Internationalization and Two Liberal Welfare States
Australia and New Zealand

HERMAN SCHWARTZ

3.1. Introduction

Australia and New Zealand differ in four ways from the other cases here. First, relatively weak manufacturing sectors rendered them vulnerable to international economic pressures earlier, necessitating "stop-go" policies that constrained employment protection and the elaboration of social policy early in the postwar period. Second, their employment and social protection models are quite different from the typical European model, and they created dynamics that amplified those international vulnerabilities over time. Third, these dynamics created crises that led to earlier and more profound transformations of their employment and social protection models. A relatively high dependence on foreign investment inflows to spur growth and cover chronic current account deficits combined with relatively liquid share markets and early financial liberalization to amplify pressures for transformation of their models. In particular, chronic balance of payments deficits made politicians and financial bureaucracies sensitive to falling exchange rates (which increased the real cost of foreign currency denominated debt), to interest rate shocks (including credit rating downgrades), and to the distribution of risk between the public and private sectors. Fourth, both countries have Westminster systems of government that permit governments anchored in minority voter blocs to change things rapidly.

'Golden age' Australia and New Zealand turned common European patterns of social and employment policy upside down. Employment policy in the antipodes operated primarily through trade policy (protected import substitution industrialization [ISI]), while social policy operated

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1 Except where noted, all data here, including in the Figures, are from OECD, Economic Outlook, various dates.
primarily through judicial regulation of wages and the labor market. What we will here call the informal welfare state—the whole range of state policies supporting delivery of a socially defined wage in a full employment environment—was thus much more important than the formal welfare state—tax-financed, state-provided transfers and services. Australia’s and New Zealand’s common history as highly indebted primary product exporters explains social and employment strategies based on ISI and informal welfare (Mabbett 1995; Schwartz 1998). These strategies generated internal dynamics and faced external trends that threatened to price their largely primary product exports out of world markets. Social policy—that is, judicially regulated wages—reversed the usual Scandinavian dynamic and pushed up costs in the sheltered sector of the economy in order to shift rents out of the exposed sector. Employment policy—that is, ISI—constantly expanded the sheltered part of the economy. But because Australian and New Zealand primary product exports faced declining and volatile terms of trade, accompanied by slow volume growth, eventually the sheltered sector got too big for the exposed sector to support, necessitating some change in the model. Foreign direct investment largely financed ISI, while direct borrowing overseas financed recurrent current account deficits. This pattern of borrowing and investment simply shifted the locus of foreign pressures from one kind of burden to another, in two directions: away from volatile prices for primary goods and onto maintenance of the exchange rate, and away from the exchange rate onto wage developments in the sheltered sector. These dilemmas had already emerged in the late 1960s, but became acute in the 1970s.

Despite their similar ‘golden age’ models, these two countries displayed enough divergence in three critical variables so that their economies did not run along absolutely parallel lines after 1973. Australia’s and New Zealand’s different responses to the crisis of their respective ‘golden age’ models are best explained by divergence in the patterns of institutional representation for organized interests, in union structures (and thus in attitudes about the possibility of working within existing collective bargaining arrangements), and in notions about what constituted the social wage. Put simply, one combination of state structures, union structures, and the moral economy generated a Labour Party-led neo-liberalism that changed New Zealand more profoundly (in many respects) than Thatcher changed Britain, while a different combination of state structures, union structures, and moral economy allowed the Australian Labor Party (ALP) to produce a more gradual corporatist restructuring of labor markets and the state. The initial transformations sponsored by the left, in turn, structured even greater divergence in the intensity of change when right-wing governments replaced each labor party in 1990 and 1996, respectively.

State power in the collective bargaining arena was much more robust in Australia than in New Zealand, providing an institutional arena in which corporatist compromises could be enforced. Second, Australia’s labor movement was much more centralized than New Zealand’s, and the same is true of their respective business communities. Relatively greater organization for labor and business meant that a compromise program for adaptation could be negotiated and, conversely, that efforts to ‘smash through and crash through’ were much less likely to succeed. In New Zealand relatively fragmented manufacturing and labor communities were unable to articulate compelling compromise responses to international pressures. Finally, the values unpinning unions’ and voters’ ‘moral economy’ determined whether compromise positions would find electoral support, giving parties with programs for adaptation time to reorganize employment and social policy.

Thus, in Australia the Labor Party was able to transform implicitly corporatist collective bargaining structures into open corporatist structures, to expand the social wage, and to redistribute an expanded employment base until a more neo-liberal coalition government came to power in 1996. The Labor Party also systematically introduced competitive pressures into most product and service markets. 1980s Australia thus most closely resembles the post-Wassenaar Netherlands or Belgium after the decision to tie wage increases to those in Belgium’s seven largest trading partners. In New Zealand the Labour Party put forward similar policy proposals but could not make them stick, and eventually it turned to more radical attempts at replacing the old model of protected employment with pure market forms. Then the successor National Party government replaced socially defined wages with market wages. Both of these governments also systematically introduced market competition into most product and service markets. New Zealand thus resembles a more systematic and theoretically rigorous version of Thatcher’s ad hoc reorganization of the British economy.

Differences between Australia’s and New Zealand’s Westminster systems of government also matter, but not much. Until 1996 New Zealand’s system clearly gave electoral minorities with parliamentary majorities tremendous leeway to implement their agenda. Australia’s version of proportional representation and its strong upper house tends to retard proposals for change, particularly when they emanate from a party representing only a plurality of voters. But this institutional difference only conditions the rate of change, not its direction. Table 3.1 presents a precis of electoral and constitutional structures.

The discussion below combines perspectives on Australia’s and New Zealand’s very similar ‘golden age’ models. The discussion then turns to
Table 3.1 State institutional structures, c.1970

<table>
<thead>
<tr>
<th></th>
<th>Australia</th>
<th>New Zealand</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>State</strong></td>
<td>Federal, central government funds but state governments control tertiary education, health, and social assistance</td>
<td>Unitary; local government has no independent status</td>
</tr>
<tr>
<td><strong>Legislature</strong></td>
<td>Bicameral, effective upper house</td>
<td>Unicameral</td>
</tr>
<tr>
<td><strong>Elections</strong></td>
<td>Lower House: single transferable vote Senate: proportional representation, thus minority parties exist in Senate</td>
<td>First past the post, single-member districts, thus majority parties from plurality vote shares</td>
</tr>
<tr>
<td><strong>Parties</strong></td>
<td>Labor, Liberal (urban bourgeoisie), National (rural bourgeoisie)</td>
<td>Labour (largely urban), National (largely rural), Social Credit (rural protest)</td>
</tr>
<tr>
<td><strong>Typical government</strong></td>
<td>Coalition Liberal—National, majority in House with 40–50% of voters, minority in Senate</td>
<td>National Party majority, with 40–45% of voters</td>
</tr>
</tbody>
</table>

*For simplicity's sake I will use National Party to designate its predecessors, the Country Party and National-Country Party.

serial consideration of their divergent responses to the shocks of the 1970s and 1980s, looking first at the unraveling of their models, then at their reconstruction. The conclusion illuminates the similarities and differences between the two countries.

### 3.2. ‘Golden Age’ Australia and New Zealand

Australia's and New Zealand's essentially similar employment and social policies worked differently from European models. In Australia and New Zealand, employment policy operated through trade policy. Both governments deliberately sheltered local manufacturing from world markets in order to encourage import substitution industrialization (ISI) and thereby generate employment. Both governments shifted rents from efficient primary product exporters toward the protected parts of the economy to induce ISI. In Australia and New Zealand, social policy operated through judicially set wages (Castles 1989). Formal, state-run arbitration courts.

set wages at socially defined levels rather than leaving them to market forces or free collective bargaining. This created highly structured labor markets in which both unions and business organizations were often little more than appendages of the state. Consequently, in contrast to Europe, where taxes and transfers level out the unequal incomes labor markets produce, here incomes are leveled in the labor market itself, and taxes and transfers do minimal work. The typical worker receives around 90 percent of his or her income from wages, unlike the Scandinavian combination of 70 percent from market wages and 30 percent from government transfers. Both countries thus had relatively limited formal welfare states (i.e. a European-style social policy) at the beginning of the 1970s, because both accommodated most new social demands by retooling the arbitration system rather than creating new welfare programs. For example, formal disparities between female and male wage levels were removed in the 1970s. Both countries thus had relatively little in the way of an active labor market policy, because they responded to rising unemployment with growing trade protection. So long as trade protection and robust raw materials exports generated full (male) employment, these small formal welfare systems adequately handled residual pockets of poverty. Relatively speaking, Australia relied more on high, socially defined wages and New Zealand more on an elaborated formal welfare state.

#### 3.2.1. Employment Policy by Other Means

Australia and New Zealand used high tariffs and import licensing to generate local full employment. These trade policies, in turn, accommodated the relatively high direct and indirect wages in the manufacturing sector that arbitration created. In tandem, full employment and high wages obviated the need for many of the tax-funded transfers and services common in Europe. The effective rate of protection for manufactured goods—that is, the share of value added by tariffs—averaged between 60 and 70 percent in New Zealand and 46 percent in Australia, and reflected deliberate efforts to generate more employment (OECD 1972: 29–31, 1989: 39). In Australia, the Tariff Board literally told industrial firms, ‘You make it and we’ll protect it’ (Capling and Galligan 1993: 105). The deliberate suppression of manufactured goods imports gave both economies relatively low levels of trade compared to similarly sized OECD economies (see Table 3.2).

Exports of foods and raw materials from their highly efficient primary sectors funded residual imports of manufactured goods. In New Zealand, dairy, meat, wool, and timber accounted for about 76 percent of exports, while in Australia coal and other ores, wool, meat, wheat, and dairy
Table 3.2 Trade structure, various indicators, 1961–1997

<table>
<thead>
<tr>
<th></th>
<th>Australia</th>
<th>New Zealand</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trade (% of GDP)</td>
<td>31.8  32.0 40.4</td>
<td>36.6  47.8 60.4</td>
</tr>
<tr>
<td>Compare (Sweden)</td>
<td>42.3  70.6</td>
<td>49.5  64.0</td>
</tr>
<tr>
<td>Wool</td>
<td>41.4  13.8 7.2</td>
<td>33.0  18.8 6.0</td>
</tr>
<tr>
<td>Meat</td>
<td>9.2   10.3 3.2</td>
<td>24.2  33.5 16.8</td>
</tr>
<tr>
<td>Dairy, fruit, fish, sugar</td>
<td>13.3  11.7 2.9</td>
<td>25.3  23.1 28.7</td>
</tr>
<tr>
<td>Metals, ores, aluminium</td>
<td>7.3  10.0 17.1</td>
<td>0.0  0.0 3.7</td>
</tr>
<tr>
<td>Coal, oil, fuels</td>
<td>5.8  19.3 0.0</td>
<td>0.0  0.6 2.7</td>
</tr>
<tr>
<td>Australia: cereals</td>
<td>9.4  12.1 7.5</td>
<td>—  —  —</td>
</tr>
<tr>
<td>NZ: Forestry (+ pulp, paper)</td>
<td>—  —  —</td>
<td>1.3  5.8 10.0</td>
</tr>
<tr>
<td>RAW MATERIALS SUBTOTAL Manufactures</td>
<td>80.6  63.7 57.2</td>
<td>83.8  81.8 67.9</td>
</tr>
<tr>
<td>Commodity based</td>
<td>18.3  11.0 9.7</td>
<td>19.4  11.0 7.3</td>
</tr>
<tr>
<td>Non-commodity manufactures</td>
<td>—  15.0 22.5</td>
<td>—  9.0 17.0</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>23.9  11.2 3.5</td>
<td>53.0  35.9 6.4</td>
</tr>
<tr>
<td>Europe (exc. UK)</td>
<td>15.9  9.4 8.7</td>
<td>16.9  11.6 9.2</td>
</tr>
<tr>
<td>United States</td>
<td>7.5  11.9 8.1</td>
<td>13.1  16.1 11.9</td>
</tr>
<tr>
<td>Japan</td>
<td>16.7  27.1 22.9</td>
<td>2.9  9.8 14.7</td>
</tr>
<tr>
<td>Rest of world</td>
<td>36.0  40.7 56.8</td>
<td>14.1  26.6 57.8</td>
</tr>
</tbody>
</table>

n.a. = not available.
Sources: OECD, Economic Surveys, Australia or New Zealand (Paris: OECD, various dates).

Australia and New Zealand

used government ownership and regulation of services to absorb labor. In both, manufacturing and services contained considerable hidden unemployment.

Protection funded itself by inducing inflows of foreign investment (see Table 3.3). In New Zealand, foreign firms accounted for 20 percent of employment and, because their productivity typically exceeded that of local firms, 26 percent of value added by the end of the 1960s. Foreign firms dominated most of the durables sector and a substantial part of the non-durables, leaving light consumer durables and non-durables to local firms. New Zealand’s small domestic market limited economies of scale and the incentive to use capital-intensive production processes, leaving most enterprises labor-intensive and inefficient. Firms with fewer than 100 employees generated over half of employment by the 1970s; the average firm had 30 employees. The 5 percent of firms employing over 100 people were typically capital-intensive export processing operations like meat packing or subsidiaries of multinational corporations (Gould 1982: 108; Hawke 1985: 258–59, 274; OECD 1975: 42).

