

**Australia New Zealand Foundation
CER Awareness Programme**

**Confronting Economic Realities:
The New CER Agenda**

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CONFRONTING ECONOMIC REALITIES: THE NEW CER AGENDA

I have entitled my remarks 'Confronting Economic Reality' because that is where I believe New Zealand and Australia are now at. Both are between a rock and a hard place. If we are to make our way as countries in the 1990s, this must be the new CER agenda.

I thought you might be interested in some possible variants of CER which I understand were being considered at the time the agreement was negotiated.

The first was TACT, the Tasman Agreement on Closer Trade. Perhaps that symbolised our collective habits of pussyfooting around. We still sometimes seem to behave like an old boys' club rather than real competitors, for example in agricultural trade between the two countries.

The second was TATTERS, the Tasman Agreement on Trade, Transport and Economic Relations. That seemed to reflect the steady slide of both countries into genteel mediocrity. This hasn't stopped yet.

A third suggestion was TEAT, the Tasman Economic Agreement on Trade. No doubt its promoter had in mind the prevailing beliefs of industries on both sides of the Tasman that taxpayers and consumers were there to be milked.

Finally there was a proposed name for a joint secretariat: OCER, the Organisation for Closer Economic Relations.

We have come a long way since CER began in 1983, but not far enough. Taken as a whole, the 1980s were another decade of lost opportunities for both countries. The world did not stand still while we continued our debates about protectionism, welfarism and trade union reform. The Asian countries in particular continued to pass us by.

On the positive side, governments in both countries started to accept that we had to open up our economies to the world. Starting with Australia, both countries largely deregulated their financial markets, removed exchange controls and floated their currencies. They made some progress in reducing budget deficits and reforming their tax systems. Belatedly they started to corporatise and then privatise state-owned industries.

But these and other steps towards the sort of policies that the successful countries of the world have adopted have not added up to a coherent economic programme. Once again, both countries are in deep economic trouble. Our economies are in recession, our unemployment rates are climbing towards 10 percent of the labour force and we have large current account deficits, dangerous levels of external debt and shattered business confidence.

Some in New Zealand have drawn the conclusion that our structural reform programme was an experiment that failed. As *The Economist* said recently:

"In truth it didn't. New Zealand's industry had been isolated for so long that competition was bound to be painful. The moral for reformers in Eastern Europe is not that New Zealand tried to do too much too fast but that it did not go far enough. The former Labour government did only part of the job - the easiest part. It left the least responsive market to last: the labour market remains riddled with restrictive practices and a wage fixing system which suppresses pay differentials and prevents wages from adjusting to market conditions. Here lies the real blame for job losses."

New Zealand started from a worse position. Australians have talked about becoming a banana republic; by 1984 we were just about there. As a recent *National Business Review* editorial put it, there was a belief that:

"In many ways Australia can afford to go slower than New Zealand, throw money around to ease the burden of change and hold off things like the introduction of a broad-based consumption tax. It has a lower cost welfare state, a more efficient public health service and a better education system. It has achieved these by avoiding the mistakes we have made on a wide number of fronts, from immigration to no-fault accident insurance."

But slow adjustment has its cost, as Australia has been discovering. Sooner or later, realities have to be confronted.

A genuine economic crisis does concentrate the mind, but unfortunately for New Zealand we lost concentration. After three years of working hard to put in place sound reforms, our government decided to take a teabreak and forgot to come back. The cost has been enormous. The economy has been more or less flat for the last three years, a major fiscal problem has reappeared and the markets have delivered their verdict by marking down our credit rating once again.

During the six years of the last government's term, the world economy was growing and our terms of trade were high. Organisations like the Business Roundtable were arguing that if we did not restructure when times were good, we would be forced to do so when they were bad. That is exactly what has happened. The new government has the unenviable task of having to pick up an aborted programme and telling the community that there must be further adjustment before we can expect better things, assuming that - this time - we have the resolve to see it through.

Both New Zealand and Australia have found it hard to come to terms with the idea that successful economic management requires getting all or most things right. This is the painful lesson that the East European countries are learning as they try to dismantle command economies. Some politicians like Vaclav Klaus, the Czech finance minister who is visiting Australia and New Zealand later this year, have understood the importance of moving to a "market economy without adjectives". Others are clinging to versions of reformed socialism or piecemeal perestroika-style reforms. All experience from the Soviet Union to Australia and New Zealand tells us that such strategies will only make matters worse.

