A POLICY PROGRAM FOR GROWTH, JOBS AND THE CURRENT ACCOUNT

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Unemployment is the central economic problem confronting Australia's policy-makers. While it is sometimes portrayed as the price to be paid for low rates of inflation, it is a price not just for the unemployed themselves but for the whole economy. Unemployment reflects foregone output to the extent that resources are not used to their full productive potential, and it places a direct cost on the budget through lower tax revenue and higher expenditure on unemployment benefits.

There is general acceptance of the view that unemployment stems from inadequate rates of economic growth over the last 25 years, accentuated by the boom-bust cycle, but there is less unanimity about the policy measures required to deal with it. The present Coalition Government has put its faith in the alleged self-regulating properties of the market and it has proceeded with a strategy of 'fiscal consolidation', including cuts of $1.8 billion to a range of labour market programs. While these cuts were partially offset with the introduction of the Green Corps and Work for the Dole programs, the main policy emphasis has shifted to the establishment of a private market in employment services, based on the purchaser-provider model. The result so far has been a slowdown in economic growth overall, and widening disparities between high growth and low

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growth sectors, which may have been even sharper without the series of reductions in interest rates corresponding with global trends.

However, interest rate reductions, as Keynes pointed out, are like 'pushing on a string'. They lower the cost of borrowing but will not in themselves persuade capitalists to invest in new capacity in the absence of more direct measures to increase the level of effective demand in the national economy - and to make firms more competitive internationally. Nor will such investment necessarily be encouraged by holding down wages, which simply increases the profit share of national income, or by accelerating the trend towards a two tier labour market. Currently, most investment and expansion in Australia is focused on property and capital-intensive resource projects with limited domestic value-adding or job-creation potential. As a result, employment growth has not been able to meet the modest target of 1.5 per cent a year, which was essential just to stabilise the rate of unemployment below 8.5 per cent, and, more worrying still, long-term unemployment (LTU) has resumed its upward trend. After falling by a fifth between 1993 and early 1996, LTU has since increased again to just under 250,000, with the major impact in regional Australia.

The purpose of this article is to propose an alternative set of policies for maximising employment growth - and reducing unemployment - with a commitment to the creation of high quality jobs and an equitable distribution of work and pay. Drawing upon classical (not neoclassical) value and distribution theory as well as Keynes' analysis of the determination of output, we argue for a new approach that integrates active demand management with a comprehensive supply side strategy encompassing industry policy, labour market programs and industrial relations reform. This approach addresses the traditional criticism of Keynesian demand management that it neglects the supply side of the economy and hence any potential impact on inflation and the balance of payments.

In other words, expansionary macro policy can create jobs and growth, but that growth will only be sustainable if it is supported by longer term supply side measures aimed at building a stronger, more competitive economy at the micro level, hence overcoming the contraint imposed by the current account and external debt. In specific terms, the measures

must be designed to shift firms to a high skill, high productivity path - a path that will not be generated and diffused automatically by a market model based on deregulation and microeconomic reform. Instead, supply side measures must embody an interventionist approach to the development of competitive advantage for Australia's export and import replacement industries.

The article is structured as follows. First, we make the case for a faster rate of economic growth as a precondition for reducing unemployment and moving towards full employment. We then critically examine the three models most widely drawn upon to analyse the problem of unemployment globally and in Australia and to provide policy solutions. Finally, we propose an 'integrated approach' to the problem which emphasises the interdependence of demand and supply-side analysis. This approach forms the basis of a strategy for long-term growth and jobs.

The Case for Faster Growth

Although a faster rate of economic growth does not in itself provide the complete answer to unemployment, let alone long-term unemployment, it is a fundamental precondition for making progress towards any realistically defined full employment goal. Nor is this 'growth at any cost', for the quality and composition of growth should be such as to ensure ecological sustainability. For example, if growth is driven by natural resource extraction, it will be more likely to come into conflict with ecological sustainability than if it is based on knowledge-intensive, value-adding activities, including resource recovery and recycling, which are more likely for reasons spelt out below to lead to net additional employment.

The nature and extent of the relationship between trend changes in economic growth and unemployment is central to the argument. It has significant implications for theoretical analysis and policy debate in the area, and it may be influenced by a range of factors at work in the labour market. As a general rule of thumb, GDP growth must equal the combined growth in the labour force and labour productivity on a per person basis. If GDP growth exceeds this threshold - the 'unemployment

stabilising growth rate' - then and only then will the unemployment rate decline. This relationship between GDP growth in excess of the unemployment stabilising threshold on the one hand and the unemployment rate on the other is captured by the 'Okun coefficient' (Okun, 1970).

In Australia, the Okun coefficient is around 2.1 (Indecs, 1995, ch 4); that is, for every 2.1 per cent GDP growth is above the unemployment stabilising threshold, the unemployment rate will decline by one per cent. Currently, the unemployment threshold is around 3.5 per cent, but it is not widely recognised that the threshold is now falling largely because of the trend decline in labour productivity growth. This is because sectors with the most rapid productivity growth account for a diminishing share of output and employment and because the composition of the workforce is shifting from full-time to part-time employment. The relationship between economic growth and the unemployment rate was a major issue discussed in the employment 'Green Paper' (Committee on Employment Opportunities, 1993, ch 2), which concluded that GDP growth of 4.75 per cent for eight years would be sufficient to bring down the unemployment rate from 11 per cent in 1993 to 5 per cent in 2000.