By the end of the 1970s, foreign firms controlled about one-fourth of Australian manufacturing and half of mining as measured by value added (OECD 1972: 42; UNCTC 1988: 529). As in New Zealand, much of the employment that ISI generated was actually disguised unemployment. Australian firms achieved somewhat greater economies of scale than their New Zealand counterparts, but they remained uncompetitive and unable to export. In automobile manufacturing, Australian labor productivity was less than half the Japanese average. Similarly, consumer durables firms amounted to about 65 percent of exports. In 1970 both countries were still substantially oriented towards traditional European markets, but Australia’s minerals exports were already diversifying its customer base towards Asia. The shift to minerals exports and toward Asia gave Australia much stronger growth, a better balance of payments situation, and higher average incomes than New Zealand in the 1960s and 1970s. Australia’s and New Zealand’s efficient primary sectors absorbed relatively little labor, and their employment share fell continuously after 1945. Only 6.5 percent of Australia’s labor force worked or mined (slightly more than in Sweden), and 8.6 percent of New Zealand’s (again, slightly more than in Denmark). Both countries oriented their industrial policy around protecting manufacturing to generate employment growth, and both also

Table 3.3 Inward foreign direct investment, c.1980

<table>
<thead>
<tr>
<th></th>
<th>Australia</th>
<th>New Zealand</th>
</tr>
</thead>
<tbody>
<tr>
<td>MNCs % share of manufacturing employment</td>
<td>26.7</td>
<td>n.a.</td>
</tr>
<tr>
<td>Profits of MNCs as % of profits of all firms</td>
<td>22.6</td>
<td>28.9</td>
</tr>
<tr>
<td>Book value, MNCs capital stock, as % of GDP</td>
<td>10.7</td>
<td>10.0</td>
</tr>
<tr>
<td>MNCs % share of employment (Australia) or assets (New Zealand), 1981 in</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chemicals</td>
<td>59.6</td>
<td>86.4</td>
</tr>
<tr>
<td>Transport equipment</td>
<td>45.0</td>
<td>56.5 (metals)</td>
</tr>
<tr>
<td>Electrical equipment</td>
<td>37.1</td>
<td>55.5</td>
</tr>
<tr>
<td>Coal and/or petroleum</td>
<td>80.8</td>
<td>n.a.</td>
</tr>
</tbody>
</table>

n.a. = not available.
MNC = multinational corporations
*Data vary, 1978 through 1982-83
had an estimated 25 percent cost disadvantage based on diseconomies of scale alone (BIE 1983).

3.2.2. Social Policy by Other Means

Australia and New Zealand have fairly minimal formal welfare states by European standards, because their arbitration courts achieve European social welfare goals by setting wages at high levels, mandating occupational welfare, and regulating work conditions, while tariff protection generates full employment. The arbitration system structures collective bargaining and, thereby, both employee and employer organizational patterns.

3.2.2.1. Australia

In Australia, for roughly a century, federal and state courts have set wages through judicial proceedings. Only labor and employer organizations may initiate proceedings; individuals have no standing. The courts hand down judicial decisions — awards — setting the "basic" or minimum wage, additional skill-based wages for specific occupations, conditions of work, occupational benefits, and "wage relativities" (i.e., the relationship or parity between wages in different occupations). After 1907 the federal court set a high basic wage, defined socially by reference to a decent standard of living for a family of four (originally presumed to be male-headed). Wage relativities were set by awarding additional wages — margins — for skills and enforced via a doctrine of comparative wage justice. The arbitration court determined comparative wage justice to mean that "employees doing the same work for different employers or in different industries should by and large receive the same amount of pay irrespective of the capacity of their employer or industry" (CAR 1970: 165; Plowman 1980: 85). The ruling created an almost automatic transmission of wage gains from one sector to another. Women received 75 percent of the male basic wage until the early 1970s. Beginning in the 1930s awards covered roughly 85–90 percent of workers. In 1974 the basic wage was equal to US$12,650 (in 1998 dollars), or about half of Australia's per capita GDP at the time.

As in the Netherlands and Denmark, awards generally bind workers and employers who did not go to court themselves but who do operate in the industry governed by the award. De facto, this compels capital and labor to organize in order to participate in wage setting; de jure, registration before the court creates a monopoly of representation. Consequently, "Australian unions are a part of the state, but in the sense of local governments with entrenched traditions of autonomy" (Scherer 1985: 92). In 1976, 322 unions covered 2.8 million Australian workers (versus 40 unions for 3.6 million Swedish workers), and over 50 percent of the labor force was unionized. Many awards provided for a closed shop, but there was not compulsory unionization across the board as in New Zealand. The union movement was divided between a few large industrial unions and many small crafts-based unions.

Public sector workers roughly 25 percent of the workforce in 1970, were handled in a similar way. State tribunals governed most public sector workers (because the states did most service delivery) and typically awarded wage increases across the board. Across the board public sector wage increases meant that wage relativities among occupational groups there increasingly diverged from wage relativities in the private sector (Scherer 1980). But after 1962, occupational groups in the public sector began getting group awards based on private sector awards generated in the federal system, and so the metals award became the implicit standard for comparison.

The apparent lack of concentration in collective bargaining conceals two important axes of centralization. First, the Australian Confederation of Trade Unions (ACTU) represents the entire union movement in basic wage cases. By the 1970s the ACTU covered virtually the entire unionized private sector workforce, or roughly 75 percent of unionized workers. Within the ACTU, unions representing over 100,000 workers were covering the metals industries, rural workers, the retail sector, clerks, and hospitality by 1971, and by the late 1970s the ACTU included most public sector unions. Second, the Australian Metal Workers Union (AMWU) and its employer counterpart, the Metal Trades Industry Association (MTIA), typically have a decisive hand in shaping the Metal Trades Award. The MTIA covers over 10,000 firms, but its eight largest enterprise groups account for nearly 30 percent of employment and value added. The metals award covers about half of manufacturing labor, most skilled labor, and about 10 percent of all Australian workers. Until 1967 higher pay from the metals award spilled over into manufacturing, construction, and eventually white-collar jobs via well-established unions (Frenkel 1987: 100). The AMWU and MTIA thus had a decisive hand in shaping the wage differentials and working conditions that the federal arbitration court subsequently imposed on the majority of manufacturing workers.

Employers, by contrast, were more divided, spanning about 700 organizations which aggregated themselves into three broad confederations representing manufacturing in sheltered industries, primary production

1 I use AMWU to label the Amalgamated Engineering Union and its successors after 1972; I use MTIA to designate the Metal Trades Employers Association and its successors.
and manufacturing for export, and multinational firms. In the early 1970s employers were split between the Associated Chambers of Manufacturing and the more primary product-oriented Australian Council of Employers Federations. These amalgamated as the Confederation of Australian Industry in 1978, but rancorous rifts continue to split this group (Plowman 1989). Meanwhile a separate, parallel, and powerful lobbying organization, the National Farmers Federation, represented 80 percent of farmers (Matthews 1991: 197), typically taking a harder line against unions than did the various manufacturers associations.

How did arbitration really work? Essentially, prior to the 1960s, Australian unions were so weak that most wage increases came only via basic wage claims organized by ACTU and brought before the arbitration courts. Industrial employers, aware that tariff protection would rise enough to compensate them for their increased wage bill, usually acquiesced. With full employment after 1967, bargaining on a second tier became more prevalent and a larger share of wage gains emerged from this more local bargaining. When the courts tried to enforce wage restraint in the late 1960s, unions struck and the court could not enforce any legal sanctions against them. Politicians ratified the courts' weakness by legislating away penalties. Employers counterattacked, revealing unions' fundamental weakness as unemployment rose after 1973. Unions thus spent the 1970s building the ACTU into a real federation with central powers, which helps explain why arbitration functioned as a de facto incomes policy in the 1970s and 1980s.

3.2.2.2. New Zealand

New Zealand's arbitration system pre-dates Australia's, but a socially defined living wage did not emerge until the 1920s. Collective bargaining occurs inside a set of state-run courts. Unlike Australia's courts, however, which were staffed by professional jurists, New Zealand's three-person arbitration panels were composed of a judge, an employer representative, and an employee representative. The two labor market actors were constantly tempted to cut out the middleman, forcing the state to intervene directly in pursuit of balance of payments and macroeconomic goals. The courts covered only about three-fifths of the labor market. This relative lack of coverage and institutionalization, together with the courts' lack of insulation from labor market actors, hurt their ability to discipline both capital and labor while remaining free of idiosyncratic political pressures.

The court set private sector wages and conditions across most industries and agriculture, fixing and adjusting the minimum wage with flat dollar or percentage increases under General Wage Orders, similar to Australian Basic Wage increases. No formal, Australian-style principle of comparative wage justice existed, but the court refused to change established wage patterns. Sectorally, employer associations and unions usually bargained over wages, and the court imposed binding arbitration only when talks failed, much as in Denmark. The court ratified collective bargaining through industry-specific awards, which bound firms and workers who were not members of either the employer associations or unions in the affected industry. In principle, employers and unions could sign limited contracts approximating 'enterprise bargains' (i.e. plant-specific contracts). Prior to the 1990s, the enterprise bargains affected about 25 percent of workers, in contrast to the 40 percent covered by industry awards, so that there was a significantly higher degree of decentralization than in Australia (Boston 1984: 70).

Compulsory union membership from the mid-1930s through 1990 put three-fifths of the labor force into largely craft-dominated, and thus fragmented, unions. In 1973 24 unions with more than 5,000 members represented only 60 percent of the unionized workforce (Deeks and Boxall 1989: 50). By the 1970s two broad but weak federations existed. The private sector Federation of Labour (FOL) covered about two-thirds of unionized workers, while the public sector Combined States Unions covered one-third. On the other side, the similarly fragmented Employers Federation covered 10,800 employers and 80 percent of the private sector workforce. Until the 1980s, the Employers Federation supported the existing collective bargaining system, although one current within the Federation wanted more Scandinavian-style centralization and a different current preferred more enterprise bargaining. Farmers presented a united bargaining and lobbying front through Federated Farmers, which had extensive ties to the National Party. As in Australia, retail, manufacturing, and farming employers were divided against each other.

The award system tended to compress wages and preserve wage differentials, despite some wage drift. Wage drift had no legal standing, but in the 1960s and 1970s roughly 25 percent of FOL workers enjoyed the benefits of drift above contractual wages (Boston 1984:68, 81–82). Generally wage increases tended to follow the gains made by the Engineers (i.e. metals) Union, the three electricians' unions and the General Drivers' Union. Technically, strikes and lockouts were illegal during the tenure of any given award. From 1946 onward, public sector wages were linked to private sector wages in principle, and statutorily after 1969. Though the state intended public sector wages to follow private sector wage movements, public sector employees were wage leaders in some bargaining rounds during the 1970s. As in Australia, the basic female wage was initially set at 40 percent of the male wage but later normalized. Female public sector

The state used arbitration in its attempt to control the balance of payments and inflation during the full employment era of the 1950s and 1960s, typically arguing for a low General Wage Order when either inflation or the current account deficit grew. The court’s awards in the 1960s held real wage growth below GDP growth (Boston 1984: 90). As in Australia, the court’s ability to enforce awards disappeared in the late 1960s, when wage pressures were greatest, labor markets tightened, and labor militancy high.

3.2.3. The Formal Welfare State

Australia and New Zealand also had formal welfare states—state-funded services and transfers—though these were clearly secondary to trade protection and arbitrated wages. Before the 1980s welfare supplemented work, buffering against life cycle events and accidents. Generally, these formal welfare programs provided flat-rate benefits funded from general revenue (see Table 3.4). Universality varied, but tax abatements were common. In 1960 Australian social spending was about 25 percent lower than in the other small OECD economies, although it grew faster. While New Zealand started out at about OECD average levels, real expenditure grew more slowly in the 1960s (OECD 1985: 28).

3.2.3.1. Australia

Australia’s welfare state is an adjunct to the system of full employment at a high minimum wage (Castles 1987, Castles 1989). Complex combinations of public and private funding characterized many sectors. In health care during the 1960s, for example, public funding provided roughly 90 percent of hospital costs, but private insurance favored by tax incentives funded most medical services. In 1974 the Whitlam Labor government passed a law creating Medibank, a public health insurance system financed out of an earmarked flat income tax. Old age pensions were flat, small, universal, tax-abated, and financed through general tax revenue. About half of all people had private, earnings-related pensions, but the bulk of these were males in large or public sector firms. Social assistance was essentially non-existent until Whitlam’s Australian Assistance Plan in 1973 and its accompanying single-parent benefit. Spending on these roughly doubled in the 1970s, in line with a tripling of unemployment and a two-thirds increase in the number of single-parent families. Primary education, however, was free and universal, with substantial federal and state support for private and parochial schools; tertiary education was essentially free after 1975. Labor tried to create a national compensation scheme and a national superannuation (second-tier pension) scheme in 1972–75 but failed because the Liberal–Country Party coalition controlled the upper house, and because of potential constitutional objections to having the national government absorb activities traditionally reserved to the states.

