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HOW MILTON FRIEDMAN CAME TO AUSTRALIA: A CASE STUDY OF CLASS-BASED POLITICAL BUSINESS CYCLES

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In this [inflationary] situation a powerful alliance is likely to be formed between big business and rentier interests, and they would probably find more than one economist to declare that the situation was manifestly unsound. The pressure of all these forces, and in particular of big business – as a rule influential in government departments – would induce the government to return to the orthodox policy of cutting down the budget deficit. (Kalecki, 1943 [1990: 355])

Thirty years ago, in April 1975, Milton Friedman, came to Australia to declare that the world economic situation manifestly unsound.¹ Friedman asserted on that trip what Michael Kalecki predicted in his 1943 article would be the response of 'captains of industry' to Keynesian macroeconomic policies; it was that '...government expenditure financed by borrowing will cause inflation' (Kalecki, 1990: 348). A chorus of Australian businessmen and mandarin economists came out in support of Friedman, leading to the demise of Keynesian macroeconomic policy and the rise of neo-liberal policies. The contractionary process that

1 Milton Friedman, at the time was the Paul Snowden Russell Distinguished Service Professor of Economics at the University of Chicago; and acknowledged head of the 'Chicago School' of monetary economics, called 'monetarism'. A year later, in 1976, Friedman received the 'Bank of Sweden Prize in Economic Sciences in Memory of Alfred Nobel', confirming his status in the financial community and the neo-liberal mainstream of the economics profession during this period. At the time he was also a regular contributor to *Newsweek* magazine.

emerged was more than a short-term 'stop-go' fine-tuning exercise that Kalecki identified as a political business cycle (PBC). It was the start of a political trend, enabling the capitalist class to assert its economic and social dominance over labour and to cleanse the capitalist economies of inefficient businesses and oversupplied old capital stock.

This paper is a case study in the international transmission of ideas, namely how monetarism spread to Australia. It aims to identify an important watershed in Australian macroeconomic policy-making and the role that Milton Friedman, as the world's leading monetarist, played in this paradigm shift from Keynesian to neo-liberal (anti-Keynesian) economic policies. In the process, the paper uses Kalecki's PBC concept as a reference framework to understand how this paradigm shift came about and why the Friedman visit to Australia, financed by private businessmen, was pivotal in accelerating a paradigm shift. Conclusions from this case study of political business cycles indicate how an opposition political party in the Australian context can gain coherence and credibility for an alternative economic policy that initially was regarded as far-fetched. While Friedman's denunciation of the simple-minded Philips curve and other Keynesian precepts was known amongst Australian policy makers, the public reception (and in some cases, acclaim) of his visit paved the path for the official adoption of his policies. It was also a precursor of what was to later happen in Britain when monetarism entered public debate there, as Margaret Thatcher sought a new approach to economic management, including privatisation and major labour market 'reforms' (Jones, 1983).

Australian Economic Policy Prior to Friedman's Arrival

Inflation accelerated to a peak in 1974-75 of 16.7 % (measured by the consumer price index, CPI) or 20.8 % (as measured by implicit price deflator for domestic final demand, IDFDD).² This was extraordinary,

2 The CPI captures price changes in a basket of commonly bought consumer items, excluding capital goods. The IDFDD captures price changes from all components of final demand, including expenditures on capital goods and imported goods and services.

given that for most of the 1960s inflation was around four per cent by either measure (Junor, 1995: 40 & 49). As at August 1975 there was also 4.6 % official unemployment, compared to 1.6 % for the decade 1962-72 (Stegman, 1995: 64-5). The combination of the two resulted in stagflation (*stagnation with inflation*) that was unprecedented in Australian economic history but was reflective of similar dire economic conditions in other advanced capitalist economies around the globe. This climate of economic uncertainty was exacerbated by political uncertainty created by a reformist Whitlam Labor Government which, after many years in the opposition wilderness, wanted to take advantage of the strong and stable economic growth through the 1960s to benefit a broader sector of the Australian society. Into this world of uncertainty stepped Friedman, with assured presence and a simple recipe for returning to stable conditions.

The Whitlam Government was elected in December 1972 against a backdrop of a fully employed economy and even a one-off year (1972-73) of balance of payments surplus. The economic bounty suggested that it would be practical to implement Whitlam's election promises. The only apparent bugbear was that their predecessors, now in Opposition, had allowed an inflationary problem to linger. Annual IDFDD inflation rates of 6.5% (1970-71) and 7.3% (1971-72) were significant for the time, coming from both domestic cost pressures and rising import prices (Junor, 1995: 47). The prior McMahon Liberal-Country Party Government, by first refusing to deal with average wage increases of over 10% for 1972 and then by not revaluing the Australian currency to adequately reflect market conditions³, exposed the economy to underlying economic tensions. The Labor leader, E.G. (Gough) Whitlam, had little understanding or aptitude for economics and was committed to significant social reform through government spending despite these economic clouds on the horizon.