However, for the 1990s, annual economic growth is averaging less than 3 per cent and annual employment growth is around 1 per cent. In addition, current policy sits uncomfortably between the demands of financial markets, which favour microeconomic reform over macro activism, and the dynamics of 'reform fatigue' in an electorate which gives priority to secure employment. The consequence is policy paralysis and an unemployment rate anchored for the foreseeable future at nearly 9 per cent. On the other hand, it is important to note that the GDP growth requirement is declining because of a slowdown in the growth of the labour force. In the DEET (1995) *Workforce 2005* projections, the labour force is expected to grow by 1.6 per cent per year over the next decade. This represents a decline from the long-term trend and is a response to the decline in natural population growth, the fall in net immigration and an ageing population.

The DEET projections also forecast a trend increase in the female employment share and a continuation of the growing part-time employment share (to over 30 per cent in the next century). Hence, we

estimate that the projections imply an unemployment stabilising growth rate of 2.8 per cent (Burgess and Green, 1997). Using an Okun coefficient of 2.1 suggests an annual reduction in the unemployment rate of around 0.4 per cent through to 2005 if GDP growth can be sustained at about 3.5 per cent. This is not spectacular, but it does give recognition to Australia's current account and external debt constraint, which we address below.[1]

As a result, despite the favourable structural developments, economic growth well above 3 per cent per year remains imperative over the next few years if the unemployment rate is to be reduced. Even if this is achieved, the Green Paper persuasively demonstrated that special labour market measures are required to address long-term unemployment and different forms of labour market disadvantage (Committee on Employment Opportunities, 1993, chs 4-6). In other words, it is not enough to secure sustainable rates of economic growth of 3.5 per cent per year. There is also a need for supplementary policies to address long-term unemployment, regional unemployment disparities and the uneven access to jobs and income across the community. In the next section, we discuss the competing models and approaches to job creation and economic performance.

Overcoming the Limits of Growth

What are the barriers limiting the growth of output and employment in Australia? Is economic growth above 3.5 per cent sustainable on a continuing basis over the medium to longer term? Is it feasible to aim for even higher growth to ensure a rapid and permanent reduction in unemployment, with additional measures to tackle LTU? On the face of

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1 The recent Mortimer report on industry policy sets a similar overall target, but offers no practical mechanism for its achievement (Mortimer 1997, ch 2). In this it is reminiscent of the 1965 National Plan in Britain, which was abandoned in all but name after the currency crisis of 1967. A further attempt in the 1970s was equally unsuccessful because it relied upon the state to substitute itself for the market, rather than tripartite mechanisms which involved employers and unions. The lesson of this period was that government could *enable* but not prescribe the pattern of economic growth.

it, finding the right answer to these questions should provide the basis for developing new policies that address the barriers more effectively and overcome the limits to growth. However, there are at least three different models or views on what direction analysis should take and how the barriers might be identified and tackled in practical policy terms.

The Perfect Competition Model

The first view is based on the idea of 'perfect competition' in orthodox neoclassical economics. This view assumes a functional relationship between prices and quantities, which are determined simultaneously in all commodity markets, including those for factors of production such as labour. Equilibrium is achieved when markets 'clear' and the economy, treated as a self-regulating mechanism, produces optimal efficiency and welfare outcomes. Unemployment is explained here by 'imperfections' which prevent the labour market from clearing. These imperfections or impediments include, predictably, trade unions attempting to gain 'monopoly rents' from driving wages above market-clearing levels, and minimum wage regulation that distorts price signals by 'artificially' raising the floor price of labour. There is no role in this model for macroeconomic stabilisation policy, which cannot affect the long-run growth rate except by 'crowding out' private investment, and policy is therefore best directed to the elimination of budget deficits and market impediments.

The main policy implications of the perfect competition model, or 'economic rationalism' as it has become known in Australia, lie in the area of microeconomic reform. Since the barriers to full employment are unions and wage regulation, they must be eliminated to the extent that their operation and impact are inconsistent with desired market outcomes. This is the rationale in neoclassical economics for deregulation and wage flexibility throughout the world. It means, in the first place, pursuing a political and legislative strategy to restrict collective bargaining and union organisation and, secondly, marginalising or abolishing wage fixing tribunals, including their role in establishing industry-wide agreements and awards (Brown and Wadwhani, 1990). The model suggests that only when wages are set individually between employers

and employees without external 'interference' will they be able to reflect both the marginal productivity of labour and the forces of demand and supply in the labour market.