<table>
<thead>
<tr>
<th>Unemployment</th>
<th>Unemployment, 1960–73</th>
<th>2.0</th>
<th>0.2</th>
<th>2.2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment, 1971–73</td>
<td>19</td>
<td>38</td>
<td>40.5</td>
<td></td>
</tr>
<tr>
<td>Type</td>
<td>Flat, family related</td>
<td>Flat</td>
<td>Varies</td>
<td></td>
</tr>
<tr>
<td>Financing</td>
<td>Revenue</td>
<td>Revenue</td>
<td>Usually payroll</td>
<td></td>
</tr>
<tr>
<td>Participation</td>
<td>Male</td>
<td>92.4</td>
<td>n.a.</td>
<td>89.7</td>
</tr>
<tr>
<td>Participation</td>
<td>Female</td>
<td>45.6</td>
<td>n.a.</td>
<td>48.3</td>
</tr>
<tr>
<td>Health</td>
<td>Doctors</td>
<td>Private, fee for service</td>
<td>Private, fee for service</td>
<td>—</td>
</tr>
<tr>
<td>Population with private insurance coverage (%)</td>
<td>88</td>
<td>n.a.</td>
<td>n.a.</td>
<td></td>
</tr>
<tr>
<td>Public Funding (%)</td>
<td>56.7</td>
<td>80.3</td>
<td>73.8</td>
<td></td>
</tr>
<tr>
<td>Old age pension</td>
<td>Replacement rate (married)</td>
<td>25</td>
<td>60</td>
<td>n.a.</td>
</tr>
<tr>
<td>Old age pension</td>
<td>Means test/Eligibility age</td>
<td>Yes/65</td>
<td>Yes/65</td>
<td>Rare/65</td>
</tr>
<tr>
<td>Old age pension</td>
<td>Financing</td>
<td>Revenue</td>
<td>Revenue</td>
<td>n.a.</td>
</tr>
<tr>
<td>Old age pension</td>
<td>Secondary pension</td>
<td>Private</td>
<td>Public</td>
<td>Usually public</td>
</tr>
<tr>
<td>Old age pension</td>
<td>Coverage</td>
<td>ca. 50%</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
<tr>
<td>Social assistance</td>
<td>Replacement rate</td>
<td>&lt;25%</td>
<td>58%</td>
<td>n.a.</td>
</tr>
<tr>
<td>Social assistance</td>
<td>Means test?</td>
<td>Yes</td>
<td>Yes</td>
<td>n.a.</td>
</tr>
<tr>
<td>Social assistance</td>
<td>Outcomes (1980)</td>
<td>Post-tax/transfer Gini</td>
<td>0.29</td>
<td>n.a.</td>
</tr>
<tr>
<td>Social assistance</td>
<td>Single mothers, % in poverty</td>
<td>44.5</td>
<td>n.a.</td>
<td>17.1</td>
</tr>
</tbody>
</table>

n.a. = not available.

*Publicly mandated, tax sheltered.

3.2.3.2. New Zealand

During the 1930s the New Zealand Labour Party created a stable and generous formal welfare state that slowly decayed as inflation eroded benefits. Labour legislated universal, public, and free hospital care, free drugs, and medical payments to independent doctors. It replaced a means- and morality-tested old age pension with a universal flat rate (though income-tested) pension and added a second tier of voluntary earnings-related pensions. It subsidized mortgages for state housing. It made tertiary education free and provided a portion of students' living expenses. It passed a comprehensive social assistance package financed from general revenue. This basic architecture remained largely untouched until the 1970s, when two major changes occurred. First, in 1975, the National Party substituted a single generous flat-rate pension—universal but taxable, and financed from general revenue—for Labour's two pensions. Second, various forms of disability assistance (including workman's compensation) were homogenized into one Accident Compensation fund, financed by various user fees—wage levies and taxes on cars—and paying out tax-abated, contribution-based benefits at 80 percent of prior wages.

One final commonality between formal welfare in New Zealand and Australia that stems from arbitration wage awards which are normed against a four-person family is the use of universal child and family benefits to lift larger families out of poverty. The Australian system relied on a mix of tax expenditures and direct allowances. In the mid-1970s this combination was transformed into a direct cash benefit that was not indexed for inflation. In New Zealand a universal cash benefit was changed into a tax rebate in the 1970s.

3.3. Vulnerabilities

Australia's and New Zealand's arbitrated labor markets interacted with their export profile to create long-term vulnerabilities. Arbitration deliberately raised wage and input costs in sheltered sectors to squeeze economic rents out of the export sectors and fund an expansion of employment in the sheltered sectors. The arbitration courts awarded high wages in the manufacturing and service sectors. Manufacturing industry asked for and received high levels of tariff protection to stay competitive, despite low productivity. Employment grew because of Keynesian multiplier effects, as more workers got jobs at higher wages. Racist immigration laws kept the supply of labor low. The sheltered sector captured part of the rents generated by hugely competitive primary sectors because export firms passed on high domestic costs to foreign buyers. In effect, Australia and New Zealand ran the Scandinavian EFO-inflation model, which prescribed that sheltered sector wages should not rise faster than export sector wages, backwards. The sheltered manufacturing sector deliberately raised wage and input costs for the exposed primary sector to squeeze economic rents out of exposed sector production.

This growth model worked as long as the export sectors generated enough foreign currency to fund imports of manufactured goods not locally produced, pay interest on foreign currency-denominated debt, and reappropriate profits for direct investors. But over the long term, the export sectors could not earn enough dollars to fund a volume of consumption and capital good imports consistent with the socially defined standard of living. Both governments addressed the symptomatic aspects of this problem without curing the underlying causes. They used a variety of standard policy routines, pressing on one side of the balloon only to see new symptoms bulging out elsewhere. They tried boosting the volume of primary exports to offset falling prices, diversifying among primary exports, substituting domestic manufactures for imported manufactures, and (eventually) exporting more manufactures. By 1975 the failure of both traditional strategies forced each country into addressing underlying dynamics by using incomes policy to moderate the sheltered sector's wage gains and by moving away from informal welfare and towards formal welfare. Australia institutionalized this shift, but the failure of incomes policy in New Zealand led it decisively in a neo-liberal direction. The discussion below examines both countries together until they begin to diverge in the 1970s.

This 'Antipodean' growth model had two fundamental problems generated by its domestic dynamics and one fundamental problem generated overseas by agricultural protectionism. First, arbitration plus protection led to diverging productivity levels between the stagnant sheltered sector and the more dynamic export sectors. Second, arbitration reduced the primary sector's long-term viability to export profitability. Third, European over-production depressed global prices for food exports. This last threat was the easiest to understand, so politicians predictably responded to it first and only tried to reorganize the production model's internal dynamics after exhausting the easy responses. As changes in the international economy removed the export sector's ability to extract rents by the late 1970s, the old redistributive model could not long endure.

3.3.1. Falling Terms of Trade: Four Responses 1945–1970

Falling (and quite volatile) terms of trade, rising agricultural protection, and British entry into the European Union (EU) comprised the exogenous
threat to the Antipodean model. Falling terms of trade after 1953 slowly eroded the generation of rents in the primary sector. Falling terms of trade meant that a given unit of exports bought fewer and fewer units of imports, and that real incomes in both countries would inexorably fall relative to more robust manufacturing economies. In fact, per capita income in both countries did slide relative to other OECD countries during the post-World War II period.

Alternately, if local consumption of imported goods did not fall as terms of trade fell, then both countries would have chronic current account deficits and rising foreign (though not necessarily foreign currency-denominated) debt. From 1949 to 1974, Australia ran a current account surplus in only four years, of which three occurred during the Korean War and 1972/73 commodities shocks. Interest on foreign debt and multinationals' profit repatriation tended to overwhelm Australia's merchandise trade surpluses. New Zealand, similarly, saw a 30 percent secular decline in the terms of trade for its three largest exports, meat, dairy, and wool products (1965–1982). As in Australia, repatriated profits and interest payments offset merchandise surpluses and accounted for 75 percent of New Zealand's current account deficit in the 1970s (Gould 1982: 144; Blomdal 1986: 188–90; Reserve Bank 1986: 446; 1989: 155). In both countries, current account deficits and unemployment were the dominant macroeconomic concerns vying with each other for the attention of policymakers. Both countries accumulated modest new foreign debts through the early 1970s (see Figure 3.1 for trade and invisible deficits).

Finally, the volatility of export prices interacted with collective bargaining structures to create a tendency to overconsume imports. Australia's and New Zealand's exports from 1951 to 1971 had average annual price changes of roughly 7.5 percent, versus about 3 percent for Europe; including the chaotic 1971–74 period, boosts the average swing to 12 percent. Export volumes were similarly erratic, with the peak decline in New Zealand's exports at minus 10.0 and the peak gain at 13.8 (OECD 1976b: 6, 10). This volatility will be examined later.

There were four potential responses to falling terms of trade: increasing export volumes to offset price declines, shifting to new primary product exports, local production of manufactured goods to reduce import volumes and conserve foreign exchange, and exporting manufactured goods.

Both countries increased export volumes, and New Zealand subsidized dairy and meat exports in the 1970s. But agricultural protection and the EU's subsidized exports limited volume expansion. Britain's entry into the Common Market also reduced export volumes, although Australia weathered this better than New Zealand because it had already diversified towards minerals exports and Asian markets.

What about diversification? Wool, grain, dairy, and meat had accounted for about 68 percent of Australian exports in the late 1950s, and minerals only 7 percent. By 1970 the former accounted for only about 32 percent of exports while minerals and fuels jumped to 40 percent (OYBCA, various dates). In New Zealand, wool's share of exports fell, while non-traditional exports like pulp and paper, fish and fruits rose in volume, but nothing like Australia's wholesale shift towards minerals occurred. Diversification occurred within product groups, as skim milk powder replaced other dairy exports and beef replaced sheepmeats. The really big shift into forestry and fruits did not occur until the 1980s. Finally, both began exporting modest volumes of non-traditional manufactured goods, that is, something other than processed foods.

Import substitution thus was the dominant policy response. This was politically easy: it simply continued explicit pre-World War II policy, generated the most employment quickly, and (given arbitration) also generated high wage employment. But ISI had a significant internal limit, because the more successful ISI was, the greater the burden on the primary sector. The volatility of primary sector exports interacted with collective bargaining structures to create persistent tendencies towards balance of payments deficits.
3.3.2. ISI, Collective Bargaining, and Incomes Policy

SI interacted with collective bargaining structures to create an endogenous crisis dynamic. Because arbitration consistently pushed up sheltered sector wages, and because protection permitted ‘cost plus’ pricing in the sheltered sector, inflation was a persistent problem. Rising prices for sheltered goods lowered rates of return in the export sector, inhibiting investment and slowing volume growth. Perversely, the interaction of ISI and collective bargaining structures also meant that even favorable export price trends led to current account deficits. Arbitration’s normal operation quickly transferred export sector wage gains to the sheltered sector through established formulas on relative wages, eating up export price gains. Higher wages then turned into increased import consumption that could not be sustained over the long run. Because wages were sticky downwards, upward price shocks were thus more pernicious than the secular decline in terms of trade. Thus, while the 1970s price shocks temporarily boosted export prices, they also led to large current account deficits and rising inflation. Politicians tried to use arbitration as an incomes policy tool to keep wages and inflation at sustainable levels. Arbitration and its associated incomes policy thus stood at the intersection of the domestic and international markets: the more successful ISI was, the greater the need to use incomes policy to contain inflation in order to keep the export sector profitable. Put differently, successful ISI in Australia and New Zealand exposed the inherent limits in running the EFO model backwards.

New Zealand’s typical postwar economic cycle shows this well. In any given cycle, wool and/or dairy prices would revive temporarily. To prevent export receipts from being turned into unnaturally high levels of imports, the state would use its marketing boards or private stabilization schemes to try sequestering part of the additional export income. Sequestration worked well given the availability of effective capital controls. The Reserve (central) Bank captured roughly 40 percent of export revenue, and marketing boards much of the rest. But by the 1970s farmers discovered they could borrow against sequestered money and spend the money anyway, boosting imports. This forced the state into increasingly intrusive and futile controls over interest rates and credit allocation in the financial sector. Meanwhile the tight labor markets created by import substitution and booming exports led to growing militancy among meat workers. Rising wages in meat packing spread into the rest of the economy as the award system maintained parities across industries, also boosting imports. Meatpacking firms simultaneously passed their rising wage costs onto farmers as lower farm gate prices, inhibiting investment in agriculture and limiting further expansion in exports. The packers’ behavior also shifted rents from exporters to sheltered firms. When export prices fell, import demand did not, starting a balance of payments crisis and the ‘stop’ part of the ‘stop–go’ cycle.