With the economy in boom through 1973, the Federal Treasury was aghast at the growth in outlays, and thus it advised caution. In his first

3 'The logical response was to revalue the dollar against the greenback [US dollar] by at least 7.9%. Instead, under pressure from Nationals [Country Party coalition partner], PM Billy McMahon came up with a revaluation of 6.3% - a formula for inflationary pressure' (Walsh, 2005).

budget as Federal Treasurer, Frank Crean allowed the inflationary problem to loom larger by allowing a significant growth in federal outlays financed by Treasury notes and cash balances with the central bank (Whitwell, 1986: 208). Fred Gruen, Whitlam's economic adviser, later recalled that the demand pressures building in 1973-74 were of 'a greater intensity' than anything since the end of World War II (cited in Whitwell, 1986: 208). A 25% tariff cut (July) and a further 4.8% revaluation (September)⁴ by the new Labor Government in its first year (1973) helped macroeconomic policy by diverting demand pressures to imports. There was also price control aimed at big business in the form of the Prices Justification Tribunal (PJT), which Chapman and Junor (1981) argue assisted in reducing the inflation rate from what it otherwise would have been without the PJT. However on the fiscal policy front, Crean – who had been Shadow Treasurer for twenty years – was not tough enough to exercise restraint on the growth in departmental expenditures that the Treasury felt advisable.

Australia's domestically generated inflation and unemployment problems were then exacerbated by the quadrupling of oil prices by the Organisation of Petroleum Exporting Countries (OPEC) cartel in the year from December 1973. Continuing strong wages expansion in the first two years of the Labor Government further facilitated a booming economy (Whitwell, 1986: 210-211). As a result, the wages share of national income rose at the expense of profits.⁵ An industry submission to the Cabinet from the Trade Development Council regarding the 1974-75 Budget suggested that the Government seemed 'unable or unwilling' to confront the inflation problem. The Council encouraged the Government to recognise that Australia's inflation was being led by wage-push factors, not by demand. It warned that higher unemployment was imminent though it would have some 'therapeutic' benefit.⁶

4 This is additional to a revaluation of the exchange rate of 7% by the Whitlam Government immediately it came to power in December 1972 (Jones and Perkins, 1981: 364).

5 This only partly redressed the 10% shift of the national product from labour to capital which occurred during the early 1950s under the Menzies Liberal-Country Party Government (Catley and McFarlane, 1981: p.78).

6 See 'Economic Conditions', Trade Development Council, A5925, 2431/EC, National Archives of Australia.

With fiscal policy already prescribed, the Labor Government moved to contain the inflation problem by sharply raising interest rates in late 1973. According to Whitwell (1986: 213-214), the subsequent credit squeeze went on for far too long and thus led to the subsequent recession. Firms and businesses were caught short, having built up their stocks and over-ordered to catch up with a booming domestic demand. Given the sudden appearance of weak markets, Australian firms could not easily pass on wage and other cost increases. Profit margins were further squeezed. Moreover, the public sector was increasing its command over resources at the expense of the private sector. This was the classic scenario predicted by Kalecki (1943) in his PBC perspective of the 'stop-go' Keynesian policy approach: i.e. strong cost-push inflation on top of demand pressures, together with increasing resources at the disposal of the public sector. This scenario was ripe for the Opposition leadership to exploit.

Into this macroeconomic cauldron came Dr. Jim Cairns, who was ideological leader of the Labor left and hero of the anti-Vietnam Moratorium Movement. During the May 1974 successful election campaign, Cairns:

...became Labor's most effective counter to the Liberal-Country Party thrust on inflation. He understood inflation as well as anyone on either side of politics and had a better capacity than most for reducing it to simple ideas suitable for political rallies, television and radio. (Ormonde, 1981: 170)

Cairns perceived inflation as the outgrowth of the pricing practices of multinationals (in Australia and from overseas), the military arms race and excessive wages growth.⁷ In this context, Cairns provided the left with an ideal standard-bearer in a period of economic crisis. Whitlam believed that too, so that, after his colleagues elected Cairns Deputy Prime Minister in June 1974, Whitlam suggested to Cairns that he should take over as Treasurer. Cairns initially rejected the suggestion, but eventually he was appointed in November of the same year (Ormonde, 1981: 181-86).

7 'Inside Dr Cairns', *The Australian Financial Review* 4 September 1974.

In a speech in October 1974 to the Labor faithful, Cairns told his audience he believed that the events of the years leading to 1975 could prove as significant for economic theory as those leading up to 1930. The only way to deal with inflation was through social reform' (Ormonde, 1981: 182). The problem of inflation he ominously attributed to 'the system'. His words were prophetic in hindsight but, as this paper argues, more in terms of Kalecki's view of how capitalists reassert their power, rather than Cairns's view of collective action of the masses supporting Labor.

Cairns's influence on economic policy preceded his own appointment to the Treasury. The 1974-75 Budget (handed down in September 1974 by Crean) became known as 'Cairns's Budget'. This budget was unorthodox in a period of very high inflation, providing urban renewal to deprived areas, low-income tax relief and a 33% increase in government expenditure, together with increased taxes for the business sector. The idea was to encourage union agreement for wage restraint, thus limiting the pass-on of international inflation through cost pressures in Australia. However, the budget was unacceptable to the business community. John Valder, Chairman of the Sydney Stock Exchange, '...saw the Budget as disguised socialism' (Ormonde, 1981: 180).