The policies associated with the perfect competition model have been embraced by many governments and are currently championed by Australia's Treasury and Reserve Bank. While the model was moderated and adapted in various respects under the Labor Government, its more extreme version has an ideologically receptive audience in the Coalition. Labor was prepared to deregulate financial markets, through the floating of the dollar and removal of exchange controls, and to deregulate product markets to the extent that it introduced a program of tariff reductions and national competition reform. However, it baulked at the 'last frontier' of micro reform - deregulation of the labour market - given that this compromised the core principles of its Accord with the trade union movement, including the commitment to social justice objectives (Green, Mitchell and Watts, 1997). While Labor's caution in this area was supported by evidence on the existing scope for flexibility, the debate was no longer about evidence but ideology. Without the distraction of the GST, labour market 'reform' may have formed the basis for a Coalition victory at the 1993 election.

Labor was adept at retaining the overall support of business groups while it continued to shift the focus of wage bargaining to a more decentralised level, and correspondingly to restrict the role of the Australian Industrial Relations Commission (AIRC), but it lost support when the limits to further micro reform became apparent. The then Prime Minister's ambitious post-1993 election pledge to make enterprise agreements not 'add-ons' but full substitutes for awards, which raised employer expectations, was not delivered in subsequent legislation, though bargaining was opened up under AIRC scrutiny to the non-union sector. Significantly, the Coalition has now seized the opportunity to implement the same pledge through its Workplace Relations Act, despite amendments in the Senate, by stripping back awards to minimum standards and expanding the role of non-union bargaining and individual contracts. This strategy, like its counterpart in 1980s Britain, is thought to have a greater chance of success if it weakens organised labour through

the promotion of high unemployment as part of the fiscal consolidation strategy.

The 'Imperfectionist' Model

The second view challenges not so much the conceptual basis of the perfect competition model but rather its practical efficacy. This view is influenced by the Institutionalist tradition of economics, which has treated the imperfections of neoclassical economics not as impediments to the working of the economy but as a necessary part of it. In the 'imperfectionist' approach, which characterised policy-making under the Accord, the legitimate role of institutions such as unions and tribunals is recognised, and the policy focus is shifted to achieving wage and price-setting behaviour that holds unemployment as close as possible to its 'natural rate' or non-accelerating inflation rate of unemployment (NAIRU) (Indecs, 1995, ch 4). In other words, union activity and minimum wage regulation are still seen as impediments to full employment in a theoretical sense, but it is not acceptable to try to eliminate them. Instead, a value judgement is made that a moderate level of unemployment, accompanied by policies to control inflation, is a price worth paying for greater equity in the labour market than would otherwise be justified. The debate here turns on whether higher unemployment should be tolerated, as in Europe, or more wage dispersion and 'low quality jobs', as in the US (Freeman, 1994; OECD, 1996).

There is also a further component to this view, which identifies a fundamental contradiction between the determination of wages by demand and supply in the external labour market (as assumed in the perfect competition model) and by factors such as skill, responsibility, performance, loyalty and commitment in the internal labour market of the firm or organisation. These factors were highlighted initially in industrial relations research on the 'open-endedness' of the employment contract, rehabilitating Marx's notion of 'labour power', which showed that employers purchase not labour as such with a given marginal productivity but only the capacity of workers to perform labour (Nolan and Brown, 1983). According to this research, the quality and productivity of labour will be contingent upon the way in which management structures its

relationship with the workforce, including the nature of work organisation, the role of employees in decision-making and the design of the payment system.

In mainstream economics, the research has given rise to 'implicit contract' theory and the 'efficiency wage' hypothesis, which maintains that wages set within the firm to maximise employee commitment and performance in product markets are largely impervious to fluctuations in the labour market (Ackerloff and Yellen, 1986). Indeed, the recent experience of the UK has resulted in 'evidence that unemployment has, at most, a very small depressent effect on wage increases' (Gregory, Lobban and Thomson, 1987). However, the research also points to the emergence of a two tier labour market - with a high status, high skill core gaining access to efficiency wages in permanent, stable internal labour markets, while an insecure, low skill periphery of part-time and casual workers, comprising mainly women and disadvantaged groups, is subject to the vagaries of the external labour market. The jobless may be said to constitute a third tier, which is increasingly part of a growing 'underclass', for while it may enter the periphery, it has only limited opportunities to join the core workforce.

While unemployment in excess of the NAIRU is generally attributed to over-expansionary fiscal and monetary policy settings, a high level for the NAIRU itself, especially when it includes a significant proportion of long-term unemployed, is attributed by the imperfectionist view to 'market failure'. Moreover, a perverse 'hysteresis' effect may be at work as well; since the NAIRU is not independent of the actual unemployment rate, any growth deficiency can soon result in a build up in the numbers of long-term unemployed and a growing NAIRU (Indecs, 1995, ch 4). This is the essential justification for intervention by public agencies and the operation of active labour market programs throughout the OECD, such as the former Labor Government's *Working Nation* programs. In this context, the programs are designed for the most part not to create net additional employment, which is generated by economic growth, but to provide the long-term unemployed, young people and other disadvantaged groups with relevant skill attributes and entry points to the core workforce.