The strikes of the late 1960s aggravated this cycle by decisively shifting income away from capital, especially in farming, and towards workers. A 14 percent fall in farmers’ share of the gross sales price in the 1960s depressed their investment. Despite subsidies amounting to 25 percent of net farm income, New Zealand’s livestock herd barely grew between 1968 and 1979 (Gould 1992: 137–38, 161). While agricultural exports became less and less able to fund New Zealand’s import bill, protected manufacturing could not generate enough exports to fund itself. The same dynamic occurred in Australia, although minerals exports eased the balance of payments problem. Australian rural debt-to-income ratios rose from dead even in 1960 to 2.4 to 1 by 1970 (OECD 1972: 33).

Efforts to change employment and social policy in Australia and New Zealand have to be understood in this context. When import substitution no longer generated new investment and growth at the end of the 1960s, inflation and current account deficits became prominent problems. The proximate causes for change were the essentially simultaneous collapse of wool prices and the arbitration rounds of 1967–69, wage explosions following the 1973 commodity shocks, and British entry to the EU. The shift to floating exchange rates as Bretton-Woods collapsed produced an exaggerated version of the usual routines. The Australian and New Zealand dollars both appreciated by roughly 30 percent from 1970 to 1974, making imports cheaper and increasing the socially necessary level of import consumption. When both dollars subsequently depreciated by the same amount from 1974 to 1977, the current account deficit increased substantially.

The parallel labor party (Whitlam in Australia and Rowling in New Zealand) governments of 1972–75 tried unsuccessfully to cope with these shocks by using incomes policy and more formal welfare to regulate class conflict and wage growth, and by decreasing trade protection. Australia’s better institutionalized arbitration system preserved real wages and kept inflation at roughly the OECD average level in the 1970s, while Australian unions suffered increasing unemployment and import penetration in the manufactured goods markets. New Zealand, by contrast, had inflation one-third higher than the OECD average, as the government used overseas borrowing to finance a soft-money, full-employment policy constellation, while its relatively poorly institutionalized arbitration system could not enforce wage restraint. These differences had substantive consequences in the 1980s. Australian unions proved willing to trade a higher social wage
and more employment for a gradual liberalization of the economy; New Zealand unions refused a social contract and got abrupt liberalization and a worsening social wage. Because the story diverges at this point, we consider each country separately.

3.4. New Zealand: Towards a New Model

3.4.1. Summary

The postwar model has been more thoroughly transformed in a market-oriented direction in New Zealand than in any other country considered in this volume, including Britain. The inability to run a well-institutionalized incomes policy led New Zealand governments in the late 1970s to combine a last, disastrous round of import substitution with a politiciized wage policy. In turn this probably made an Australian- or Dutch-style incomes policy impossible in the 1980s, although the incoming Labour government of David Lange (1984-89) initially seemed inclined toward such a solution. Lacking an incomes policy, the Labour Party successively liberalized all parts of the economy except for labor markets. This rapid change split the Labour Party, and an openly neo-liberal National government (Bolger) was elected in 1990. This government completed the transformation to a full market model by replacing arbitration with purely private contracts between individuals and firms, and by replacing socially defined wages with market wages. These rapid changes proved to be just as politically unacceptable as Labour's reforms, creating a wave of popular support behind a referendum that introduced a German-style mixed member proportional representation (MMP) electoral system for the 1996 election. Subsequent center-right coalition governments have been driven by conflict over the degree to which markets should continue to be inserted into welfare and other state operations. The next three sections focus on incomes policy and the last spasm of the old model under National in the 1970s, Labour's response 1984-90, and National's neo-liberal spasm 1990-96.

3.4.2. Incomes Policy Falls in the 1970s

The Rowling Labour Party government (1972-75) and Muldoon's National Party governments (1975-84) persisted with the essential elements of the old model of the 1960s: ISI efforts to increase export volumes, and control over finance to dampen import demand. All three governments ran a typical 'stop-go' cycle, responding first to inflation and current account deficits with a contractionary policy, shifting to an expansionary policy as unemployment rose, and then resorting to direct controls in order to maintain employment without also boosting inflation and the current account deficit. Both Labour and National governments borrowed overseas to sustain the old employment model, and in doing so they generated international financial obligations that the existing structure of production could not sustain. When this became apparent in 1984, the old model collapsed in the face of an unsustainable foreign debt burden, large fiscal and current account deficits, and a currency crisis. The commodity price boom of the early 1970s reinforced the tendency toward inflation and a current account deficit despite a rise in New Zealand's overall terms of trade from 80 in 1971 to 124 in 1973. By using currency controls and wage and price freezes, both the outgoing National government and the new Labour government tried to prevent boom level imports from becoming endogenized in consumer habits. A successful incomes policy might have eased these problems. But New Zealand's arbitration system became increasingly politicized, personalized, and deinstitutionalized after 1968.

Arbitration collapsed in 1967/68 when the state tried make use of its traditional role as the enforcer of macroeconomic stability. The 1967/68 devaluation of the British pound and the simultaneous collapse of wool prices in 1967/68 motivated the arbitration court to protect the current account balance by denying workers a general wage increase (Boston 1984: 91). But in the tight labor markets of the 1960s some FOL unions had begun bargaining directly with employers and then allowing the court to ratify these private agreements. Confronted with rank and file anger about the zero wage order, both the Employers Federation and FOL had their representatives jointly vote to overrule the state's representative in a second ballot. But stronger unions—metalworkers and electricians—went on strike anyway, striking for even higher wage gains. The number of workdays lost to strikes doubled in 1968 and then doubled again by 1970 (Deeks and Boxall 1989: 40). Without the arbitration system to maintain relative wages, unions engaged in wage leapfrogging, producing an 8.4 percent rise in real wages in 1972.

Politicians responding to the street compelled New Zealand's politically subservient central bank to ratify both these wage gains and the government's loose fiscal policy with an accommodating monetary policy (see Figures 3.2 and 3.3 for real interest rates and fiscal deficits). They also continued tariff protection and import licensing to ratify firms' ongoing practice of markup pricing. As in Britain, the state's lack of a credible threat to punish aggressive union wage demands with a restrictive monetary policy and the FOL's institutional inability to moderate its constituent unions'
Robert Muldoon's two follow-on National Party governments also failed at incomes policy, oscillating between outright wage freezes and free collective bargaining. The initial freezes combined with twelve-month contracts and flat wage increases to preserve the disturbed pattern of relative wages that had been driving the dynamic of continuous leapfrogging in wage demands by different unions. Muldoon intervened repeatedly to secure the outcomes he preferred, which further weakened the institutions of arbitration. Knowing full well that the government would eventually reverse moderate arbitration outcomes, export sector unions took to striking in the middle of wage freezes. This naturally provoked even more strikes in search of exceptional settlements. While free collective bargaining rounds went on, Muldoon also intervened to influence the trendsetting metalworkers' contracts. Finally, Muldoon shifted the locus of wage determination from the arbitration court to the Remuneration Authority, which corresponded to a shift in procedure from formal legal precedent to simply amended regulations. All this soured the FOL on any notion of a formal incomes policy run by politicians.

Figure 3.2 Real long-term interest rates, net of US interest rate, 1970–1995
Source: OECD, Economic Outlook (Paris: OECD, various dates).

Figure 3.3 Fiscal deficits, 1970–1997

wage demands led to high inflation and downward pressure on employment (Scharpf 1991).

At this point the state began searching for a new institutional framework to control wage growth and implement a formal incomes policy. From 1970 to 1975 both National and Labour attempted to freeze wages and reconstitute the arbitration system as the only bargaining arena. Both governments legislated flat wage increases and prohibited reopening contracts to prevent wage 'leapfrogging'. Both efforts failed in the face of rising worker militancy and employer accommodation to the reality of essentially zero unemployment through 1977. Unlike in Australia and Britain, where strikes subsided after 1974, in New Zealand strike activity rose 70 percent between 1975 and 1977.

The 1972–75 Labour government also used the temporary surge in export receipts to repay New Zealand's foreign debt (a variation on the sequestration theme), and it induced farmers to voluntarily sequester NZ$83 m in 1973. It sharply increased welfare payments by restoring the real value of a variety of means-tested benefits that had been eroded by inflation. It introduced a contribution-linked national pension. Both of these efforts at formal welfare made a European-style pact over the social wage more likely if and when unions became a reliable bargaining partner.
Muldoon also resorted to price controls, interest rate controls, and direct credit allocation. These policies created as many macroeconomic problems as they solved (see Figure 3.3 for fiscal deficit, Figure 3.4 for unemployment, and Figure 3.5 for inflation rates). This, in turn, led Muldoon to try solving all his government’s self-induced macroeconomic problems through an exaggerated version of the old ISI policy. After 1978 he borrowed NZ$5 bn to expand steel production, increase refinery capacity, and create a synthetic fuel plant in the ‘Think Big’ program. Think Big closely resembled the British Labour Party’s ‘Alternative Economic Strategy’ of the 1980s. Partial monetization of Think Big’s interest costs and subsidies for agriculture and manufactured exports drove inflation up to 16 percent by 1982, and the current account deficit to nearly 6 percent by 1984 (EMG 1984: 5-8). Muldoon essentially financed unemployment at below-average OECD levels with more foreign public debt, which rose from 5.3 percent in 1974 to 24.2 percent of GDP in 1984; total overseas debt was 45.8 percent of GDP (Reserve Bank 1986: 555).

This proved economically and politically unsustainable. Muldoon’s electoral base had steadily shifted away from business and towards lower income New Zealanders. This change in Muldoon’s constituency, combined with his steadily increasing interventionism, provoked a rising tide of pro-market opposition within the National Party that eventually spilled over into the formation of a new minor party, the neo-liberal New Zealand Party. In the 1984 election, this party attracted 12.5 percent of the electorate, giving Labour a plurality. Speculators, anticipating that Labour would win and devalue the dollar, had meanwhile exhausted the Reserve Bank’s foreign exchange reserves, forcing the incoming Labour government under David Lange to devalue the New Zealand dollar 20 percent.

### 3.4.3. New Zealand: Toward a Pure Market Model, Step One—Labour 1984–1990

While Labour used the currency crisis to drive through significant change with the usual ‘there is no alternative’ rhetoric, the Lange government initially oscillated between two paths for change: either a corporatist bargain, like Australia’s 1983 Accord, or the systematic introduction of markets into sheltered sectors. Labour had run on an anodyne platform that concealed conflicts between interventionist and market-oriented wings. A loose coalition of unions and politicians seeking to imitate the Australian Accord opposed another coalition of politicians (including the finance ministers), the Treasury, some unions, and internationally exposed businesses seeking to reverse Muldoon’s excessive interventionism and introduce markets as widely as possible. The latter group won, partly because the currency crisis allowed it to liberalize financial markets immediately. It is important to note, however, that many actors in the liberalizing

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**Figure 3.4 Unemployment rates, OECD definition, 1970–1996**

*Note:* The 12 smaller OECD economies as opposed to the 6 or 7 big ones (G7): Austria, Australia, Belgium, Denmark, Finland, Ireland, Netherlands, New Zealand, Norway, Spain, Sweden, and Switzerland.  

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**Figure 3.5 Consumer price inflation, 1970–1998**

*Source:* OECD, Economic Outlook (Paris: OECD, various dates).
coalition sought to save the welfare state from itself, that formal welfare spending rose throughout both Labour terms in office, and thus thatLabour was not openly imposing costs on its major constituencies until late in the 1980s.

The market faction’s triumph pushed Labour to change the old model’s core elements by introducing market principles into a wide range of formal and informal welfare state activities. Labour removed trade protection for manufacturing and commercial services, removed subsidies from agriculture and manufacturing, and privatized the bulk of state-owned enterprises (SOEs). This forced businesses newly exposed to competition state agencies operating on business-like principles to shed excess labor. Because the old informal welfare state operated through systematic overmanning of all enterprises in order to assure low unemployment, Labour in this sense dismantled an important part of the welfare state. It did not, however, fully attack the wage regulation side of the old informal welfare state. Labour pursued a mix of policies intended to create a slightly more flexible labor market. This was not done at the expense of unions’ bargaining power relative to employers or, even more significantly, at the expense of the notion that wages were to be set socially rather than by markets. Public sector collective bargaining was reformulated along private sector lines. Finally Labour expanded and consolidated social assistance programs. We will primarily deal with these policy changes below. Marketization was at its most limited in the formal welfare state (health, education, and various pensions) and greatest in areas that were commercial operations by nature, like agencies producing easily marketed goods and services.

Labour also pursued four subsidiary policies designed to enforce market pressures. It liberalized the financial sector, institutionalized the world’s most independent central bank, broadened and flattened taxes, and tried to privatize the public debt by the simultaneous privatizing SOEs. Labour privatized a greater proportion of the public sector than Thatcher, selling everything from the state’s computer services to NZ Telecom. Figure 3.6 shows the falling share of public sector employment relative to the entire population.