The 'captains of industry' needed a strong powerful voice to counter Cairns's growing popularity, influence and power,⁸ and to justify the suspension of fixed investment spending (a capital strike) that became apparent.⁹ Meanwhile, Friedman, through his monetary theory research, his simple messages in regular *Newsweek* columns and his persuasive personality, had developed a strong international academic profile as the leading monetarist. Friedman's strong pronouncements against government expenditure and support for an increased role for 'the market' provided Australia's powerful business interests with a perfect antidote to Cairns's 'socialism'. By the end of 1974, arrangements were under way for Friedman to visit Australia and express his views that

8 Ormonde (1981: 180-1) noted that in '...the wilderness of the western suburbs of Melbourne and Sydney the reaction to the Budget was optimistic.'

9 This is despite a mini-budget tax cut for individuals and companies on the 12 November. See 'Capital goes on strike and freezes spending' *The National Times* 24 March 1975.

counter-cyclical Keynesian economics (represented in Australia by Cairns) was 'manifestly unsound'.

In the context of the opening quote by Kalecki, the influential public institution that led the business orthodox position was, as Evan Jones articulates, Australia's central bank, the Reserve Bank of Australia (RBA) (Jones, 1983: 436). A week into his new portfolio as Treasurer, Cairns received a missive from the RBA Governor, Sir John Phillips, with his 'solution' to stagflation. The malaise in the business sector, Phillips felt, was deep-seated in character and could not be resolved by the re-emergence of a boom in spending led by government. Phillips felt it advisable that government expenditures and the rate of monetary expansion be reined back as inflation was badly disrupting business planning. The Governor articulated the new wisdom that when inflation is high and expected to continue, the choice between inflation and unemployment disappears; any action to create more jobs merely adds to inflationary expectations and, in turn, a further rise in unemployment. Apart from keeping wage pressures under check, reducing the rate of government spending would restore confidence to the private sector.¹⁰ Judging by his subsequent actions, Cairns was unimpressed with Phillips's advice.

Phillips's advice stemmed from the RBA's 1973 *Annual Report* that was noticeable for joining with the dominant economics government department, the Treasury, in arguing that inflation mattered more than unemployment. The dominant culture amongst the RBA's economists had recently become monetarist. It was symbolised the year before (1973) by the presence of a leading English monetarist, Michael Parkin within the Research Department.¹¹ Economists and senior officials within the RBA were the first to accept 'inflationary expectations' as a significant factor within the policy domain (McGuinness, 1975). Treasury economists, too, accepted the importance of inflationary expectations before comparable acknowledgement by their academic brethren (Stone, 2004: 267). Despite its misgivings about some of

10 Sir J. Phillips to J.F. Cairns, 18/12/1974, A 5931 CL 155, National Archives of Australia.

11 'Reserve Bank backs the Treasury line' *The Australian Financial Review* 28 August 1974.

Friedman's work, the Treasury became more monetarist in outlook following the salutary experience of late 1973 credit squeeze.

Apart from the neo-liberal tendencies of leading economists at Monash University (for example, Richard Snape and Michael Porter), the vast majority of Australian academic economists in 1974 did not accept the full gamut of the monetarist orthodoxy (Hughes, 1980: 44). They were 'mostly confirmed Keynesians' in their belief in the efficacy of fiscal policy (Nevile and Stammer, 1972: 9). At the instigation of Bob Hawke, then Federal President of the ALP and President of the ACTU, Victor Argy of the ANU (urged on by Trevor Swan) penned a letter which was counter-signed by 130 economists, supporting the Labor Government's economic policies, which it took to the 1974 May federal election (Guttman, 2005: 33; Butlin and Gregory 1989: 375-6). Hughes (1980: 44) argues that most Australian academic economists did not accept the charge by Friedman that Keynesianism was invalid. Jones (1983: 435) detected that, even in the early 1980s, most Australian economists remained, for several reasons, sympathetic to Keynesianism. Two groups of economists, one at the Melbourne Institute and the other at Adelaide, suggested policies inspired by institutional economist John Kenneth Galbraith (Friedman's major public opponent in the USA) that were broader than the standard 'stop-go' Keynesian approach, including wage indexation and taxes on speculation as more effective ways to curb inflation. Cairns articulated similar policy solutions at the time in order to, as he said himself, '...keep people in jobs and I'm not mesmerised by any economic theory' (cited in Ormonde, 1981: 215).

The Opposition's Shadow Treasurer, Philip Lynch, receptive to local monetarist voices, including some within his staff, had begun to reconstruct a new economic program distinct from the discredited policy platform taken into the 1974 election by the Coalition (Guttman, 2005: 43-46). Lynch entertained a hunch that Friedman's prophecies and mantras were something upon which to build a new credible alternative economic policy and also to develop a robust monetarist critique of Labor's economic policy. Cairns rebutted Lynch's parliamentary question on 9 April 1975, a question which implied that the ballooning government deficit was causing the rising inflation rate. Cairns said:

The deficit was aimed directly at the economy to increase production, to get the economy going and to employ resources wherever there are resources available for employment. The Labor Government will never see those resources remain unemployed because of a shortage of money. That battle was fought in this country 50 years ago and we are not going to fight it again.¹²

Barely more than a stone throw away in Canberra, Friedman had just finished an address to the National Press Club on how to control inflation by narrowing the role of government in the economy.¹³