The Keynesian Model

While the imperfectionist approach has much to commend it in practical policy terms, especially its commitment to labour market programs, it is flawed to the extent that it shares theoretical underpinnings with the neoclassical perfect competition model. In particular, it is implicit in the concept of the NAIRU and the associated operation of wage subsidies that unemployment can be reduced most effectively by lowering wage costs for business. Alternatively, the Keynesian or post-Keynesian view would suggest not only that wage subsidies are ineffective when unemployment results from deficient demand, since they merely promote the substitution of cheaper for more expensive workers, but that a policy of wage reductions in general is counter-productive. If such a policy were actually to succeed in reducing wages to any significant extent, it would further depress demand in the domestic economy as a whole and hence contribute to higher not lower unemployment. This was the key message of Keynes's *General Theory of Employment, Interest and Money* in 1936, which confronted the Treasury orthodoxy and its use of supply and demand assumptions in the determination of output.

However, with the more recent emergence of internal labour markets in firms and organisations, a wage reduction policy is unlikely to affect all groups equally, for its impact will be largely confined to workers in low skill, low paid and insecure jobs with little or no union organisation. The evidence suggests that the policy will not in itself expand job opportunities for these workers in the long-term, since labour demand throughout the OECD is moving upmarket to high skill jobs, but will only serve to accelerate the growth of wage dispersion and a two tier workforce (OECD, 1996, ch 3). In addition, the efficiency gains from a more flexible use of labour will be dwarfed by the huge costs to the economy in lost production, together with the cost to the budget in unemployment benefits and foregone tax revenue, that results from persistent mass unemployment (Junankar and Kapuscinski, 1992). Any short-term gains in international competitiveness will be more than offset by the inherent disadvantages of a low wage strategy in a world of even lower wage economies.

Keynes argued that there is no inherent tendency for a market economy to adjust to a position of full employment, and that even in savings-investment equilibrium, output can fall short of its full employment level for an indefinite period in the absence of additional sources of effective demand. Rather than devising measures to remove impediments from the labour market, and to pursue a self-defeating wage reduction strategy, Keynes made the case for stabilisation policy, primarily through deficit-financed government spending, to increase aggregate demand and generate a full employment level of output. While this marked a theoretical departure from the perfect competition model, it did not overcome the problem of the limits to growth of output and employment, which had their source in the structure of the market economy. Keynes himself conceded that interventionist policies might be required to raise the level of capital accumulation, and even to undertake the 'socialisation of investment'.

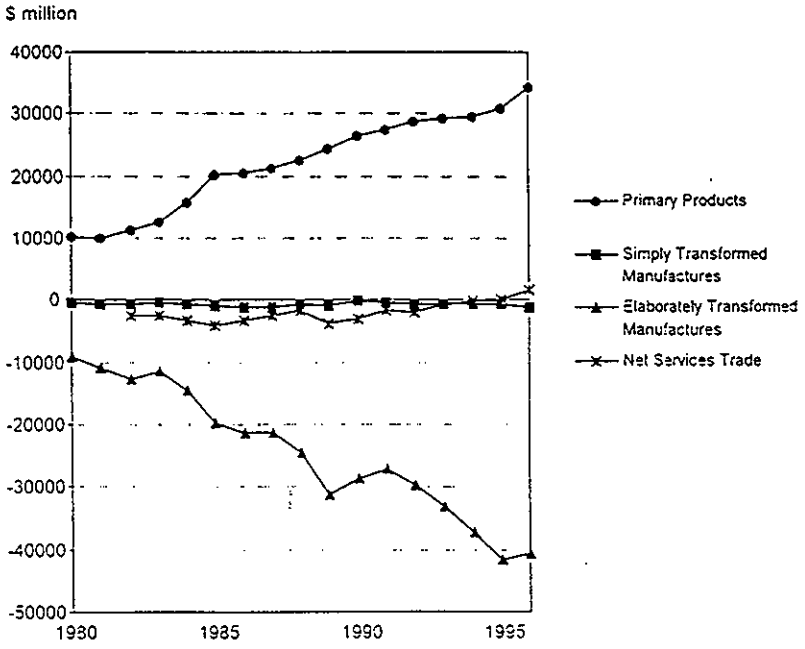
However, Keynes' analysis of supply side issues did not progress beyond the orthodoxy of the 'marginal efficiency of capital', and it is still the classical economists and their post-Keynesian interpreters who provide the most coherent alternative to neoclassical value and distribution theory (Eatwell and Milgate, 1984). These economists address the structural dynamic of capitalism in a global context, the drivers of growth and accumulation and the need for supply-side policies going beyond the Keynesian prescription. The dilemma for policy makers has been characterised as follows

> For the patterns of interest rates and prices of financial assets, and the exchange rates which keep overseas holders in particular happy, may well not be the levels which are consistent with the rate of domestic investment spending - both public and private - that may be needed to bring about the desired restructuring and provide the proper level of activity and employment overall, and with which is associated a suitable supply of exports and demand for imports. (Harcourt, 1992, 8)

Without a strategy that takes account of the structure of Australia's economy and its position in world markets, the limits to growth are likely to be imposed by the balance of payments constraint and an associated deflationary bias to monetary policy. The current account deficit for

1996/97, for example, was over $20 billion, which at 4 per cent of GDP is at the upper end of the OECD range. This largely reflects the net income deficit, especially interest payments required to service Australia's foreign debt. Although lower world interest rates, the conversion of debt to equity and the recent strength of the Australian dollar have reduced these payments from around a third to just over 10 per cent of export revenue, the net income deficit continues to be 'lead in the saddle' for domestic fiscal policy. It is perpetuated by the deterioration of the trade balance in elaborately transformed manufactures (ETMs), offset only by Australia's traditional surplus in primary products (see Figure 1).