3.4.3.1. Financial and Trade Liberalization
Labour concentrated on financial and trade liberalization and desubsidization in its first term, 1984-87. These reforms profoundly transformed New Zealand’s welfare state by making disguised unemployment transparent and imposing market allocation of capital. Henceforth, instead of having the state create employment (indirectly, via protection, or directly, via SOEs and targeted capital allocation), jobs had to be self-sustaining in open markets. Total substantive deregulation of financial markets removed capital allocation, interest rate controls, and barriers to foreign entry and domestic exit. Financial liberalization permitted aggressive local investors to use foreign capital in order to take over businesses, amalgamate them into large conglomerates, and shutter inefficient operations. Effective rates of assistance (the share of value added provided by subsidies and protection) for manufacturing fell from an average of 38 percent in 1984 to 19 percent in 1990 (OECD 1991: 63). Failing protection and high real interest rates cleared out inefficient, labor-intensive manufacturing enterprises and roughly 25 percent of manufacturing employment. Investment in manufacturing fell in real terms through 1989 (Reserve Bank 1988: J1, J2, 1989: 112-17). While productivity per employee increased, manufacturing employment has not. Manufacturing output returned to trend levels during the 1990s, but at a lower level of employment. Some new, ‘non-traditional’ manufactured and services exports have emerged, particularly where manufacturing has strong linkages to the major commodity exports.


![Figure 3.6: Public sector employment to population, 1970-1997](source: OECD, Statistical Compendium: Economic Outlook (Paris: OECD, 1998); own calculations.)
the New Zealand dollar led to plummeting real income and land values. Farmers responded by reducing investment to half its historic levels in traditional export commodities, while diversifying aggressively into new commodities like fruits, deer, and eco-tourism. These expanded from 4.8 percent to 6.9 percent of New Zealand's exports under Labour, somewhat ameliorating declining terms of trade for traditional exports.

Labour also removed government monopolies over the production of many goods and services. In 1984 state-owned enterprises (SOEs) accounted for over 20 percent of investment in New Zealand and employed 5 percent of the labor force, but they generated only 12 percent of GDP and consistently lost money (Gregory 1987). The State Owned Enterprise Act (1986) split trading activities off from regulatory and line agencies and created nine major commercial firms. These new firms were self-standing corporations with business-like management, obliged to charge full market prices for their services and to pay taxes like any other firm. They could borrow freely in capital markets, but only at market rates, without government debt guarantees or subsidies. Management had to promulgate explicit performance targets using private sector notions of profit. They could only underprice services if parliament provided them with an explicit subsidy and policy mandate (Jennings and Cameron 1987). Market-based reforms reversed the situation for public enterprises SOEs shed 18,000 workers, despite rising output, between 1984 and 1988. Market pricing of basic public services meant that SOEs' dividends, taxes, and interest payments to the state rose, providing nearly 6 percent of revenues in fiscal year 1987/88 and 8.7 percent a year later (Reserve Bank 1989: 124–26, Cavigill 1989: 28–33). By 1993 all of the SOEs had been sold off, yielding receipts equal to 3.55 percent of New Zealand's average 1988–92 GDP, proportionately three times as much as Britain's privatization receipts (Economist 1993: 112).

3.4.3.2. Labor Markets
Labour's financial and trade policies had direct labor market consequences, driving official unemployment up 40 percent by 1990, to 7.7 percent (OECD basis). Participation dropped 2.6 percent, long-term (over six months) unemployment rose from 15 percent in 1986 to 45 percent in 1990, and part-time work increased from 14.9 percent to 20.0 percent of the labor force. Figures 3.7 and 3.8 show falling total labor market participation and a falling ratio of business sector employment to total population; for the former, the divergence between trends in New Zealand and in the smaller OECD countries is notable. Rising unemployment structured the politics surrounding Labour's cautious introduction of market forces into the system of socially defined wages during its second term, 1987–90.
Labour's wage bargaining reforms aimed at breaking up the rigid wage relativities that had bedevilled incomes policy all through the 1970s. As in Australia, Labour used carrots (promises of an increased social wage) and sticks (tight fiscal and monetary policy) to get wage discipline from unions (Easton 1987, Sandlant 1989). But with unions divided between two federations, and with the finance-dominated Business Round Table as the employers' loudest voice, the outcome was octo- or deca-partisum, not a tripartite dialogue among business, labor and government. Moreover, unions' experiences from the 1970s inclined them against cooperation. The FOL pushed the Labour Party to end compulsory arbitration in 1976. But by 1987 rising unemployment and unease about Labour's proposed wage bargaining changes motivated the FOL and CSU to merge into the Council of Trade Unions (CTU, covering 78% of unionized workers).

Labour reformed SOE wage bargaining first. The 1986 SOE Act contained wage bargaining changes that dovetailed with commercialization. Commercializing SOEs was pointless if wage bargaining practices blocked the reorganization of work, productivity-based remuneration, and redundancies. Before the Act, the State Services Commission set wages and conditions according to centrally determined job categories, without regard to a firm's individual needs, and enforced complex procedures for civil service tenure, appeals, and grievances. The 1986 Act harmonized SOE wage bargaining with existing private sector practices.

Labour then moved on to change private sector bargaining itself with the 1987 Labour Relations Act, which tried to increase unions' relative power while simultaneously decentralizing bargaining to the 'enterprise' (firm) level. Enterprise bargaining would break the automatic transmission of wage gains between the sheltered and exposed sectors, allow more variation in both wage levels and wage parities, and perhaps induce higher productivity. The Act simultaneously bolstered unions. Only union locals could initiate and sign contracts outside the arbitration system, and compulsory union membership continued. The Act also would have forced the roughly 60 percent of New Zealand's unions representing fewer than 1,000 workers (8.6% of all workers) to amalgamate with larger unions, without regard to traditional occupational boundaries. This would enable labor organizations to form a united front against individual or similar employers. Finally, unions' right to monopolize worker representation was made contestable by a ballot of affected workers. The Engineers (i.e. metals) Union almost immediately employed the new regime to opt out of the national award and negotiate industry-specific awards with employers. Still, deviations from the first metals settlement were very small (the standard deviation of wage increases in 1988 was 2.9%), and greater wage dispersion awaited the National government's shift from enterprise to individual bargaining in 1991.

In two acts passed in 1988 and 1989 Labour finished the job of homogenizing public sector bargaining with private sector practices (Walsh 1991). The 1988 State Sector Act and the 1989 Public Finance Act created private sector-style wage and work disciplines in the traditional welfare state and in those 'non-commercial' agencies still overseen by the State Services Commission. Agency management gained the right to hire and fire at will, to reclassify and redeploy labor, and to set employee remuneration on an enterprise basis. Managers could cut separate deals with their workers on staffing levels, hours worked, productivity bonuses, etc., so long as they were in conformity with basic labor legislation. The State Services Commission became management's agent in agency-level collective bargaining. Managers thus could behave like private sector managers in their search for greater efficiency and productivity. This helped produce more customer-friendly service delivery in many instances.

Labour's industrial relations reforms addressed some of the dynamics underlying New Zealand's vulnerabilities. They exposed more people to market pressures and weakened socially determined wages. Was there a compensatory expansion of the formal welfare state based on tax-funded transfers and services?

### 3.4.3.3. Formal Welfare

Higher unemployment made the formal welfare state more important, and overall real social spending rose. Labour implemented the Guaranteed Minimum Family Income in 1986, a kind of negative income tax guaranteeing working families roughly 80 percent of the average post-tax wage. However, high effective marginal tax rates and rising unemployment limited the guaranteed income's impact on participation rates. From 1985/86 to 1988/89 health and education spending expanded 9.6 percent and 24 percent, respectively. Transfer spending also rose slightly as unemployment rose (OECD 1991: 39). In contrast to this partial expansion of the welfare state, Labour was also effectively slowing the growth of old age pension spending by (1) changing the basis for indexation from the CPI (consumer price index) to the average wage, a more slowly growing indicator, and (2) by increasing the eligibility age from 60 to 65. (See Figure 3.9 which shows the evolution of social spending.)

Labour increased social spending so it could buy acquiescence to institutional changes in the formal welfare state paralleling those changes taking place in the former SOE sector. Inquiries into health care and tertiary education promoted a more market-based governance structure. In tertiary education Labour imposed charges equaling 10 percent of tuition...
Politically, though, core Labour voters rejected all this. During its first term, 1984 to 1987, Labour had bought acquiescence to economic liberalization with a series of payoffs to its core constituencies: the ‘no nuclear ship visit’ policy for the peace movement, an environmental ministry for the greens, decriminalization of homosexuality for the gay movement, a women’s ministry for feminists, reinstatement of the closed shop for private sector unions, ratification of Treaty rights for the indigenous Maori population, and expanded social service spending for public sector unions. But in Labour’s second term, 1987 to 1990, reforms and events like privatization, the widespread introduction of user fees, and the stock market collapse alienated both traditional Labour voters and yuppies. In 1989 supporters of the old welfare/growth model split off from Labour and formed the NewLabour[sic] Party, helping the National Party to win a 38-seat majority in a 97-seat house in the 1990 election.

3.4.4. National from 1990 Onward: Build It and They Will Come

The National government finished dismantling the informal welfare state by attacking unions directly and individualizing wage bargaining. It finished privatizing and desubsidizing the economy. In the formal welfare state it fully monetized education and cut social assistance, but it failed to introduce real markets into health care and to privatize old age pensions. National basically bet that the natural operation of markets would ensure New Zealand’s future prosperity and that no positive policy, aside from the introduction of markets, was needed to generate growth. But National hedged its bet by actively soliciting direct foreign investment, which jumped from about 5 percent of gross domestic capital formation in the 1980s to 25 percent by 1992. Exports increased 48 percent in volume between 1989 and 1996. This seemed to validate National’s “build it (the free market) and they (the investors) will come” policy stance. However, renewed economic expansion merely brought New Zealand back to its long-term trend rate of growth. By 1998 the chronic current account deficit re-emerged for the old reason—repatriation of investment income, which increased from 5.3 percent of GDP in 1988 to 9.1 percent in 1995. At that point this outflow was roughly twice the size of the current account deficit (OECD 1998: 178, 182, 184).

3.4.4.1. Informal Welfare and Collective Bargaining

National fundamentally changed the old informal welfare state mode with its Employment Contracts Act (ECA) 1991 (Damin 1997). National argued that market-based, flexible wages would lead to higher productivity and growth. Under the ECA employers could contract freely with...

Figure 3.9 Social expenditures as a percentage of GDP, 1980–1997
individuals, while unions could only represent individuals who explicitly delegated bargaining rights to the union. The ECA destroyed socially determined wages by limiting the arbitration court's jurisdiction to the interpretation of employment contracts, eliminating unions in sectors where workers were least able to organize themselves (e.g. hospitality and clerical work), eliminating automatic transmission of wage increases through general wage orders and clauses on relative wages, and allowing employers to avoid collective bargaining entirely.

After 1991 unions representing workers with weak labor market positions—like those in agriculture, construction, retail, wholesale, accommodation, and restaurants—simply collapsed. Union density fell from 50 percent to 20 percent by 1996, and the number of workers covered by union contracts fell 42 percent. Multi-employer contracts fell from 77 percent to 20 percent of all contracts, and individual contracts and wage scales became common even in the public sector. The collapse of weak unions lifted the 'market share' of the ten biggest unions from 45 percent to 77 percent of unionized workers. The labor movement split, as a minority of militant unions left the NZCTU to form the Trade Union Federation (TUF).

Deuninonization drove unskilled workers' wages down and wage dispersion up every year after 1991. Productivity did not increase markedly, though profits did. The wage share of GDP is now back to its old levels from the 1960s, while rates of return have roughly doubled from where they were in the 1980s (see Figure 3.10). Unemployment fell from its recessionary high of 10.3 percent in 1990–91 to 6.7 percent by 1997, and labor market participation recovered to 1980s levels (Figures 3.4, 3.7, and 3.8) (Harbridge and Crawford 1997). 22.7 percent of employment was part-time work (OECD 1998: 187). So the ECA restored employment to its status quo ante level, but without unions.

Finally, National finished the job of exposing all sectors to international competition, cutting tariffs another third to 12 percent between 1993 and 1996. By 1998 falling tariffs forced all automobile assemblers to exit and most of New Zealand's clothing manufacturers to shift overseas to low-wage countries.

### 3.4.4.2. Formal Welfare

National's primary goal of eliminating the fiscal deficit and shrinking the state colored its policy towards the formal welfare state until the introduction of proportional representation in the 1996 election. After that, National's need to forge a coalition with the more centrist New Zealand First Party halted spending cuts. The threat of a credit rating downgrade linked to New Zealand's large foreign debt strongly influenced the general decision to cut nominal public spending by 7 percent, largely by cutting social assistance about 10 percent (Dalziel 1992; Rudd 1992). This sharp drop shows up in Figure 3.9. Total expenditure fell slightly in absolute terms over the course of the three National-led governments in the 1990s; in relative terms public spending thus dropped from 40.3 percent of GDP to 33.7 percent by 1997, in what amounted to yet another restoration (like the employment picture) of the pre-Labour status quo. Absolute revenues were also flat, falling to 33.7 percent of GDP. Fiscal surpluses after 1994 allowed the government to reduce gross public debt from 56.1 percent of GDP in 1994 to 37.5 percent in 1997, and to bring foreign-held public debt down from 42 percent of GDP in 1990 to 22 percent in 1997 (OECD 1998: 188).