The Friedman Visit

Friedman arrived from Chile to begin his Australian lecture tour on 1 April 1975. A Sydney stockbroking firm, Constable and Bain, under the leadership of Maurice Newman, arranged and financed his trip (Friedman and Friedman, 1998: 427-428).¹⁴ Newman, currently the Chairman of the Australian Stock Exchange, was described as a close friend who was also 'a convinced libertarian, a member of the Mont Pelerin Society'¹⁵ (Friedman and Friedman, 1998: 428). A veneer of academic gravitas came from a body called the Graduate Business School Club. QANTAS was also generous in its financing of the Melbourne fares for Friedman (CEDA, 1975: ii). A booklet published to mark the occasion declared that the purpose of the visit '...was intended

12 'Deficit budget best means to aid the economy', *The Canberra Times* 10 April 1975.

13 'Exchange control seen as violation of freedoms', *The Canberra Times* 10 April 1975.

14 Newman, now Chancellor of Macquarie University, recalls that the apart from having his trip and accommodation paid for, Friedman received a modest fee of \$5,000 for giving several public lectures. Since the trip was therefore financed by private funds, Friedman could not accept an offer from Peter Groenewegen to give the 1975 R.C. Mills lecture at the University of Sydney (Personal communication with one of the authors).

15 The Mont Pelerin Society, founded in 1947 by Frederich von Hayek and other European intellectuals, was a think-tank which espoused libertarian economics (Cockett, 1995, 100-121).

to heighten public awareness of the dangers of inflation and to point to possible cures consistent with the maintenance of individual liberty and free enterprise' (Friedman, 1975: 5). Apart from upholding all this, Newman was keen to inject more debate into the causes of inflation as he felt that the local discussion had become staid and wanting.¹⁶

Friedman had risen to pre-eminence with a simple restatement of the Quantity Theory of Money (QTM) in 1956, at a time when economists had accepted the received Keynesian wisdom that the QTM was obsolete (Friedman, 1956a).¹⁷ Like the monk Martin Luther, Friedman shocked the American economics establishment by putting forward, in a 1970 address entitled 'The Counter Revolution in Monetary Theory', his eleven theses on the relationship between monetary supply and output (Bernanke, 2003: 1-2). In short, Friedman held that controlling monetary aggregates was the key to dealing with the business cycle. The use of government spending to stimulate the economy and to provide jobs was counter-productive because such spending required additional and uncontrollable monetary growth. Friedman said the choice was not between inflation and unemployment but between some unemployment now or more unemployment later. As soon as workers realised that inflation was rising, caused by excessive government spending, wages would increase and, with it, unemployment; while the subsequent anti-inflationary medicine meant a higher amount of unemployment in the future. Inflation, he insisted, was not due to militant trade unionism or avaricious businessmen but rather was solely due to excessive monetary growth. Friedman's mission was to discredit Keynesian policies and the discretionary 'stop-go' macro-management of the economy. In its place came the panacea of allowing a measured increase in the money supply to guarantee economic stability through the market mechanism, while no budget deficits were permitted to fuel monetary growth.¹⁸

A leading economic journalist, Paddy McGuinness, unaware perhaps of Kalecki's remark (quoted at the start of this article) about hiring an

16 Personal communication with one of the authors.

17 The four subsequent essays in Friedman (1956b) are empirical studies by students of Friedman that purport to verify the Friedman restatement.

18 For a simply explained pro-monetarism book published at the peak of its short ascendance, see McCulloch (1982).

economist to disparage expansionary economic policy, suggested that the visit might induce other stockbroking firms and financiers to follow suit (McGuinness, 1975).¹⁹ McGuinness (who had studied aspects of monetarism at the London School of Economics during the 1950s) did not think that the visit would result in the 'sudden conversion' to monetarism simply because the process was well under way. Although this was true for some of the staffers in the backrooms of the Liberal Party who had entertained a monetarist agenda since the loss of the 1974 election, McGuinness overplayed just how far the conversion had gone. There were still strong believers in the conventional wisdom of Keynesianism both within the community and at the commanding heights of policy-making. The Friedman position, with its questionable theoretical and empirical elements, was also contentious within the mainstream economics profession.²⁰ A leading pro-monetarist book began its second edition with the statement: 'In 1975 when the first edition of this book appeared, monetarism was regarded as something of an eccentricity by most economists' (McCulloch, 1982: vii). This statement clearly shows that Lynch was courageous in persuading his party from 1974 onwards to adopt a monetarist approach (let alone trying to convince the 'rural socialists' in its coalition partner, the Country Party).

The impact of the Friedman mission to Australia (after his success in Chile²¹) was powerful and immediate. In part this was due to Friedman's own charismatic and persuasive appeal, as well as a generally compliant and uncritical media that was willing to give much space to his ideas. A pro-business thinktank, the Institute of Public Affairs, while not in agreement with Friedman's views on the expansion of the public sector, likened the visit to 'a breath of fresh air' (IPA, 1975: 29). Friedman's simple message about the causes of inflation appeared to clear away

19 Paddy McGuinness, a one-time economic adviser to Labor member, Bill Hayden, took up the monetarist cause with impressionable fervour (Guttman, 2003: 69-70).