Figure 1: Australia's Balance of Trade



Source: ABS, DIST, Mortimer (1997)

As we have seen, Australia needs at least 3.5 per cent economic growth to bring down unemployment on a consistent basis. However, in present circumstances, if this objective is pursued through demand expansion, our propensity to import will result in a corresponding increase in the current account deficit.[2] Does this matter so long as the rest of the world is prepared to finance the deficit through capital inflows? There are at least two reasons why it must matter to an open trading nation like Australia. The first reason, as Thirlwall explains, is that 'interest rates will be higher than otherwise would be the case in order to finance the deficit, or to stop the currency from depreciating' (Thirlwall 1992). This is illustrated by the relationship between real interest rates and the current account in Australia's recent economic history (Figure 2), which has had a damaging effect on investment plans. It is also illustrated by the $A depreciation against a trade weighted average over the last decade. While this has increased competitiveness, it has also exacerbated the level of debt, which is denominated in overseas currencies.

The second reason why the current account matters is because 'no country in the long run can grow at a rate faster than that rate consistent with balance of payments equilibrium on current account unless it can finance an ever growing deficit - which in general it cannot' (Thirlwall 1992). In other words, the balance of payments becomes the ultimate constraint on growth, and, in the absence of supply side measures to address the current account deficit, it establishes the conditions for a damaging 'stop-go cycle' and increasing levels of unemployment, especially long-term unemployment, with each successive cycle. At the same time, reliance on currency depreciation will encourage the adoption of an export strategy based on low wage competition rather than a high skill, high productivity economy. Meeting this challenge calls for a more integrated approach to economic policy than has previously been contemplated in Australia, combining active demand management with

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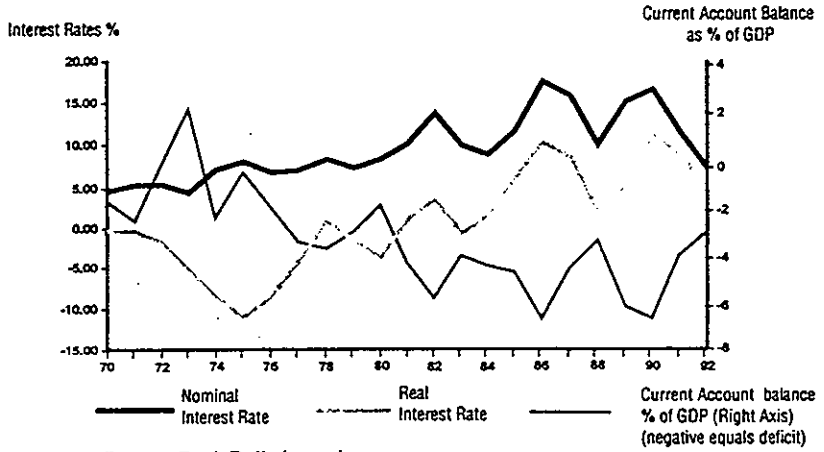
2 This does not imply acceptance of the 'twin deficits' theory, which rests on the pre-Keynesian assumption that savings are a pre-condition for investment, rather than the consequence of investment, and that public expenditure, or 'dissaving', necessarily crowds out private expenditure. This theory confuses an identity with causality.

an interventionist supply side strategy encompassing industry policy, labour market programs and industrial relations reform.

Figure 2: Interest Rates and the Current Account, March



Source: Reserve Bank Bulletin, various

A Strategy for Jobs

The most effective strategy for overcoming the balance of payments constraint on growth and jobs is to tackle the merchandise trade component of the current account deficit, since the net income deficit problem is unlikely to be resolved on its own. This would address the major weakness in the Keynesian position without necessarily accepting the free market model underlying the perfect competition and imperfectionist approaches discussed above. It will strengthen the case for expansionary fiscal policy and associated public sector job creation by modifying it to include additional components, such as a more coherent framework for industry policy. The aim should be to create a trade surplus that offsets the net income deficit, and provides the scope and capacity for the nation to reduce external debt as a proportion of GDP to more sustainable levels. At the time of the last recession, for example, a number of scenarios were developed on adjustment paths for

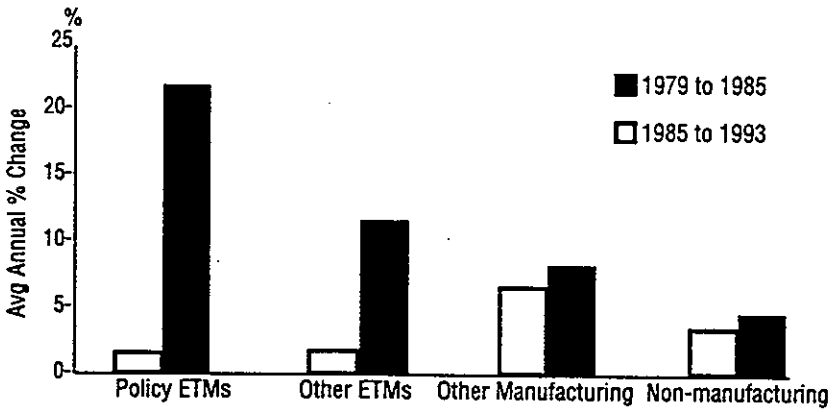
export growth subject to assumptions about import penetration (EPAC, 1992) and on the size of the surplus required for debt stabilisation (Green, Mitchell and Watts, 1992).