National tried to recuce public involvement in the formal welfare state by getting more private money and private actors into newly created 'markets' for welfare services. In health care the public share of spending declined from 82 percent in 1991 to 76 percent by 1993. By 1993 about 40 percent of New Zealanders had some private health insurance (Kelsey 1995: 216). National's deepest cuts came in social assistance, where benefits were reduced on average by 10 percent and eligibility requirements were considerably tightened. The average reduction conceals a much sharper cut in social assistance for able-bodied males and childless
females, designed to push both back into the labor market. National increased the effective tax rate on the old age pension and suspended indexation for two years. These cuts drove old age pension expenditure down from 7.84 percent of GDP in 1991 to 5.69 percent in 1996. Benefits fell from 72 percent of mean household income to 58 percent (Cheyne, O'Brien, and Belgrave 1997: 185).

Cutting spending does not make markets, though. National followed the recommendation of a Labour White Paper and broke the health system into four Regional Health Authorities that contracted out for services from primary care physicians and 25 Crown Health Enterprises (i.e. hospitals). These CHEs competed with private providers for ‘consumers’ and paid dividends and interest on the capital they borrowed from the state. However, the 1996 center-right coalition government reversed much of this, explicitly designating public service, not profitability, as managers’ core goal.

National inserted markets more successfully into public housing, dividing the state housing agency into a mortgage provider and a property management firm, raising rents to market levels, and partly compensating the poor with a housing benefit. In education National funded schools with a capitation-based block grant for both primary and tertiary education. Parent-dominated school boards and university administrations now compete for students, pay teachers individually calibrated wages, and offer services tailored to their ‘market niche’. The state pays 75 percent of tuition costs for tertiary education (95% for those on social assistance), and universities charge students directly for the rest. Students are expected to borrow or earn that money.

National also introduced legislation that made it difficult to reverse their reforms. The Fiscal Responsibility Act 1994 mandated prompt publication of fiscal data based on generally accepted accounting practices, benchmarking so that the public can assess this data, and publication of budget statements well in advance of the actual budget in order to stimulate public debate over budget goals. The law forced diversion of operating surpluses into debt reduction and some balancing of the budget over the economic cycle.

3.5. Australia: Towards a New Model

3.5.1. Summary

Australia presents three contrasts with New Zealand: change in the model was negotiated rather than administered as shock therapy; change has been more gradual, and by most indicators economic performance has been better. The ease of the transition in Australia partly reflects the lingering benefits of a relatively ‘hard money’ policy stance in the 1970s as compared with New Zealand. It also reflects earlier conscious efforts to change the model by the Whitlam Labor government (1972–75) and the Fraser Liberal-National coalition (1975–83). Both of these governments changed the ancillary elements of the old model. Change in the model’s core—arbitrated wages—did not occur until the Hawke (1983–91) and Keating (1992–96) ALP governments successfully negotiated an incomes policy, the Accord. The Accord gave the ALP time to introduce markets into the service sector gradually, while liberalizing product markets to a greater extent than in New Zealand. The Hawke-Keating governments used the Accords to decentralize collective bargaining while still preserving minimum wages, to remove trade protection and encourage more manufactured exports, and to generate robust part-time employment as lower barriers to trade destroyed unsustainable full-time jobs. The ALP secured fairly broad public support for this policy shift, winning five straight elections through 1996.

The more classically neo-liberal Liberal-National coalition since 1996 and like-minded state-level governments continued privatizing and ‘marketizing’ the service sector. Despite the clamor for deregulation and the attainment of wage relativities, substantial elements of the old social wage remain. The Howard Liberal-National coalition government since 1996 has continued decentralizing collective bargaining, but it failed to create something akin to New Zealand’s Employment Contracts Act. The arbitration court still sets the basic wage. A severe reduction in the Liberal-National coalition’s parliamentary majority in the 1998 federal election and the coalition’s defeat in the 1999 election in the state of Victoria suggest political limits to further marketization. As in New Zealand’s 1999 election, rural voters who have lost from the desubsidization of public services shifted their votes to Labor in Victoria.

3.5.2. Incomes Policy and Monetarism in the 1970s

As in New Zealand, the 1970s commodities shocks gave Australia sharply rising terms of trade that set off a wage explosion deleterious to the IS model. The metals union (AMWU) and its employer counterpart, the Metal Trades Industry Association (MTIA), tried to get the arbitration court to limit wage increases to the CPI plus productivity gains. Both feared unsustainable wage gains that would raise unemployment. As in New Zealand, tight labor markets meant that rank and file workers demanded and employers conceded large second-tier wage increases.
These concessions ignited battles over wage parities, and strike levels doubled to nearly 600 lost days per 1,000 workers, three times New Zealand’s rate and slightly higher than Britain’s. Rising wages and Whitlam’s tax increases shifted the wage share of GDP from 60 percent in 1974 to 66.7 percent in 1976, while the profit share collapsed from about 17 percent to 14 percent by 1976 (see Figure 3.10) (OECD 1976a: 24). Firms shed labor, pushing unemployment up to 4.5 percent by 1975 and 6.1 percent by 1978. Deteriorating terms of trade shifted the current account from surplus to a deficit of 3.3 percent of GDP by 1974. In short, wage dynamics in 1970–75 displayed all the model’s pathologies.

The Whitlam ALP government and the Fraser Liberal-National coalitions both attacked different sides of the central dynamic while protecting their core constituencies. Whitlam lowered tariffs by 25 percent. He also built a formal welfare state with new public health and social assistance programs. Still, Whitlam maintained informal welfare by supporting the arbitration court’s introduction of centralized wage indexation. Fraser (like his British contemporary British Dennis Healey) introduced a mild monetarism, targeting public sector wages and staffing in order to reduce inflation. Fraser undid Whitlam’s tariff cuts, though. Like Muldoon, Fraser triggered one last spasm of the old model after 1979, abandoning his monetarism by increasing spending during a shortlived minerals export boom from 1979 to 1981.

Whitlam’s and Fraser’s efforts created the conditions essential to making the Hawke government’s formal incomes policy work in the 1980s. Whitlam’s ALP government tried to weaken workers from the informal welfare state by creating a formal welfare state and to weaken industry from protection and recrion it to export markets. Shifting from primary products to manufactured exports would ameliorate the problems caused by rigid wage relativities. Welfare spending came up to the OECD averages by 1975. The introduction of national health insurance (Medibank) drove public health spending from below to above the OECD average, and the public share of health spending increased 10 percentage points to 74 percent. Medibank reduced private insurance coverage from 80 percent to 60 percent of the population and private funding from roughly half to about one-quarter of spending (Scotton 1977: 7; Deeble 1978: 21). Whitlam substantially increased social assistance and old age pensions, doubling real spending in three years (see Figure 3.9). Public sector employment grew twice as fast as the OECD average between 1970 and 1975.

Whitlam cut tariffs across the board by 25 percent as a way of reminding the metals sector that insulation from world markets was a political choice; the assumption was that lower trade barriers would moderate wage militancy. Metalworkers learned this lesson right away, though other unions did not until the late 1970s. Whitlam’s expansion of the formal welfare state increased public sector employment and thus the relative strength of public sector unions. Tight labor markets and even tighter wage parities generated inflation, which rose to 15.1 percent by 1974.

To control inflation (Figure 3.5), Whitlam proposed an explicit social contract with the ACTU in 1974. If the ACTU accepted flat dollar wage increases above a certain income level, the ALP would preserve real wages via tax indexation or an increased social wage. As then ACTU president Bob Hawke noted, this would gradually reduce the wage share of GDP if productivity grew. This early anticipation of the Accord failed because none of the partners could perform as expected. The ACTU did not include white-collar unions, and many of its blue-collar unions were still quite militant. The ALP lacked the Senate majority needed to deliver tax indexation and social wage increases. Business was still fragmented. Nonetheless, these tentative talks between the unions and the government revealed the ACTU’s willingness to commit itself to centrally driven wage restraint (Plowman 1981: 20-24).

Fraser’s conservative coalition governments, from 1975 to 1983, helped resolve these organizational problems, albeit inadvertently. Fraser anticipated classic 1980s monetarism by exercising greater fiscal restraint in the 1970s than happened in New Zealand, though not relative to OECD averages (Figure 3.3). Public sector employment grew in the states but not with the federal government (see Figure 3.6). Fraser cut public investment to keep spending growth below GDP growth. From a peak of 5 percent of GDP in calendar year 1975 the fiscal deficit fell to 0.3 percent in 1982, and the federal government’s share of GDP fell from 30.7 percent in 1976 to 28.1 percent in 1981. Meanwhile inflation fell from 15.1 percent to 11.1 percent (Blondal 1986: 93-95). Fraser also shifted income to better off groups with tax changes, he de-indexed transfers, and he reduced Medibank funding. Fraser’s policy efforts limited but did not change the old model. First, the protected service sector continued to expand, especially the states’ public enterprises and community services. These firms’ losses increased the total public sector deficit to an average level of 5.3 percent of GDP and with no consistent trend across the 1970s (Treasury 1997: 7-16). Employment by state and local government community services increased 25 percent to total one million by mid-1979.

Second, Fraser was not able to weaken arbitration or the existing system of wage parities. White-collar workers unions proved difficult to control, and it was they who drove wage outcomes in the 1970s. White-collar workers had become half the workforce by 1970, and their unions constantly struck to preserve wage parities with blue-collar workers (Plowman 1981: 14, 21-23).
Finally, Fraser yielded to the temptation to use traditional solutions, acquiescing in an exaggerated version of the standard policy response between 1979 and 1983. Rising commodity prices sparked a rough doubling of foreign direct investment into Australia, including a 35 percent increase in investment for minerals production in 1979. Tighter labor markets convinced both the government and the unions that prosperity was imminent, and strong unions in both sectors pressed for wage gains. Fraser made a pre-election wage concession well above the arbitration court's guidelines for public sector unions in 1980. This relaunched the battles over wage relativities and drove strike activity back up to 1974 levels. Unfortunately, recession hit in 1981, and by 1983 unemployment had nearly doubled to 10 percent. The ACTU and its manufacturing unions realized that declining manufacturing employment was a secular trend and signaled their preference for having the arbitration court restrain wages rather than for having to endure a government-imposed wage freeze (Singleton 1990: 61–64).

Why did the ACTU prefer arbitration? During the 1970s the arbitration court preserved real wages and contained inter-union rivalries. This experience convinced unions to exchange wage restraint for a managed expansion of the formal welfare state and employment in the 1980s. They hoped that wage restraint would allow them to reverse the job losses of the 1970s. Income policy worked in Australia but not in New Zealand (or Britain) for three reasons. First, Australia’s professionally staffed arbitration court was committed to judicial autonomy, unlike New Zealand’s tripartite court (Bray and Nielsen 1996). Arbitration jurists strove to preserve their role suppressing industrial conflict and defining wages, rather than simply steering a course between labor and business demands. This strong definition of the arbitrator’s role created a shadow of hierarchy for enforcing negotiated incomes policy. Second, the increased centralization and unionization of both social partners in the 1970s meant they could actually bargain. The ACTU incorporated public sector and white-collar workers, and the ACTU’s largest unions represented a greater share of ACTU workers. On the business side, manufacturing firms created a coherent organization. Finally, unemployment and tariff cuts motivated both manufacturing unions and firms, as well as public sector unions, to seek negotiated change. Rising import penetration made firms seek productivity increases from unions. Public sector unions preferred negotiated change to Fraser’s open attacks on the public sector. With institutions, actors, and motives at present, the election of the Hawke ALP government provided an opportunity to try an incomes policy.

Substantively, during the 1970s and 1980s the arbitration court centralized wage regulation and disciplined unions in their own interests. The court had consistently tried to reassert its control over wage determination after the breakdown of 1968, and rising unemployment in the 1970s motivated the ACTU to work with the court. The court’s reintroduction of quarterly wage indexation facilitated a gradual reduction in the wage share of GDP. The ACTU itself sought this in order to protect employment and wages simultaneously: while real wages stayed flat, productivity gains would bolster profitability and investment. Over the 1970s indexation compensated for roughly 80 percent of the rise in the CPI. This gave the ACTU a more uniform outcome than it could have gotten from free collective bargaining, because battles over relative wages would have created “wage chasing” and higher unemployment (Carr 1979: 96; OECD 1980: 47). The court also created a legal loophole permitting a sustainable widening of wage parities: if individual unions could show that changes in “work value” (productivity) had occurred, they could get wage increases above and beyond what indexation warranted. The court’s maintenance of real wages also forced employers to cooperate with unions in seeking productivity growth. Productivity growth rates in Australian white goods, for example, were twice as high as in the USA during the 1970s. Improved productivity reduced employment by 30 percent but gave another 30 percent of the labor force “job security”-based wage increases (BIE 1983). The arbitration court helped preserve the ACTU unions’ internal unity because it moderated wage compression and allowed unions to externalize the blame for wage moderation. In contrast, the Danish and Swedish LOs had direct responsibility for both wage moderation and compression.

The court also helped centralize business organizations. Employers submerged their internal differences in order to cope with the wage indexation cases that came up every three months. The traditionally antagonistic Associated Chambers of Manufactures (protected industry) and Australian Council of Employers’ Federations (export industry) merged into the Confederation of Australian Industry in 1976.