20 For strongly critical responses to monetarism published around the time of its ascendance, see Kaldor (1982) and Nell and Azarchs (1984).

21 Frank (1979) describes how monetarism came to Chile and dominated macroeconomic policy in the late 1970s. Friedman's visit in 1975 was the initial foray after the USA-inspired overthrow of the democratically elected Salvador Allende government in Chile in September 1973.

some of the clouds of confusion about how to deal with stagflation. In general, the visit would shape the climate of economic opinion that the money supply mattered and that government should 'intervene' much less in the economy. This was the thin edge of the neo-liberal wedge, and it was Friedman who drove in the wedge by convincing governments of (as Kalecki puts it) the need for fiscal orthodoxy. Friedman's arrival would have as much impact upon the Australian political scene as his later forays to Britain during the early 1980s (Parsons, 1989).

Meanwhile, Cairns, the leading political advocate for anti-monetarism in Australia, was being isolated and diverted. Brian Brogan, his main economic adviser, '...was at this stage giving much of his time to hearings of the Jackson committee on manufacturing industry, of which he was a member' (Ormonde, 1981: 214). Brogan also felt he was no longer as effective, because Cairns's new Private Secretary, Junie Morosi, became the catalyst for Cairns's major personal transformation away from economics and into moral philosophy.²² At the executive policy level Cairns became isolated, with Morosi guarding access to him especially from Treasury officials (Strangio, 2002: 321-22). 'Consequently,...He had no regular personal confidante' (Ormonde, 1981: 214).

Friedman's eighteen-day visit was well publicised and provoked much comment in the media. Apart from addresses to business forums, banks and universities, Friedman also gave public addresses in Sydney, Canberra and Melbourne. His arranged meeting with Whitlam was cancelled because the Prime Minister had quickly ascertained who Friedman blamed for causing the inflation rate to soar (Friedman and Friedman, 1998: 430). Friedman did, however, observe Whitlam in a parliamentary question time session saying that he would rather listen to Bob Hawke than Milton Friedman about identifying the factor behind inflation (Friedman and Friedman, 1998: 431). Friedman did meet the ALP caucus Economics and Trade Committee and the Opposition front bench. He also gave seminars at the RBA and the Treasury. His views struck a chord in financial circles (representing 'rentier interests') and the

22 Morosi had no interest in economics and was heard to say 'What do we have on this Milton Friedman?' (Strangio, 2002: 321).

then relatively few bank economists, as there was an intellectual uncertainty over the correct economic policy that Australian authorities should adopt to deal with stagflation. The apparent failure of 'stop-go' Keynesianism to respond to stagflation fanned the growing uncertainty as to whether one could continue to have a nicely managed economy. Friedman reflected a libertarian belief that it was time for governments to assume less omnipotence in the art of economic management and to adopt a political agenda of smaller government with less interventionism.

Friedman was the salesman for offering something less grand. Nicholas Kaldor, (1982: 78) a leading Cambridge Keynesian economist, described monetarism as a new doctrine '...assiduously propagated...by a growing band of enthusiasts, combining the fervour of early Christians and selling power of a Madison Avenue executive'. Friedman was both messiah and showman. *The Economist* (1970) had once described Friedman as 'able to argue the hind leg off a horse'. He was also, as Australia was to see, an adept television performer. Friedman appeared on the ABC-TV program *Monday Conference* which, given its popular impact, was repeated six weeks later. In the audience were economists like Colin Clark, Heinz Arndt and Duncan Ironmonger who came away convinced that much of Friedman's analysis and policy was probably correct. Both Clark and Arndt took the opportunity to criticise Cairns's handling of the economy as 'irresponsible', with Arndt forecasting that inflation would climb to over 30% if government spending continued at its current rate.²³ Ironmonger, from the University of Melbourne, prefaced a question to Friedman with the gushing remark 'A lot of what you are saying is agreeing with a lot of what we're saying. A lot of sense is being said which is comfort to us' (cited in Hughes, 1980: 43).

At Friedman's opening seminar, organised by Newman and held in Sydney before a capacity audience of 500 people mostly drawn from the business sector, a presiding panel of four economists was seen nodding in agreement at his discourse and the way he fielded answers.²⁴ Considerable support for the Friedman line began to build during the visit and continued to strengthen after the visit, with credible academic

23 'Moderate cut sought in currency rate', *The Canberra Times* 22 April 1975.

24 'Friedman deflates indexationists', *The Bulletin* 12 April 1975.

defence of the position and a compliant media enthralled by the new wisdom. Friedman's public speeches were replete with continual reproduction of the same message in neat phrases, adorned with pseudo-scientific but simple graphs linking the growth in money supply with the subsequent inflation rate.²⁵