All these scenarios implied, however, that the key to success must be found in effective supply side measures to develop Australia's export and import replacement capabilities. This is not to suggest that all or even most of the net additional employment will be created directly by exports or the replacement of imports, for they simply generate the conditions for demand-led growth in the economy as a whole through their effect on the balance of payments. As we have seen, the additional employment is more likely to take place in other areas, including public sector industries and services, which now have greater scope for expansion without increasing the current account deficit. Such industries have a low import requirement, are labour-intensive and, in some cases (health, education, community services) generate considerable externalities and in others (transport, communications) also form part of the infrastructure for the private sector (Burgess, 1992).

Supply Side Linkages

The question now arises, what is the source of export growth and import replacement that can at least potentially underpin this broader impact on employment? According to the traditional doctrine of comparative advantage, Australia should concentrate on its primary commodity exports, which are still a large component of our total exports, but these have experienced a secular decline in their terms of trade over the post-war period. In other words, they may increase in volume, but export revenue has not increased correspondingly in value, and is unlikely to do so in the foreseeable future. While primary commodities experience declining terms of trade, the reverse is the case for manufacturing, particularly ETMs, which comprise the largest and fastest growing area of world trade. Globally, the most successful economies have relied not on comparative advantage, but on creating 'competitive advantage', based on investment in knowledge and skills rather than natural endowments and high value added production as opposed to high volume production (Reich 1991).

Figure 3: Components of Australia's Export Growth, 1979-1993



Source: Sheehan *et al* (1994)

Although manufacturing has contracted in Australia as a proportion of GDP, and the role of the services sector has correspondingly increased, manufacturing output and productivity have risen markedly and the decline of total employment in manufacturing has stabilised in recent years.[3] In addition, ETM exports, which grew very slowly between 1979 and 1985, tripled between 1985 and 1993, with even more rapid growth in the ASIC categories targeted by the former Labor Government's industry plans (see Figure 3). While it is also true that the net trade deficit in ETMs also increased from around $21 billion in 1985 to $40 billion in

3 Indeed, a recent study suggests that the declining employment share of manufacturing in leading industrialised economies has its source in rising labour labour productivity (Rowthorn and Ramaswamy, 1997).

1995, this represented a significant slowdown in the growth of the deficit and a fall in the ETM deficit/GDP ratio over the period up to 1990 from 9 per cent to 7.9 per cent (Sheehan *et al*, 1994). Whether this slowdown continues under current economic policies, which have reduced support for ETM exports, remains to be seen. The evidence indicates that the services sector is also becoming a major source of export growth, but not yet to the extent or with the value-adding capacity of manufacturing.

The next question is, how does manufacturing create jobs? What are the linkages and mechanisms? First, while the manufacturing sector itself has limited scope for jobs growth, it is undergoing a fundamental shift in the nature and composition of employment as a result of the introduction of new technologies and skills. This is reflected in the fact that the industries experiencing the most rapid and sustained employment growth on a global scale are those making knowledge-intensive products and services, and that within most of these industries the main areas of employment growth are characterised by high complexity and high skill. On the other hand, low skill jobs are generally declining in the OECD, except in traditionally labour-intensive industries, or are being outsourced to low wage economies.[4] The relationship between technological change and the growth of high skill jobs has been depicted as follows:

> Technology both eliminates jobs and creates jobs. Generally, it destroys lower wage, lower productivity jobs, while it creates jobs that are more productive, high-skill and better paid. Historically, the income-generating effects of new technologies have proved more powerful than the labour-displacing effects: technological progress has been accompanied not only by higher output and productivity, but also by higher overall employment. (OECD 1994, 33; also Green 1995)

Moreover, the recent trend in the manufacturing sector has been to outsource not only low wage activities but also a range of high wage services, such as design, marketing, training and maintenance, which are then counted for statistical purposes as services rather than manufacturing

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4 Australia resisted the trend temporarily as a result of the wage restraint policies of the 1980s, which resulted in the substitution of labour for capital and a low rate of productivity growth (Green 1996a).

employment. It is in this sense that we live not in a 'post-industrial' society, but one in which the distinction between manufacturing and services is increasingly blurred (Jaikumar, 1986; Reich, 1991). This touches upon the second mechanism by which manufacturing creates jobs, which is through its relationship to services that are directly or indirectly dependent upon it. An example of the former are business and financial services, and the latter includes retail outlets and personal and recreation services. Historically, manufacturing has given rise to a 'clustering' effect, with the establishment of formal and informal customer-supplier chains which include services as well as other manufacturers.