As in New Zealand, incomes policy became the focal point of efforts to balance employment, inflation, and current account deficits. During the mid- to late 1970s the Australian court, unlike its New Zealand counterpart, absorbed all the damaging political consequences that Danish and New Zealand unions experienced from directly legislated wages, that Swedish unions experienced from direct, centralized collective bargaining, and that British unions experienced from the failure of collective bargaining. Compared with unions in 1970s New Zealand, Australian unions endured higher unemployment, more import penetration, and a hostile government, while finding an ally in the institutions of arbitration. So Australian unions entered the 1980s willing to institutionalize wage
restraint, and they made this public with the ACTU–ALP Accord that exchanged wage restraint for more employment and a higher social wage.

And as in New Zealand, the incumbent's mishandling of the economy put Labor in power, allowing it to try out the Accord. The Liberal-National coalition took the blame for the widening of the current account deficit from 1.5 percent of GDP in 1979 to 5.2 percent in 1982, for unemployment running at 10 percent, and for a public sector borrowing requirement of 8.1 percent of GDP. The ALP won a 25-seat majority in the 125-seat lower House, and a working majority in the Senate.

3.5.3. **Australia Reconstructed: The Accord, Markets, and Change in the 1980s**

The ALP wanted to change the link between sectoral wages that generated current account deficits while preserving social equality and a decent society by retaining some definition of wages and expanding the formal welfare state. The Accord was Labor's tool for breaking down the old horizontal pattern of wage parities responsible for pricing exports out of world markets. The Accord process aimed at freezing real private sector wages in order to generate more employment, at eroding sheltered sector wages in order to cheapen export prices, and at helping reorient manufacturing towards exports.

Simultaneously, the Accord explicitly and implicitly continued to provide basic social protection through a centrally set minimum wage. The Accord facilitated and rewarded productivity growth while still putting a floor under wages, and (as in the 1970s) the arbitration system helped the ACTU to externalize conflicts over greater wage differentiation. Meanwhile the ALP expanded the social wage in order to repay the ACTU for wage restraint. The ALP restored public financing for the health system, added a new second-tier pension and more social assistance, and created a negative income tax. Nonetheless, Australian social spending as a share of GDP was flat under Hawke and remained well below OECD and even New Zealand levels.

The Accord's macroeconomic side dovetailed with the ALP's liberalization and desubsidization of product markets. Decentralized collective bargaining and productivity-based wage increases rewarded competitive firms and cooperative unions. The ALP's microeconomic reforms—changes in trade and competition policy—forced firms to upgrade. The ALP reduced tariffs and non-tariff barriers across a wide range of industries. Though

4 Bob Hawke, pressed in 1983 to explain the difference between the Australian and British Labour parties, said, 'We win.'

there was less outright privatization than in New Zealand, the institutionalization of competition in the public sector went further. However public sector employment did not decline as in New Zealand (see Figure 3.6).

During the 1980s Australia created jobs at roughly twice the OECD average rate even as labor force participation rose (Figure 3.7). The social wage grew in absolute terms through the ALP's first term and then stabilized for ten years. Australia's manufacturing and service sectors did increase their exports after sheltered sector costs were controlled. Here the ALP delivered to its silent business constituency, lowering the wage share from 62.3 percent in 1983 to 59.5 percent in 1995, relative unit labor costs fell from 117.8 in 1983 to 83.8 in 1987, before rising to 103 in 1989; and productivity grew twice as fast as wages between 1983 and 1995. By some estimates, the trend rate of productivity growth in Australia has increased sharply, from roughly 1 percent annually between 1975 and 1991 to 2.7 percent each year after 1991 (OECD 1999: 65). Australian export performance was well above OECD averages under Labor, rising at an annual average of 3.3 percent in 1984–96.

International shocks and pressure from domestic business shaped the evolution of specific policies, including the various Accords. As the economy recovered from the 1982/3 recession Australia's predominantly privately owed total foreign debt tripled to 28 percent of GDP and the current account deficit swelled to 5.5 percent of GDP. In response, the Hawke government committed itself to no increases in Federal taxation, spending, or deficits as shares of GDP. This so-called 'trilogy' promise severely constrained relative increases in the social wage. It also focused attention on attaining greater productivity in both the public and private sectors so as to boost GDP and thus the volume of spending permitted. Another constraint with an impact similar to Hawke's 'trilogy' promise, the 16 percent fall in the newly floated Australian dollar, also galvanized a series of changes: the devaluation led to the great push for a new kind of labor relations in the public sector, to a new style of public management, and to the corporatization of public enterprises. The 1990–92 recession sparked a new round of collective bargaining decentralization and a search for active labor market policies.

The next sections deal in turn with the Accord, incomes policy, and collective bargaining; trade protection and competitive policy; the formal welfare state; and public reactions.

3.5.3.1. **The Renewal of Corporatism in Australia and the Evolution of Collective Bargaining**

The ALP and ACTU tried to resolve the contradictions in the Australian model and stabilize that model through the Accord. (Here Accord refers
to the basic ALP–ACTU compromise and Accord Mark II, III etc. to the eight specific Accords the two parties ultimately negotiated.) The Accord process had four aims. The first, tactical goal was to control any explosion in wages that might occur as Fraser’s wage freeze came undone in 1983. This succeeded. A second, strategic aim was to reduce the wage share from its 1970s peak in order to stimulate employment. The wage share did fall from 64.6 percent of GDP in 1982/83 and stabilized at around 60 percent; investment rose from 22.8 percent of GDP in 1983 to 25.4 percent in 1989 before falling back to around 20 percent in 1990s. Foreign debt financed much new investment. The third goal, articulated in Accord Mark II (1987–88), was to make wage gains in the sheltered sector contingent on productivity gains. Though harder to assess, the largest losses in real wages occurred in the public sector, while in the exposed sector (especially metals) real wages were stable. The fourth goal, hinted at in Accord Mark III and emphatically part of Accord Mark VI (1990–92), was to decentralize bargaining downward to the enterprise level, while still maintaining a decent, centrally set basic wage. This would permit successful exporters to pay high wages without the danger of automatically transmitting this higher pay to weaker sectors. By 1996 roughly one-third of all workers operated under enterprise-level contracts, one-third operated under centrally set awards, and one-third did not bargain collectively at all. Union density declined from 46 percent to about 31 percent during this period (Buchanan et al. 1997: 109).

The Accord process thus attacked the contradictions in the Australian model. With ISI exhausted as a development model, domestic demand alone could not make manufacturing output grow. Productivity had to grow in order to facilitate manufactured exports. The Accord linked productivity and wage growth, inducing unions to press employers for productivity-enhancing restructuring. The Accord rewarded cooperative unions and workers with legal second-tier wage increases. It also motivated employers to seek productivity gains and to invest. The combination of trade liberalization and persistently high basic wages meant that survival rested on productivity gains and investment. Firms that found acceptable productivity gains could raise workers’ pay and attract more and better skilled workers, so firms needed to bargain with workers over acceptable productivity gains merely to compete in local labor markets, let alone compete with low-wage imports. Here the ALP tried to assure that the shift of income from labor to capital would not be frittered away in increased consumption, much like what befell the Swedish Rehn-Meidner model.

The centralization of business and (even more so) of labor made this strategy plausible. By 1980 the ACTU had incorporated the major public

sector white-collar unions, bringing its coverage to 85 percent of unionized workers. In the early 1980s business split into two peak associations, each with a credible claim to speak for an important segment of Australian industry. A third association, the AFE, represented the smallest (and thus politically less important) firms (Techritz and Hatcher 1981: 79). The Confederation of Australian Industry (CAI) represented SMEs (small and medium-sized enterprises) and local firms. In 1983 the Business Council of Australia (BCA) was formed by the fifty largest firms in Australia, each with 5,000 or more employees. Both participated in the 1983 National Economic Summit and in tripartite organizations created after the Accord. The CAI was more willing than was big business to accommodate the ALP. On collective bargaining, business presented a full spectrum of opinion: the AFE (the smallest employers) wanted to ‘smash and crush’ the whole arbitration system, the BCA wanted to replace arbitration with enterprise bargaining over a fifteen-year period, and the MTIA (representing the metal sector) wanted coordinated sectoral bargaining, while the CAI was content with the status quo supplemented by some enterprise level bargaining (Plowman 1987).

The ACTU and particularly its metal unions felt that business had to be led because, as then ACTU president, Bill Kelty put it: ‘We have a management class which is ... incompetent ... [and] it did not generate the levels of investment and borrowing [needed] for this country’ (Sydney Morning Herald, 30 Apr. 1986). The ALP and ACTU used corporatism to divide and neutralize business opposition. Each Accord involved a silent partnership between the ALP and one of these business organizations. The metals firms (MTIA) supported the early Accords, while the BCA was decisive in shifting the Accord process more in the direction of enterprise bargaining around the time of Accord Mark IV (1988–89). MTIA firms (like Danish metals firms) preferred to take wages out of competition for their sector, while the multinationals in the BCA wanted their own enterprise bargaining. So the evolution of the Accord was as much a political process as a rational response to Australia’s structural problems.

Accord Mark III (1987), which supplemented award-based basic wage increases with productivity-based second-tier increases at the enterprise level, reflected the MTIA’s influence. The arbitration court had to bless productivity-based increases to prevent cheating (and retain its institutional role). The metals sector stood to benefit most from this arrangement, which permitted skills-intensive sectors of the economy to raise wages without fear that increases would spill over to stagnant parts of the economy (Thornthwaite and Sheldon 1993, 1996). Most of the metals sector enterprise bargaining were true supplements to the basic award, consistent with the MTIA’s desire to keep wages out of competition in the metals
sector. Private sector wages diverged strongly from public sector wages since, while public sector unions were motivated to seek enterprise bargains, they had fewer opportunities to actually increase productivity. Over time enterprise bargains became more common in the public sector.

The 1988 Industrial Relations Act formalized Accord Mark III, permitting enterprise bargains with the approval of the arbitration court. Enterprise bargains were not allowed to violate minimum standards, including the basic wage (Plowman 1992). As in New Zealand, the ALP used the new law to force smaller unions to merge or disappear, setting a 3,000-member minimum for union registration by 1991. By 1993, 98 percent of unionized workers were in nineteen unions, making coordination easier (Gahan 1993: 613).

In contrast, Accord Mark VI (1990), formalized in 1993 with the Industrial Relations Reform Act, reflected the BCA’s influence. Accord VI extensively promoted enterprise bargaining as a real alternative to central awards (Reitano 1994). However the arbitration court continued to impose minimum wages and conditions on enterprise bargains. Furthermore, while non-unionized firms could sign an enterprise bargain, doing so exposed them to the possibility of union intervention. Most such awards granted through 1992 were generated by the metals industry, while small and medium industry outside of metals tended to avoid formal enterprise bargains. By 1995 over 60 percent of federal agreements were enterprise bargains (Buchanan et al. 1997: 109).

The Liberal–National coalition government elected in 1996 also tried to pass a bill very similar to the New Zealand Employment Contracts Act. This bill would have permitted unrestrained individual contracting, removed minimum conditions, banned industrial unions, and lowered the minimum size required for registration. However, lacking a majority in the Senate, the coalition was forced to retain an ongoing institutional role for the arbitration court. The court continued to impose minimum conditions (in the form of a ‘no disadvantage’ test) on enterprise bargains but lost its ability to do this for individual contracts (i.e. so-called ‘Australian Workplace Agreements’). These individual contracts replaced the old non-union enterprise bargains of the 1993 Act and allowed small and medium-sized businesses to escape existing unions or prevent unionization. So far the new law has not significantly undermined either the award system or the ALP’s version of enterprise bargaining, for two reasons. First, New South Wales’ Labor government reversed similar state-level legislation. Second, unions in the waterfront and mining industries have successfully fought firms trying aggressively to move towards house unions.

3.5.3.2. Product Markets, Trade, and Competition

In trade policy both the ALP and Coalition government emulated New Zealand Labour, reducing effective rates of protection to industry and agriculture, albeit more slowly. Effective rates of assistance for manufacturing fell from 22 percent in 1983 to an estimated 13 percent in 1993 and were projected to fall to 5 percent by 2001 (OECD 1994: 78). Effective rates of assistance for agriculture fell from roughly 12 percent to 9 percent. These averages conceal wide variations in protection and also in the political modalities for reducing protection. Mirroring their core Accord bargain, the ALP showed a marked preference for corporatist solutions to problems in sensitive sectors.

In manufacturing, for example, the textiles, garments, footwear, automobile, and steel sectors were the most heavily protected, the last two for macroeconomic reasons and the first three because they accounted for 10 percent of manufacturing employment. The ALP made continued aid conditional on increased competitiveness and set up three tripartite fora for negotiating mutually acceptable transitions. Steel received the first such package in 1983, followed closely by autos and then by textiles, clothing, and footwear as a single group (Capling and Galligan 1993). These policies combined pre-announced and gradual market liberalization with penalties for firms if they did not comply with plan targets for upgrading quality and productivity.