During the same month the leading Cambridge left-wing Keynesian economist Joan Robinson entertained Australian audiences.²⁶ She was also given some airplay to announce her views on inflation and other economic matters. In her own *Monday Conference* program, also televised in April, and subsequently in her R.C. Mills lecture at the University of Sydney, she accused Friedman of engaging in a sleight of hand by deliberately confusing the money supply with money expenditure as a cloak to recommend deflationary economic policy.²⁷ Robinson, like Cairns, saw cost-push inflation as the outcome of a sociological struggle between capital and labour over the national income. In order for inflation to be expressed, she conceded, the money supply must increase, but only as a consequence of demands of trade coming out of this struggle and the consequent profit and wage increases. This tended to give legitimacy to Friedman's argument in the eyes of the 'captains of industry' and their supportive acolytes. When Maurice Newman (organiser of the Friedman visit) asked Robinson about the primacy of the money supply and received what, to his mind, was an unsatisfactory response, he remarked in a high-handed manner: 'I think we'd be here all night debating backwards and forwards and I'm sure that we wouldn't achieve much purpose because I couldn't convince Professor Robinson, and I'm sure she couldn't convince me'.²⁸ In a spirited, witty performance Robinson turned the 'fight inflation first'

25 John Nevile, at the time Professor of Economics at the University of NSW (now Emeritus Professor), was Chairperson of the Sydney public address. When one of the authors asked Nevile in late 2004 to recall that address (published in Friedman 1975), his one memory was the annoyance that he felt when Friedman presented simple graphs that were not the ones that Friedman had published in recognised academic journals. The latter were more complex and with significant qualifications and limitations stated in the published form.

26 'Professor Joan Robinson, the first left-wing Keynesian economist in Australia too', *National Times* 28 April, 1975.

27 *Monday Conference* ABC transcript, 28 April 1975, 4.

28 *Monday Conference* ABC transcript, 28 April 1975, 5.

credo on its head by saying that the credo itself was by definition inflationary as it reduced aggregate output, creating supply constraints.

Robinson also stated that monetarism took on some rather unsavoury political attributes by using unemployment as a means to suppress wage demands, a view often expressed by Cairns himself. However, Robinson did not help Cairns's case by assailing what she called 'Bastard Keynesianism' (see Robinson, 1975). In her R. C. Mills lecture at the University of Sydney, when she stated that she did not subscribe to indiscriminate use of deficits in a 'stop-go' manner, libertarians saw this as a swipe against Cairns's budget policy. They ignored Robinson's strong statement of her abhorrence of any macroeconomic policy that increased unemployment.

Aftermath of Friedman's Visit

In the televised *Monday Conference* exposure of the two economic titans (Friedman and Robinson), events would suggest that Friedman won the battle in terms of public exposure and simplicity of argument. In terms of political impact, the Friedman visit exceeded all of Newman's expectations. Some of those who attended Friedman's lectures came away with a distinctly monetarist outlook (Guttman, 2005: 58). Friedman's pronouncements gave much needed credibility to the Liberal's economic policy platform erected by Lynch. Brian Buckley, press agent to Lynch, recalled that (even then) Friedman had 'celebrity' status that allowed followers to say to detractors 'Well, as Milton Friedman says, contradict that if you are game' (Guttman, 2005: 57). Friedman's arguments also strongly appealed to the big business sector and rentier interests, particularly his notion of 'crowding out'.²⁹ His visit nourished the views of private sector economists like David Love of Syntec who had been charting the money supply as a guide to nominal

29 'Crowding out' is 'Where increased public expenditure diverts money or resources away from the private sector' (Sloman and Norris, 2002: 565). Nevile (1995) provides a strong critical theoretical and empirical evaluation of this concept in the Australian context.

income fluctuations. The RBA also began to issue graphs showing the rate of monetary growth in its statistical bulletins.

An astute player in public relations, Friedman made no reference during his visit to Cairns's views on money and unemployment. To bolster monetarism in response to the Friedman visit, an opposition politician, Bert Kelly, sarcastically asked the Treasurer in Parliament: that 'If printing money is a good solution why not print more of the stuff and get rid of the unemployment problem altogether?' Cairns rather foolishly replied that 'We might do precisely that' (cited in Ormonde, 1981: 213). It was a damaging admission, for monetarism and the 'inflation-first' position was winning over adherents even within the Labor Party. Brogan conceded that by this time some within the Cabinet agreed that inflation and unemployment were positively related and not negatively as specified in the standard Keynesian-Philips curve analysis.³⁰ Even Cairns had earlier criticised the Liberals for bestowing the current inflation upon Australia by allowing excessive monetary growth to occur while in office. Cairns's parliamentary response to Kelly was immediately damaging to his credibility, with the financial press critical of his understanding of the processes of inflation.³¹ Then in early May, speaking as Acting Prime Minister, Cairns said there would be big cuts in government spending, in the hope that this would moderate growth in money supply, and declared that '...the main problem facing Australia today is inflation' (cited in Ormonde, 1981: 215). The Keynesian citadel had been truly breached from the inside.

Despite Cairns's acknowledgment of the need to moderate money supply growth, he remained essentially Keynesian. On the 8 May 1975 he wrote in a confidential Cabinet submission on budget strategy for 1975-76, that for the control of inflation '...money supply should not be treated as a *primary* instrument' (Cairns, 2005: 3, original emphasis). Cairns regarded fiscal policy and wages/income policy as much more important. Cairns supported Robinson by going on to state that money supply should '...be adjusted to meet the needs of the economy' (Cairns, 2005:

30 'The big risk: Inflation could hit 30 per cent plus' *The National Times* 14 April 1975.

31 'More public spending is not what the doctor should order' *The National Times* 21 April 1975.