The third mechanism by which manufacturing creates jobs is less visible but, as already indicated in the earlier discussion, of even greater significance. Here, improvements in productivity and competitiveness enable manufacturers to export to world markets and to replace imports at home. It is this process, based on private and public sector investment[5], that allows the nation to reduce the current account deficit and hence to overcome the balance of payments 'speed limit' on economic growth, it provides policy-makers with the opportunity to do so through investment in public infrastructure and community services, which not only creates new jobs directly but also via multiplier effects across the economy. Indeed, the public sector can and should be the major source of additional employment in the next century, because as manufacturing becomes more productive, government is in a better position to mobilise resources, including people, to tackle unemployment and meet clearly identified social needs (Langmore and Quiggin, 1994).

An Integrated Policy Approach

An integrated approach to policy is required to maximise employment growth. In the first place, macro policy will stimulate demand within the limits set by the balance of payments and create jobs directly in the public sector and through multiplier effects in the private sector as well.

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5 The 'crowding in' effect of public investment on private investment is now well established (Aschauer, 1988).

However, this policy stance will not be sufficient on its own to achieve sustainable jobs growth, even if it is targeted at public sector activities with a low import propensity (European Commission, 1993). It must also be supported by an interventionist supply-side strategy, which promotes exports and import replacement as a means of overcoming the balance of payments constraint. The main component of such a strategy will be a sector-based industry policy, which, after the burst of industry plan activity in the early 1980s, became virtually a policy void by the 1990s. The adoption of generic cross-sector programs aimed at boosting 'competitiveness' and the export-orientation of companies may have satisfied the desire of market orthodoxy for a 'non-discriminatory' approach, but it was not the most cost-effective use of resources.[6]

In Australia, industry policy will require new tripartite institutions outside the machinery of government to enable employers and unions to develop coherent strategies and visions for their sectors. In a world of smaller, more interdependent units of production, sectors and regions are the most efficient levels for determining investment, research and development and training plans, as well as for organising customer-supplier linkages and networking arrangements. While investment may not always lead at once to jobs growth, the long run relationship is a strong one (see Figure 4). The role of government in this context is to assist in the coordination of the plans and to provide assistance on the basis of transparent criteria related to the agreed goals of sector strategies and the mechanisms by which they may be translated into reality.[7] The strategies will also provide a clear framework for enterprise bargaining and ensure that a connection is made between decision-making at the workplace and the plans and priorities developed beyond the workplace at sector level. This

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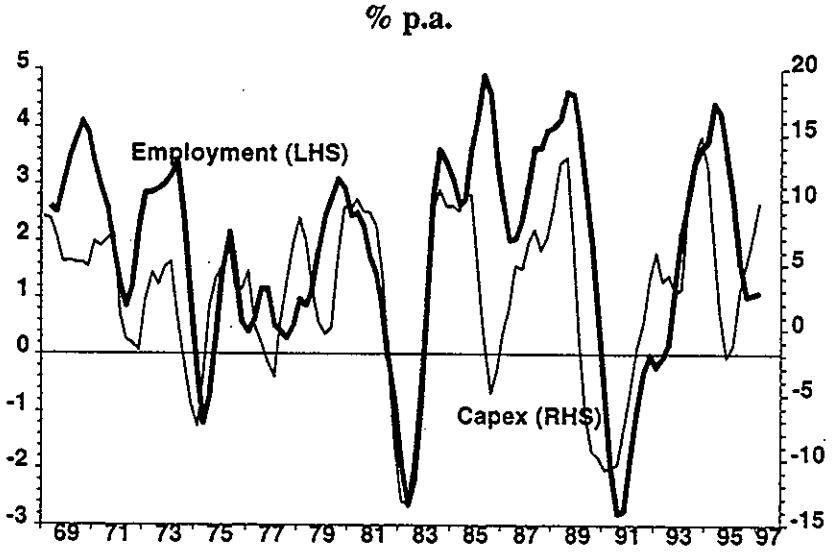
6 In a classic case study of industrialisation, Rodrik shows that in South Korea and Taiwan high levels of investment rather than exports were the 'main driver of growth' (Rodrik 1995). The same short-sighted preference for generic programs over sector-based programs is evident in the Mortimer report on industry policy (Mortimer 1997, p 164).

7 The problem of 'coordination failures' in investment markets, where returns from investment are so low or returns demanded by finance capital so high that investment remains stuck at low levels, is discussed by Cooper and John (1995) and Gill (1996).

is essential not just to industry policy but to 'articulated trade unionism' (Evatt Foundation, 1995)

Figure 4: Growth in Employment and Real Fixed Capital Expenditure



Source: Australian Economic Analysis (1995)

There will also be a role for active labour market programs to channel the impact of economic growth, develop the skills base and replace passive income support for the unemployed. Such programs are now an integral part of economic and social policy in most advanced countries (OECD, 1995b), and their rationale may be conceptualised in the short and longer term. In the short term, the effectiveness of programs will depend largely on their 'strategic fit' with macro policy. In a recession, public sector job creation programs are inherently cost-effective because they generate employment directly and increase aggregate demand through their multiplier effects, whereas wage subsidies tend to lead to job substitution and displacement (Burgess, 1992). However, during a recovery, wage

subsidies can play a part in distributing employment growth equitably and ensuring that the long-term unemployed and other disadvantaged job seekers have a better chance of entering the permanent workforce. This is a function which can also be performed by work-sharing and reductions in working time.

