The Australian

Rip Van Winkle economics will embalm shop stewards and Holdens

- by: Henry Ergas
- From: The Australian
- February 20, 2012 12:00AM

CALL it Rip Van Winkle economics. Invented by Julia Gillard, it says we should protect struggling firms so that when we wake up from the mining boom, they will still be there. It's a pity that by then the world will have moved on, ensuring today's laggards are tomorrow's relics.

An even greater pity that in backing losers, the government is picking on winners, undermining their ability to grow while making our economy more vulnerable once hard times come.

No resource boom lasts forever, and Australia's dependence on natural resources means we are especially exposed to commodity cycles. In every decade since the 1960s, the variability of Australia's terms of trade has beentwice the average of the advanced economies. In fact, our terms of trade have been only slightly less volatile than sub-Saharan Africa's and nearly as volatile as Latin America's, regions usually regarded as seriously disadvantaged by their vulnerability to commodity price shocks.

Economic policy must therefore take the long view: making hay while the sun shines, but also preparing for leaner days.

That's why the current policy mix is so poorly judged. To begin with, propping up firms that can't stand on their own two feet is hardly costless. And granting handouts triggers a rush to the public trough.

The resulting race is bizarre, for its essence is the survival of the weakest, as it is only firms on the cusp of extinction that can credibly play the game of blackmail it involves. Those firms' greatest asset is precisely that they can barely cover costs, so governments know there is a real risk they will shut down, imposing politically painful job losses.

It's no surprise the car industry, with its large, localised employment, has been this game's undisputed champion. Not because, like Novak Djokovic it beat a Rafael Nadal, but rather because it is constantly on the verge of collapse, giving it a permanent berth in intensive care.

So far, no government has had the courage to turn off the life support. But if our toytown producers can't cope today, their prospects with China emerging as the world's largest producer of cars must be nil.

Yes, the industry's closure would impose losses on local communities, but subsidies postpone the symptoms while worsening the disease. For firms, they invite slackness that increase the lack of competitiveness; and for the economy as a whole they merely shift the adjustment burden elsewhere.

After all, subsidising domestic producers reduces car imports. That reduces the supply of Australian dollars to the foreign exchange market, driving our exchange rate higher. And that higher exchange rate not only hits other, less politically powerful, import-competing manufacturers, but also shrinks our resource exporters, thus forcing efficient Peter to pay for moribund Paul.

The subsidy to the laggards is therefore a hidden tax on the export industries trying to race ahead. And that can only reduce the nation's gains from the boom.

Julia Gillard knows that, but it doesn't stop her. With the faceless men stalking the corridors, the unions call the tune. And the car producers are among the few places in the private sector where they still have members. Far better to lock those members in than help them find jobs not dependent on union power.

But that is not the only pound of flesh the faceless men are extracting. Rather, it becomes clearer every day that the unions are exploiting the Fair Work Act to secure power to entrench their authority and impose bloody disputes on a future Abbott government.

That is what the strike at BHP Billiton Mitsubishi Alliance, Australia's largest coal producer, is all about. Thanks to the FWA's widening of bargaining issues, the unions' demands are not about pay, but who controls the mine's operations. The unions' goals are to create entitlements that once in place will be difficult to remove, and in the process wrest away key management prerogatives.

If they succeed, it will set Australia back. Back a generation to when union rules meant productivity at Robe River was barely half what it could be, and when the unions' veto power meant it took BHP Iron Ore two years to secure union approval to move from a seven train daily roster at Mount Newman to nine daily, even though individual workloads would remain unchanged. Back to when the Mount Newman unions could hold up for a year BHP's shift from a contractor that used old technology to one using the latest, because they wanted a bigger slice of the gains. And union control over rosters meant workers opposed union bosses at their peril.

Little wonder productivity in basic mine operations at BHP's Mount Newman and at Rio's Tom Price increased 20 per cent with the move to individual agreements. Little wonder, too, that in 2001, the Federal Court threw out a claim by Bill Shorten's Australian Workers Union that BHP, in promoting individual agreements, was motivated by a desire to get rid of unions, rather than by the search for genuine efficiencies.

And little wonder Shorten now wants to wind back the clock.

The effect will be stark: Australian mines will be less competitive and less flexible. In the short run, that will simply slow their expansion. But from Guinea to Mongolia, vast new capacity is coming onstream. And when the boom busts, Australian mines will be slow-footed and vulnerable, as in the downturn of the 1980s, with the carbon tax increasing the pain.

But the mining giants are not alone in bearing the costs of the great leap backwards. Also paying the price are myriad small and medium firms that, unlike GMH, are not too big (and well-connected) to fail. Many that are already suffering will be further hurt as the economy-wide effects of subsidies to the favoured few play themselves out. And it is small and medium businesses that are most adversely affected by the Fair Work Act. They are the main target of the doubling in unfair dismissal claims. And the combination of minimum hours for part-time work with higher penalty rates hits small and medium businesses especially hard, as their output fluctuates more than that of larger businesses.

Already, the effects are being felt in slow private sector job creation, with the public sector increasingly accounting for employment growth. And with that happening, Morgan polling shows that after rising steadily from 1996 to 2009, workers' perceptions of their ability to quickly find a new job have worsened markedly.

So much for job security, and so much for making the most of the boom. But if things are tough now, just wait for the bust. Thank goodness we'll still have vintage Holdens and embalmed shop stewards, glowing with "the eternal lightning of Lenin's bones". Let's hope they're in demand on eBay.

Have your say