7). Reducing inflation '...without causing unacceptable unemployment, production losses and surplus capacity' (Cairns, 2005: 12) was predominant in the Cairns budget strategy. John Menadue, Head of the Department of Prime Minister and Cabinet, was critical of Cairns's Cabinet submission which reflected a strong Monetarist position. Menadue argues that '[t]he Treasurer's submission is very vague on monetary policy' and '...does not make clear, in our view, ...that *containment of the present excessive rate of monetary growth requires a substantial reduction in the prospective budget deficit*' (Menadue, 2005: 4 & 2, original emphasis). Senior economics-based public servants, led by Menadue, were clearly undermining the Treasurer.

Cairns's chief rival in economic policy, Bill Hayden, became the new Treasurer on 5 June 1975, and presented the 1975-76 Budget with an 'inflation first' focus.³² Hayden proclaimed that Australia was no longer living in '...the simple Keynesian world in which some reduction in unemployment could, apparently, always be purchased at the cost of more inflation. Today it is inflation itself which is the central policy problem. More inflation simply leads to more unemployment'.^{33 34}

By August 1975, the Whitlam Government had made a belated attempt to gain some political traction by adopting a mild form of monetarism. However, this rapid change in economic thought and practice arguably undermined its credibility while conceding ground to the Liberal-Country Party Opposition and to what was fast becoming the new 'conventional wisdom' in the public perception. This perception was vindicated by a well-timed announcement, bestowing the 'Bank of Sweden Prize in Economic Sciences in Memory of Alfred Nobel' onto Friedman in October 1976, which gave further legitimacy to monetarism.

32 With public confidence in him sagging, Cairns was removed from the Treasury portfolio by Whitlam. He was later removed from the entire ministry after being found guilty of an impropriety to do with overseas loan-raising while serving as Treasurer.

33 W.G Hayden, *Commonwealth Parliamentary Debates*, 19 August 1975, 53.

34 Over a year later the British Prime Minister James Callaghan told the annual meeting of the British Labour Party essentially the same thing, namely, that Keynesianism, in an inflationary environment, no longer worked (Morgan, 1997: 507).

Despite the Nobel Prize, the Friedman position remained somewhat contentious within the mainstream economics profession because of its questionable theoretical and empirical elements. For the next two decades, all the mainstream textbooks carried a chapter on the Keynesian versus Monetarist debate. However, politically, the debate had been clearly won by Friedman at the head of his monetarist brigade. The Friedman visit to Australia was followed by two publications, CEDA (1975) and Friedman (1975). The latter was a small, cheap monograph that sold very well and appeared on many economics teachers' bookcases throughout Australia. The Friedman *Monday Conference* programme was illegally copied in schools and universities, to be shown endlessly over the next few years.

'Operation Friedman' had some strong aspects that led to its overwhelming success: (i) a protagonist (Friedman) who was charismatic, persuasive and exuded credibility; (ii) a compliant and uncritical media that was willing to give much space to the visit; (iii) some domestic economists (especially in powerful positions of economic management) springing to the defence of this questionable theory; (iv) business interests supporting (financially and credibility-wise) the whole operation and becoming convinced that the message was getting across to the masses; and crucially (v) a confused, vacillating and sometimes complacent 'Keynesian' leadership (both politically and academically).

Friedman and the Political Business Cycle

A close observer of the drama of the Whitlam years recalls that the Friedman episode shows the '...ability of ideas to shape one conception of the world as powerfully as events themselves' (Hughes, 1980: 114). In Australia, the tide of events had certainly conspired against standard 'stop-go' Keynesianism but the visit of an eminent economist, who injected new ideas of economic management into the public domain, was a decisive element. Inflation was the new economic issue of the time and Friedman was undoubtedly the man of the hour. In the context of the thirty-year anniversary of this watershed visit, it is its lasting effect that provides a clear example of what Kalecki predicted was the basic contradiction of Keynesian economic management: the lack of

commitment by powerful groups within capitalism to provide what Galbraith (1977: 197) called 'Mandarin controlled capitalism' which would allow for permanent full employment and a more equitable distribution of resources. Kalecki wrote that any such attempt would be undermined, creating a 'stop-go' political business cycle (PBC).

Keynes (1936) expressed the faith that the power of his effective demand idea would be used to stabilise the business cycle at full employment. Kalecki (1943) also recognised the powerful tool of effective demand management (given that he developed this same analysis in 1933), while also emphasising the stronger power of business interests to prevent this process from occurring. Kalecki specified three fears that capitalists would have with Keynesian full employment: (i) loss of *economic* control, as public policy demand management would effectively deprive capitalists of their power to influence economic conditions and also governments themselves; (ii) loss of *policy* control as governments extend their impact through their own investment spending into the areas regarded as businesses' legitimate sphere of influence (e.g. transport, public utilities); (iii) loss of *industrial* control of the workforce if full employment is maintained over the long-run, so that 'the sack' ceases to play its disciplinary role for businesses. Responding to these three concerns businesses' state of confidence would be reflected in investment decisions and the business cycle that they generate.

