THE POLITICS OF ECONOMIC REFORM

Ian Henderson
Political correspondent
The Australian

There's no great secret about the politics of economic reform: For the most part, the losers from reform - indeed, the losers from virtually any economic and social change - are pretty easily identified, while the winners are often much harder to pinpoint. The former characteristic makes it relatively simple for the losers and the potential losers and those who fear they will be losers to be mobilised to oppose the change in question. The latter characteristic - the difficulty in identifying the winners - makes it hard for governments and others in the business of promoting change to identify potential supporters and to muster public enthusiasm for what they want to do. As a result, it often seems to well-meaing politicians and economocrats that they are faced with an impossible task: to win the hearts and minds of those who, for one reason or another, prefer the status quo, and can much more easily organise campaigns of opposition to change, drawing on the real or imagined costs likely to be imposed on the losers.

As reminders of those truths, think about the resistance to change in retail banking.; think about the fight put up by dairy farmers to reform that industry; not to mention the campaigns against lower protection for those old standards the auto and TCF sectors. In each of those cases, change was enforced but only against vocal and at least partially successful opposition campaigns. And in the case of dairy farmers, change came with a heavy cost to consmuers.

This conference has already heard much welcome news about the success of past efforts to boost productivity at least partly through engaging in pro-efficiency reforms - and to thereby lift national living standards. Indeed, the Reserve Bank of Australia, the Productivity Commission and the Australian Bureau of Statistics have been doing their best to publicise those successes for some time, using the findings of their research to back up their conclusions.

The conference has also heard that the reform task is never complete, that further economic reform - further liberalisation of the labour market, further pro-competition measures in product markets, further privatisations - is a must from the economists' perspective.

But, if John Howard is to be taken at his word, further economic reform is also a must from the politicians' perspective.

Howard has made it clear he wants the RBA to keep its foot off the brake and on the growth pedal, to see just how long the economy can expand at four per cent a year without reviving the inflation bogey. Whatever the central bank - or Treasury for that matter - believes, the Prime Minister believes that, after a decade of economic reform, the economy can safely expand by four per cent a year without giving rise to fears of an unacceptable outbreak of inflation.

What's more, the PM wants the RBA to test that speed limit because the Government is keen to generate enough jobs to drive the unemployment rate down from its roughly seven per cent figure at present to below five per cent. RBA governor Ian Macfarlane is on the public record saying the bank is willing to allow GDP to expand faster than it has been, provided inflation remains in check.

Howard's message will not have been lost on the RBA; nor will the RBA be reluctant to pass on, discretely, its own return message to the PM. I'd hazzard a guess that Macfarlane would like Howard to appreciate that getting trend growth up to four per cent without that giving rise to the threat of higher interest rates will require a fresh commitment to economic reform by the federal Government.

Howard's response will be determined, in part, by wanting to ensure that economic change does not lead voters to desert the Coalition, as they threatened to do during early 2001 in the months leading up to the

November 10 election. Had voters last year repeated their actions of three years earlier - when almost one million put One Nation first on their ballot papers, partly in protest at what they reckoned was an unacceptable pace of economic and social change - Howard would no longer be PM.

What Howard and his senior ministers learned - or re-learned - during 2001 was the simple truth of sound microeconomic policy that the losers from change must be cushioned from its adverse effects if that change is to be justified. The Government sought to do that on tax reform, with what it claimed was a generous compensation package to those hardest hit by the switch from the WST to the GST. But it is a lesson that politicians should not have to re-learn every time they decide to go for change. Indeed, economists should be constantly reminding them that ensuring there are no undeserving losers from enforced change is not only good politics but it is also sound economic policy ... if for no other reason than this: the alternative is almost certainly public opposition to reform.

Economists might continue to argue that it's better to target assistance to people who need it regardless of the causes of their need - straightened circumstances sometimes arise from government decisions, sometimes from private sector decisions, sometimes from elsewhere (like overseas economic conditions), but the problem is the circumstances not the cause - but politicians might be better advised to link the help they offer to the causes of the need if they are to win public support for further economic reform.

When the Productivity Commission recommended that more politically-sensitive approach in its TCF report several years ago, the Government failed to take its advice in full. Economic reform is going to get harder, not easier. So, if Howard's dream of lifting the economy's speed limit to four per cent (from the 3.5-3.75 per cent or so that seems to be the current consensus within Treasury) not to mention raising it even higher, he might need to take the PC's advice more seriously in future.

The cost of failing to do that could easily be decreased public tolerance of reform - and Government reluctance to pursue that path any further.

The result of any such reluctance is predictable: either the pace of growth - including employment growth - will begin to slow ... or the RBA will be unable to continue with its current low interest rate policy. Either of those results would diminish Howard's political and economic legacy.

1 April 2002