

# Microeconomic Policy in Australia

*by Dan Nguyen*

The government has a number of economic objectives it wishes to achieve, in response to economic issues facing Australia. Since these objectives may be difficult to achieve simultaneously, there are often trade-offs when meeting these objectives, and the government must prioritise its policies in order to achieve what is economically and socially good for the nation. Microeconomic policies specifically involved measures to improve the operation of firms, industries, and markets in order to influence aggregate supply levels. Over recent years, the government has refocused its management focus to accounting for structural supply-side problems that hampered its growth. To achieve this structural change, the government has aimed to lift productivity, improve flexibility and promote efficient production from current resources.

Over recent decades it has been argued that many economic problems have been caused by structural factors uncontrollable by macro-economic policies such as the lack of competitiveness of local producers and the high levels of structural unemployment caused by supply-side factors. As a result of this analysis, since the 1980's, the focus of government action has turned towards micro reforms. By minimising distortions to the market economy, the operation of market forces should bring about a more efficient allocation of resources. Achieving this allocative efficiency promotes structural change by allowing resources to flow to areas where they are used more efficiently. An example is moving resources away from the inefficient industries by the removal of tariff protection.

In attempting to achieve the aim of maximising efficiency and minimising production costs, firms will be more inclined to adopt latest technologies to produce their goods and services. Technically efficient industries minimise the quantity of resources needed to produce, freeing up resources to other developing areas of production. The elimination of distortions such as government regulations encourages the economy to maintain dynamic efficiency, where producers are able to respond quickly to the changing pattern of demand in the global economy, leading to progress through innovation and development. Micro-

economic reform helps achieve these goals by maximising competition. This is crucial as more competitive markets tend to embrace structural change more rapidly.

The government has assisted change by striving for workable competition; the policies are used to achieve the markets that are contestable, meaning the new firms entering the markets have a chance to compete against existing firms. The Trade Practices Act developed by the government aims to regulate industry and avoid obstructive competition such as price collusion.

Gradual removals of rigid regulations in trade and financial sectors have sped up this structural change process, where there is now greater reliance of market forces to determine economic outcomes. Such deregulations as the floating of the Australian dollar and the removal of RBA controls over the banks, as well as deregulations in the transport and telecommunications industries have opened up most economic sectors up to full competition, creating the incentive to become more efficient. Those reforms fall under the National Competition Policy of 1995, the most extensive microeconomic reform package in recent history. As a result, economic activity has been boosted by 2.5% and delivering lower costs for consumers, reflecting the increased competitiveness within these industries.

Microeconomic reforms have promoted structural change in Government Business Enterprises (GBE) through two approaches of corporatisation and privatisation. Corporatisation aims to encourage GBEs to operate independently from the government, eliminating political inability. Privatisation of industry, such as that of Qantas and Telstra, is the next step, where enterprises are sold off so they become privately owned.

Governments have historically implemented policies that attempt to influence trading patterns, but recently, micro reform has shifted towards policies aimed at improving efficiency rather than protecting industry. By gradually phasing out tariffs, resource have been reallocated to Australia's most efficient industries, allowing for improved international competitiveness by working on comparative advantages. For industries to become more competitive, and to justify the removal of protection, the government has taken to reforms of the labour market, as the core to increased productivity in the economy. In recent years,

the decentralisation of wage determination has become significant as wages and conditions are now mainly based on productivity improvements, through bargaining agreements, removing restrictive and inefficient work practices. The reduced role of unions and the Industrial Relations Commission (IRC) has given way to improved incentives for employers to improve their work practices based on terms in their agreements. Flexible

wages also helps keep inflation low and assists in keeping workers employed during periods of economic downturn. However, some argue that this system causes a great inequality of income, where weaker workers may not be able to negotiate high enough

wages than the more powerful unions, and therefore miss out. In addition, this system has no way of preventing wage-push inflation when economic growth is strong, and labour is close to full employment. In this situation, further wage rises tend to lead to inflationary spirals.

Under labour market reform, Australia has been successful in sustaining moderate wage increases, low inflation, strong productivity growth and relative employment growth. This wages growth has stemmed from accelerating productivity growth from 1.25% in the 80s to the current 3%. While there are significant positives, the government is yet to deal with the problem of wage dispersion, which has the potential to increase poverty, as well as undermine global confidence in Australia. Due to the long-term nature of these policies, it

is sometimes difficult to judge or assess the full impact in the short-term. It must also be remembered that micro reforms function most effectively when coupled with effective macro policies.

However, economists generally feel that microeconomic policy has been successful in delivering increased productivity, sustained higher rates of economic growth, low inflation and improved competitiveness, but in many areas, Australia is simply catching up with the rest of the world. Despite the effectiveness of these policies, sections of society such as the unemployed, and rural Australians are becoming increasingly frustrated with the lag effect of these policies. This political unpopularity tends to undermine the implementation of policy that would benefit the economy in the long-run. Therefore, Australia must overcome this unpopularity by educating its citizens to the long-term benefits of micro reform, rather than allowing them to view only the short-term disadvantages. Only time will tell how successful Australia's microeconomic reforms will be in helping achieve a respectable level of sustainable economic growth.