In the longer term, the key programs will be those that promote training and retraining for the whole range of client groups, including school leavers, new workforce entrants, current and displaced employees, women re-entering the labour market, as well as the unemployed and groups excluded from the labour market. These programs are not just the responsibility of government but of employers in the context of industry policy who recognise that training is an investment rather than simply a cost. Nor can the worth of training programs be judged by a 'cost per net impact' evaluation, since this confuses training with job creation, as well as encouraging discrimination against 'harder to place' client groups. While training can provide skill attributes that assist in job search, the creation of net additional employment is a separate process.[8]

Finally, industrial relations reform has a part to play not only in the job creation task itself but also in the type of jobs created. As Australia's wage fixing system becomes more decentralised, it is inevitable that workplace productivity gains will be pursued at the expense of comparability (Green 1996b). If this approach is pursued too far, however, it will actually undermine the drive to a high productivity, high skill economy for three reasons. First, achieving dynamic long-term efficiency gains at the workplace depends on a cooperative, motivated workforce, which will in turn be affected by perceptions of fairness. Second, an agreed industry-wide 'going rate' for the job ensures that employers compete on the basis of quality and innovation rather than wage undercutting. Third, the skill-based classification structures that are currently being established at an industry level could be rendered unworkable by excessive pay variations within and across workplaces.

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8 Calmfors (1994) emphasises the need for a 'balanced portfolio' of labour market programs and the tendency to decreasing marginal returns, including substitution and deadweight effects, in the absence of a broader approach to employment creation.

Industry agreements allowing scope for local flexibility, as in Germany, would provide the best fit with a sectoral approach to industry policy, competency-based training and skill formation.

Conclusions

In this article, we have analysed the rate of economic growth required to reduce unemployment, taking account of recent projections of labour force growth and productivity, as well as structural change in industry and the labour market. We argue that the projections of the 1993 Green Paper on restoring full employment should be modified to the extent that the trend to part-time employment and falling labour force growth has significantly lowered the unemployment stabilising growth rate. Our conclusion is that a 2.8 per cent growth rate is now required to stabilise unemployment and 3.5 per cent to reduce it by 0.4 per cent a year. The problem is that current and projected growth rates will not be sufficient to make a sustained impact on unemployment, and the present Government's fiscal consolidation strategy is likely to make it considerably worse. This strategy will (1) reduce public sector employment directly, (2) damage the job chances of the long-term unemployed and disadvantaged groups through cuts in labour market programs, (3) reduce private sector employment in those firms affected by cuts to export assistance programs and (4) bring about further job losses through multiplier effects in the rest of the economy.

Even in the absence of a deflationary strategy, however, there are limits to the speed at which the economy can grow. While market orthodoxy blames impediments to the operation of market forces, such as trade unions and minimum wage regulation, Keynesian approaches locate the limits to growth in the market itself. Even in saving-investment equilibrium, the market may not deliver a full employment level of output. This does not require wage reductions, which restrict effective demand, but an expansionary fiscal policy to increase demand, output and employment. Yet it must also recognised that macroeconomic policy on its own will not overcome the limits set by the balance of payments constraint. This in turn calls for a more integrated approach to policy, including industry policy, labour market programs and industrial relations

reform. None of these policies on their own, or pursued as compartmentalised portfolio responsibilities, will be able to address the increasingly complex and challenging jobs task.

The key to overcoming Australia's balance of payments constraint is to create 'competitive advantage' through investment in the fast growing global markets for high valued added, knowledge intensive products and services. This will reduce our current account deficit by adding to exports and replacing imports, thus offsetting the net income deficit associated with servicing foreign debt. While the approach will not create many new jobs directly in manufacturing, it will increase the speed limit for expansionary fiscal policy, especially in public sector job creation. It also resolves the dilemma of having to choose between promoting low skill jobs, which help to reduce the unemployment stabilising growth rate, or a high skill, high productivity path which increases competitiveness at the cost of jobs growth. The latter option may not create direct jobs, but it can do so indirectly via the macroeconomic response to relaxation of the balance of payments constraint. If the response is to create a large number of low skill jobs in, say, community services, the unemployment stabilising growth rate may still be held down to manageable levels.

To sum up, achieving high productivity and high employment growth simultaneously will require a combination of (a) macroeconomic policy to increase demand and employment, (b) industry policy to raise the level and quality of capital accumulation, (c) labour market programs to address the needs of the long-term unemployed and disadvantaged groups, and (d) industrial relations reform to balance productivity with equity in wage determination. Consequently, in the strategy that we propose to reduce unemployment, the role of an independent tribunal like the AIRC will be crucial to maintaining an integrated labour market through an effective award framework and test cases, including fair award wage adjustments, equal pay and reduced working time. International experience demonstrates that the single-minded pursuit of productivity gains at the expense of socially derived notions of fairness and comparability in the wages system leads to a two tier labour market. It is unsustainable in the long-term as an employment strategy.

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