The Australian government has recently delivered another instalment of perestroika. By some past standards it is a courageous package. As one commentator put it:

"Yesterday will go down as the day protection died in Australia".

The *Australian Financial Review* elaborated as follows:

"For almost a century... the nation built high tariff walls to shield local industry from the rigours of international competition. While most developing countries were opening up economies and developing an export tradition, Australia fostered an indolent and insular industrial culture based on political expediency. The country lost its way in the world, becoming a Third World primary producer with a taste for the industrial world's standard of living."

Mr Hawke deserves credit for acknowledging that:

"However much our competitors might bend or break the principles of fair trade, our own self-interest is served by a steadfast refusal to return to the days of protectionism."

But achieving a personal best standard is no longer enough. The *Australian Financial Review* rightly asked why the government did not go all the way to a zero tariff rate as the Garnaut review had recommended. It criticised the government for failing to tackle industrial relations reform - "perhaps the nation's most pressing obstacle to international competitiveness".

None of the Australian business organisations was satisfied with the overall thrust of the package. They pointed to the lack of action in whole areas where New Zealand has tackled structural change: labour market reform, waterfront costs, the public sector, telecommunications, inflation and taxation reform. Governments are no longer judged on the basis of their personal best. The only relevant standards now are international standards of excellence.

I am encouraged by these reactions and by a growing sense of economic maturity in both countries. New Zealanders are dissatisfied with our abysmal economic performance primarily because of the social stresses that it has generated. A continuation of past trends would see more of the best and brightest leaving and the old and unskilled left behind. Australians are dissatisfied with their track record because it has diminished their status in the world. The producing community - business and farmers - in both countries accept the reality of facing up to world competition without protection or subsidies. Electorates have been rewarding governments prepared to tackle difficult issues and jettisoning those that lose the stomach for them.

The business community in New Zealand has been very encouraged by the performance of the new government to date, and has shown little time for those peddling soft options. A recent poll of 40 chief executives of companies of all sizes showed 80 percent support for more measures to cut public spending. Most respondents were against monetary policy being eased to hasten falls in interest rates. Despite past claims that labour market reforms were not rated highly by manufacturers, a large majority of the sector said they would benefit from them. A

mere 2.5 percent of respondents favoured national awards. Those are encouraging statistics. Other polling has shown that most New Zealanders support the government's benefit reforms.

More and more businesses are accepting the view that they must stand on their own feet. As a fellow Business Roundtable member, the chief executive of a highly successful Australasian company, put it recently:

"Far too many of them developed a business base dependent on government support - licences, tariff protection, tax advantages, and so on. It is absolute folly to base long term investment decisions on the whim of a government. [We are] unshakeable in our belief that a company must never need government support."

Firms that are dependent on preferential access under CER to survive should heed this warning. Such artificial trade diversion is not in the interests of either country. As tariffs continue to fall, shareholders' funds will be at risk.

The Porter project has underlined the relatively modest role that governments can play in promoting international competitiveness. The most important one is to create a stable macroeconomic environment. We should stop arguing about whether low inflation is a priority; that should be taken as given, as should the conclusion that devaluation is no answer by itself to a competitiveness problem. Porter believes that governments can help by doing things like upgrading educational performance, investing in basic research and infrastructure and promoting immigration. Beyond that they should open markets to competition and get out of the way. It is the responsibility of firms to define their business strategies, find ways of meeting consumer needs, innovate, develop their human resources, and foot it with the best competition in world markets.

As young business people and professionals, you are the first generation to have to think globally. CER was never about swapping a hothouse domestic market for a hothouse trans-Tasman market. Much can still be done to round out our economic relationship. We should move quickly to free up trans-Tasman shipping and aviation and establish a free investment zone. As a frequent trans-Tasman traveller I wish we could scrap passports and streamline other immigration and customs procedures. But we have no need to copy each others' tax regimes or business laws unless they are world class. And we have to look beyond each others' market to the dynamic economies of Asia and the Pacific Basin, and further afield.

Most of our handicaps are still self-inflicted. A successful Uruguay Round would help us both, but only in a marginal way. Real success depends on confronting our domestic economic realities. Current problems are difficult but they are not insuperable. I hope your generation can help show the way forward.