provisions are simply government handouts or easy giveaways. They are not. Eligibility for concessional loans and for assistance (other than that for retrenched employees) is contingent on approval of applications by the overseeing authority, the Heavy Engineering Board. Eligibility requires the submission of a business plan, including details of past practises, financial performance, cost structures, employment levels, as well as details of proposed new investment and demonstration that effective agreement has been reached between management and unions/ employees for significant, positive changes in work practices with information about the effect of those changes on productivity. There must also be an agreed training plan. Unless such information is provided to the satisfaction of the Heavy Engineering Board, funds will not be available. Similar requirements apply under other industry plans.

The Steel, Vehicle, and Heavy Engineering Plans, among others, show what can be achieved by constructive negotiation and commitment. They demonstrate the integration of measures affecting investment, new technology, training and retraining, work and management practices as well as changes to levels of barrier protection. To those who seek overnight change in the latter, I would simply quote the words of Adam Smith:

> The case in which it may sometimes be a matter of deliberation, how far, or in what manner it is proper to restore the free importation of foreign goods, after it has been for some time interrupted, is, when particular manufacturers, by means of high duties or prohibitions upon all foreign goods which can come into competiton with them, have been so far extended as to employ a great multitude of hands. Humanity may in this case require that the freedom of trade should be restored only by slow gradations, and with a good deal of reserve and circumspection. Were those high duties and prohibitions taken away all at once, cheaper foreign goods of the same kind might be poured so fast into the home market, as to deprive all at once many thousands of our people of their ordinary employment and means of subsistence.

and later:

> The undertaker of a great manufacture who, by the home markets being suddenly laid open to the competition of foreigners, should be obliged to abandon his trade, would no doubt suffer very considerably. That part of his capital which had usually been employed in purchasing materials and in paying his workmen, might, without much difficulty, perhaps, find another employment. But that part of it which was fixed in workhouses, and in the instruments of trade, could scarce be disposed of without considerable loss. The equitable regard, therefore, to his interest requires that changes of this kind should never be introduced suddenly, but slowly, gradually, and after a very long warning. (Smith 1776, pp. 468–469, 471).

What does the future hold? The balance of payments is the principal binding constraint to continued economic growth in Australia over the next few years. We cannot indefinitely run a current account deficit in the order of six per cent of GDP. The level of our external debt and its concomitant servicing burden preclude that. The task of financing our current account deficit has consequences for domestic interest rates which impact directly on the agricultural sector.

If progress is to be made in winding back the current account deficit the current state of our balance on merchandise trade will need to be reversed. Any fortuitous commodity prices developments would obviously be a boon, but as the 1981–82 decentralized wage fixing experiment shows, policy should be based on analysis rather than hope. It is therefore essential that progress be made on the balance of trade front through diversification of exports, particularly manufactured exports. Current and prospective policy settings, including industry policies, are appropriate to that task and will work if the nominal depreciation of the Australian dollar since December 1984 can be secured in real terms. This requires steady progress in lowering our inflation rate, relative to our major trading partners.

A comprehensive policy package geared to that task, and imparting the greatest degree of stability and certainty to the overall economic environment will be conducive to the necessary new investment. With goodwill and commitment from employers and unions we shall be on the road to long-term recovery, but we should not underestimate the attitudinal changes required. Positive approaches will not derive from confrontation. "Fighting funds" can be put to good purposes or bad.

It should be noted that Treasury's ex-Secretary Stone—who now so ardently advocates antagonism towards the union movement as the road to our salvation—was an architect of the "overvalued exchange rate" policy of the late 1970s and early 1980s which both decimated our manufacturing industry and lowered export returns to the agricultural sector. In speeches in 1979 and again in 1981, Stone purported to outline "options" for Australia in a competitive world (Stone 1979, 1981). In fact his proferred options were of the "free-to-work or free-to-starve" kind. From the implicit premise that Australia's rosiest future prospects were as a quarry for the rest of the world, Stone insisted that it was "unchallengeable" that:

> . . . Australia will need to sustain a deficit on the current account of its balance of payments through the 1980s, (Stone 1979, p. 5).

Because "in the decade ahead there seems every reason to believe that we are going to be very successful at exporting", (Stone 1979, p. 4), Stone believed we should actively stimulate imports to ensure maintenance of the current account deficit, which could be done through slashing tariffs or by appreciating the exchange rate (Stone 1979, p. 7). Every other option was ruled out. Even though he recognized the adverse consequences for exporters of the latter route, Stone was involved in setting the exchange rate but not tariffs, and history shows we took the road of exchange rate appreciation.

Thus our present debt predicament, which arose through a succession of high current account deficits, since the beginning of the 1980s, can be seen to have had its genesis in policies of the type advocated by John Stone. The government of the day put its policy eggs in that narrow options basket and they broke. Now John Stone, preening himself as authority on all matters social, philosophic and economic, enjoins us to follow him down the labour market deregulation track (cf. Stone 1984, p. 44). Would we be so foolish as to twice follow the same Pied Piper?

In summary, the A.C.T.U. rejects, on grounds of theory and evidence, the foundations on which rests the cases of those opposing the Accord, the prices and incomes policy approach and the centralized system of wage fixing. The allocative efficiency case rests on wrong theory. The productive efficiency argument against the Arbitration system identifies the wrong cause. In formulating policies for application in the labour market, regard *must* be had not only for the "invisible hand", but also for the "invisible handshake" (cf. Okun, 1980).

The benefits of the Accord strategy to the whole economy including the agricultural sector are clear, in terms of economic growth, employment growth, lower wage and price inflation, lower unemployment, greater profitability and reduced industrial disputation.

The agricultural sector stands to benefit from the greatly improved international competitiveness which the devaluation has brought—if it can be secured over the medium term. A centralized wage system offers the best prospects for locking in that improved competitiveness.

Overall, the impact of wages and industrial policies under the Accord has been beneficial to the agricultural sector. Continuation of that policy approach offers the best prospects for a sustained beneficial impact of those policies on the agricultural sector over the medium and longer term.

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