Towards the top of the expansion phase of the cycle, the combination of profit squeeze and inflationary pressures can be expected to manifest itself as an adverse shift in business confidence. This is reflected in profit rates falling, financial gearing rising and capacity utilisation falling as large capital investment projects come on stream at the time when growth in consumption is slowing down (Courvisanos, 1996). Business interests and rentier interests then welcome mainstream economists identifying the economy as 'unsound', as per the opening Kalecki quote. Pressure is placed on governments to renege on full employment commitments and to introduce the 'stop' elements of fine-tuning by dampening effective demand through the use of monetary and fiscal policy instruments. This ensures the demise of old capital stock and the reduction in real wages, essential for the renewal of capitalism (Galbraith

and Darity, 1994: 459-68).³⁵ During the 1950s and 1960s, this approach seemed to ensure the sustainability of the 'stop-go' form of Keynesianism in Australia as both sides of the political spectrum played out their ritual roles within this paradigm.

The 'stop-go' fine-tuning economic management approach was a clear indication of how governments had 'bastardised' Keynesian economics to suit their short-term economic interests, especially after much of the means of production were destroyed during World War II. The major shift in economic conditions in the early 1970s, following the 1974 OPEC oil price rises and consequent huge international capital flows, resulted in the business sector not being satisfied with the 'bastardised' Keynesian *status quo*. This applied particularly to financial capitalists who stood to lose the most under the rising world-wide inflation. They acted by using Friedman in the USA and also on a global tour that included countries where the USA had considerable financial interests (Chile, Australia, South Africa).

A new form of PBC emerged with the advent of the Friedman world tour. This is the Steindl (1979) version of Kalecki's PBC outlined below, which sees a paradigm shift in policy-making from the Keynesian 'stop-go' mechanism to the neo-liberal political trend incorporating contractionary macro policy with minimal statism. Friedman, as an effective showman, served as a valuable ideologue (in the Kaleckian sense) to usher in the paradigm shift in Australia. Friedman, whilst in Australia, managed to influence government departments, support financial interests and provide much rational justification for a compliant press to disseminate. The neo-liberal political trend was being set in place in Australia as it was in other western economies, and Friedman assisted the intellectual and political acceptance of this long-term objective. The Australian context was particularly interesting in that a popular new Prime Minister's creditability was being undermined from within its own ranks through economic incompetence, social angst and political opportunism. However, it was Friedman and the Monetarist

35. Kennedy (1973) provides empirical support in the U.K (1953 to 1971) for a 'predominantly' planned 'stop-go' policy approach, with technical errors due to poor forecasting playing only a relatively minor role.

approach that made the neo-liberal alternative paradigm attractive and legitimate in Australia as well as in the other countries going through the same broad economic and political processes at around the same time.

Steindl (1979), Bhaduri and Steindl (1983) and Catley and McFarlane (1981) used the analysis pioneered by Kalecki (1943) to explain the long-term implications of the PBC in terms of a 'political trend'. These studies draw on the historical development of advanced capitalist economies like the USA, United Kingdom and Australia to show that the shift in economic policies in the early 1970s from Keynesian 'stop-go' policies to Friedmanite monetarism and neo-liberalism was due to the same three fears identified by Kalecki (1943) and outlined above. The difference is that in this version of the class-based PBC a longer timeframe allows for what Mair and Laramie (2002: 568) refer to as '...feedbacks between capitalists and workers over the political and social tensions of full employment to work themselves through.' These feedback effects generate rent-seeking behaviour by powerful monopoly control interests who form 'distributional coalitions' of rentiers and big business to shift profit shares upwards by establishing obstacles on the road to full employment with contractionary fiscal budgets and reduced monetary growth. Mair and Laramie (2002) provide empirical evidence from the United Kingdom to reveal that the end of the post-war full employment-based 'stop-go' strategy in the early 1970s coincided with the only significant period of income share turbulence. Aschauer (2000) sets out empirical evidence for the USA that supports this contractionary political trend with the decline of public investment since the early 1970s. Catley and McFarlane (1981) provide similar historical evidence for Australia which reinforces the argument of how crucial Friedman's visit was to the commencement of this shift from 'stop-go' PBC to 'political trend' PBC.

Conclusion

The changing political and economic conditions in the mid-1970s enabled the capitalist class to assert its economic and social dominance over labour and to 'cleanse' the economy of inefficient and oversupplied old capital stock built up during the early post-World War II period of protective regulatory capitalism. This is the significance of the Friedman

visit; it provided a paradigm shift to neo-liberalism - a political stance where by governments abandoned the Keynesian ideal of full employment and more equitable distribution of resources. Instead, government's role came to be seen as a limited one that ensures inflation is contained. Beyond that, government should stay out of the economic system in order to allow the market mechanism to operate for the benefit of shareholders and the managers of capital.

The media obsession with the monthly movements in the interest rate and the maintenance of low inflation is, thirty years on, a partial legacy of Friedman's visit, outlasting the temporary victory of a questionable monetarist theory and money supply targeting that was practised up till 1985. What followed after 1985 was a more substantial overhaul of the macroeconomic policy agenda towards 'inflation-first', less interventionist, strategies as a medium-term objective. In Australia, Friedman was the bulwark that helped to justify the initial neo-liberal political shift. This article shows that the shift can be understood in terms of a Kaleckian 'political trend' political business cycle.

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