Finally, in the single biggest signal of change, the ALP completely inverted the institutional apparatus for trade protection. The Industry Assistance Commission was relocated in the Treasury Department, combined with some of the tripartite fora, and ultimately renamed the Productivity Commission by the Coalition government. Rather than calculating the precise ‘made to measure’ tariff needed to support an industry, the Commission now churns out a wide range of international benchmark studies showing how far behind world market standards various Australian manufacturing and service industries are, so as to whip firms into higher productivity. As noted above, this new mission dovetailed nicely with the Accord’s insistence that wage increases above and beyond the basic wage increase could only come from increased productivity. At the same time all forms of export subsidy were grouped under one agency, Austrade, itself housed in an enlarged Department of Industry Trade and Commerce. Subsidies were used to promote exports rather than defend inefficient local production, and on this basis they rose to the highest level in the OECD (Capling and Galligan 1993: 141–44).

The ALP also deregulated finance and liberalized foreign entry in order to put pressure on domestic financial capital and make more foreign
capital available (Perkins 1989). The postwar Australian state had used financial regulation and repression to manipulate the economy. But the utility of regulation had declined with the rise of non-bank financial enterprises in the postwar period. Commercial banks' control of Australian financial assets fell from 52 percent to 39 percent between 1953 and 1979, while non-banks' share rose from 24 percent to 54 percent (Keating and Dixon 1989: 42). So the ALP viewed financial deregulation as an easy concession that might force down bank profits and benefit both real enterprises and workers. However, with the float of the Australian dollar, deregulation also subjected the government's ability to finance its fiscal deficit to approval or rejection by foreign financial markets. Given Australia's relatively low level of foreign currency-denominated debt, this was not an immediate constraint on the government. But financial deregulation and the floating dollar sent a strong signal to business and labor that the government would no longer guarantee full employment in the absence of reasonable relative unit labor costs. In this sense financial deregulation signaled to the ACTU that the ALP was bound either to the Accord or to an arbitration-imposed reduction in wage growth.

Finally, in the early 1990s the ALP set up the Hilmer commission on competition, which matured into the Australian Competition and Consumer Commission in 1995, and an intergovernmental National Competition Council (NCC). These organizations now oversee the introduction of competitive forces into various public and private sector markets. Hilmer and its follow-on organizations estimate that falling prices from the introduction of competition will stimulate a one-time gain of 5 percent in GDP, half of which will come from competition in core public utilities. While the NCC is a talking shop for ironing out differences between the federal and state governments, and while privatization is not a foregone conclusion of its policy deliberations, the introduction of market pressures is a certain outcome.

The federal and state governments also corporatized and privatized public enterprises. The federal government sold off its few but large holdings after 1990, including telephone. Formal privatization was more limited than in New Zealand, with both the ALP and some Liberal state governments preferring to retain public ownership but introduce competitive market pressures and full cost recovery. Only one neo-liberal Liberal Party government in Victoria privatized New Zealand-style. Essentially, though, full cost recovery, market pricing for capital, and product market competition had much the same effect that privatization would have had. By the mid-1990s, the government's business enterprises had shed labor-generated considerable income for all levels of government, halved their debt in proportion to GDP, and turned losses amounting to 2.1 percent of GDP (1985/86) into surpluses of 0.3 percent of GDP (1996/97) (Treasury 1997: ch. 7, pp. 27–31).

### Table 3.5 Australia—utilities employment, 1985–1995

<table>
<thead>
<tr>
<th></th>
<th>1985</th>
<th>1995</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employment, % of total employment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Electricity, gas, and water</td>
<td>2.1</td>
<td>1.0</td>
</tr>
<tr>
<td>Transport, storage, and communications</td>
<td>7.5</td>
<td>6.6</td>
</tr>
<tr>
<td></td>
<td>1985–90</td>
<td>1991–95</td>
</tr>
<tr>
<td>Productivity growth, annual average % change</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Electricity, gas, and water</td>
<td>11</td>
<td>6.9</td>
</tr>
<tr>
<td>Transport, storage, and communications</td>
<td>4</td>
<td>6.8</td>
</tr>
</tbody>
</table>


3.5.3.2. The Social Wage and Welfare

Formal welfare spending under the ALP was inextricably tied to the evolution of the Accord, because a rising social wage was part of the side payment to unions for acquiescing to a falling real wage. The increase in the per capita social wage was quite modest, 4.5 percent as compared with the 30 percent increase under Whitlam, but the raise reversed a 13 percent real decline under Fraser (Watts 1987). However, because the ACTU knew ALP trade policies would turn concealed into open unemployment, the bulk of the side payment to unions came as a result of increased employment. Unemployment fell by 2.8 percentage points from 1984 to 1989, despite a 5.1 percentage point increase in labor market participation. In addition, the practice of targeting made fewer dollars go further toward poverty reduction.

The ALP designed changes in the social wage to cushion the newly unemployed and to facilitate the entry of women into the workforce. The creation of dual or one-and-a-half income families and the topping up of single- or no-income families through social assistance would preserve families' disposable income during the transition to a more robust export economy. From 1985 to 1995 part-time employment rose from 18.2 percent to 24.5 percent of the labor force, and female participation rates rose from 45.7 to 53.8 percent (OECD 1997: 206).

Labor's social wage strategy had three elements: the restoration of a public health system (Medicare), more targeting of social assistance to those outside the labor market (especially single mothers), and the restructuring of universal entitlements in order to preserve public revenues for labor market losers.
In health care, the ALP reversed Fraser's privatization of Medibank. Fraser's reinstatement of private, voluntary health insurance had driven public share health spending from 72.8 percent to 62.9 percent. The ALP's 'Medicare' restored this to 71.5 percent by 1985, using a flat levy on taxable income (OECD 1995: 73). Because people paid whether they used the public system or not, this created an incentive to use the public system. Because the system was built on public payments to private providers, competition kept service quality high. Medicare's public approval rose from 44 percent to 68 percent in the 1980s, and the percentage of Australians buying private insurance fell from half to 31 percent in 1998. The system has survived Liberal–National efforts to shift people back towards private insurance with tax subsidies amounting to 30 percent of premia (Gray 1990: 238; OECD 1995: 76; Bagnall 1998: 19). Only 31 percent of the population used private health insurance in 1998. The ALP's restoration of public health detached health care access from employment access, easing fears about restructuring.

The ALP also increased in social assistance to cushion the transition from covert to overt unemployment, and from full-time male to part-time and more female employment, using targeting to husband limited fiscal resources. Social assistance programs were redesigned to top up the wages of those now working for lower pay, and to train those who had fallen out of the labor market. After two years of large real increases in federal spending, total spending at both the federal and state level declined gradually and returned to their initial levels as a share of GDP during the 1980s. But the distribution of payments did change. The ALP shifted funding towards child benefits and single parents in order to offset falling real wages. The universal child benefit was changed into a means-tested family benefit (now Basic Family Benefit), but with a test that included roughly 60 percent of the population. The Family Allowance Supplement (now Additional Family Payment), which provided additional cash on a per-child basis to working families under a much lower threshold, also cushioned the working poor while providing an inducement to stay in the labor market. Both acted like negative income taxes. Rising transfer payments offset the decline in market wages for the three poorest deciles of Australians (Saunders 1994: 183–85). However, income inequality increased from 1975 to 1994; the gini coefficient for market income rose by 36.6 percent to 46.3 percent and for disposable income by 5.2 percent to 30.6 percent (OECD 1997: 49–59). Targeting characterized more universal programs too. In Accord II (1985), unions agreed to restrain wages in exchange for the creation of an employer funded mandatory second tier pension (superannuation). This secured pension benefits without requiring government spending. Relatively highly paid skilled workers also pre-

ferred this defined pension benefit. Accord Mark VI (1990–92) institutionalized this ad hoc payment as the Superannuation Guarantee Charge, which committed employers to pay roughly 3 percent of wages into individual retirement accounts. The Liberal–National coalition has capped this at 9 percent of wages.

Finally, in May 1994 the Keating government launched a major active labor market policy called 'Working Nation'. Working Nation included a policy commitment to find public sector or subsidized private sector work lasting six to twelve months for anyone unemployed for more than eighteen months. Like similar Scandinavian programs, the idea was to keep the long-term unemployed from becoming permanently unemployed. Recipients had to choose between accepting a job offer or training. The Liberal–National government continued Working Nation as 'Jobstart'.

The ALP also introduced user fees in, among other things, higher education. Charging for access to tertiary education while providing a means-tested grant shifted resources from middle-class consumers to the poor. The Higher Education Services Charge (HESC), introduced in 1989, could be paid either up front as a discounted entry fee, or as a tax assessed as a straight percentage of income after graduation. Those without cash still had access to education; the amount they were obligated to pay back into the system was scaled against their actual income. From 1996 onwards, the HESC amounted to 23 percent of tuition costs for universities. Vocational educational venues traditionally used by poorer students either had no charge or a 10 percent charge. Efforts to bolster public primary education's share of the market for students failed when publicly funded, but private, Catholic schools fought successfully to retain their subsidies.

### 3.6. Institutional Capacity and Public Responses

Why and how did more radical change succeed in these two countries? The institutional and political capacities for change cannot be separated. Obviously, Westminster systems with fewer veto points make change easier, and (obviously) the easier it is for politicians to shift the costs of change onto politically weak sectors of society, the greater the potential for change in the face of international pressures. Like Britain, New Zealand had a pure Westminster system, 'first past the post' elections, single-member districts, a single-chamber legislature, and weak judicial oversight (Palmer 1979; Palmer and Palmer 1997). Determined minorities with parliamentary majorities could do as they pleased. In contrast, Australia has a two-chamber legislature, where the upper house is elected via
proportional representation and federalism allows state governments to impede federal initiatives. But these institutional structures did not initiate change or determine the kinds of change: rather, they affected reformers' ability to make changes. Australia's strong upper house clearly blocks any policy blitzkrieg à la New Zealand. But the mere existence of a Senate was responsible neither for generating the Accord as a strategy nor for enforcing it. What the Australian Senate does is prevent well-organized minorities from using political parties to push policy in directions the majority does not favor.

So how did the institutional landscape help or hinder the changes actors desired? Three mutually reinforcing institutional factors answer this question: (1) the degree to which the electoral system and constitution created governing majorities; (2) bureaucrats' willingness to articulate and enact change; and (3) the degree to which politicians were sheltered from short-term political pressures. Put crudely, these factors answer a threefold question: (1) Did politicians have the votes? (2) Did they have a plan and bureaucratic instruments to carry out that plan? and (3) did they have the time to carry out the plan? First past the post (FPTP) systems tend to create solid and durable majorities for reorganization-minded parties. FPTP limits the exit options of disaffected groups, making it relatively easy for governing parties to reorganize without high political costs. In turn, the more unitary the state, the larger the majority, and the more certain the government's tenure, the more bureaucrats were willing to help politicians craft and execute pre-emptive, comprehensive proposals for change that were difficult to oppose. And, finally, the more electoral breathing room politicians had, the easier it was for them to implement relatively comprehensive policies that would solidify their party's medium-term social base of support. Autonomy mattered because all the parties initiating reforms received significant electoral and financial support from actors threatened by change. Left parties experienced growing internal tensions along a fault line that separated unions representing workers in the exposed sector from those in the sheltered sector (with the public sector being the largest sheltered producer); right parties experienced tension along a fault line separating producers who were competitive in world markets from those relying on protected product or service markets.

3.6.1. New Zealand

New Zealand's state structures created considerable autonomy for both the Labour and National Parties, facilitating significant change. New Zealand's old FPTP single-member district system regularly gave minorities parliamentary majorities and great discretionary power. Labour's unqualified majority from 1984 to 1990 enabled it to ram legislation down the throats of the opposition both inside and outside parliament. National did exactly the same with the successful MMP (mixed member proportional representation) referendum in 1993. This made it certain they would be a minority party after the 1996 election.

Certainly of Labour's tenure and majority, Treasury bureaucrats provided politicians with detailed blueprints for deregulating and marketingizing the public sector (Treasury 1984, 1987; Jesson 1987; Oliver 1989). The Reserve Bank was equally aggressive with regard to exchange rate and fiscal policy; a new organic statute eventually made it the OECD's most independent central bank.

With plans in hand, Labour politicians proved adept at dividing up opposition. As noted above, symbolic and real payoffs to core constituencies in unions and the intelligentsia distracted those groups from making fundamental changes to economic and administrative structures (Vowles 1990). Significant internal opposition only emerged after unemployment doubled from 1987 to 1989, and it was concentrated among those hardest hit, mainly unskilled and public sector workers. They and their unions eventually hived off the Labour Party in 1989 and formed the New Labour [sic] Party, which arguably helped destroy Labour's chances for electoral victory in 1990 in at least eight seats. Solid majorities of voters either openly distrusted or were not sure about their preferred party by 1990 (Vowles and Aimer 1993: 148, 150, 153).

National's extension of Labour's policies into the labor market also created serious public opposition, which spilled over into two referenda on changing the electoral system. A non-binding vote in 1992 showed that 71 percent of the electorate preferred MMP to the status quo; a binding referendum in 1993 confirmed this. MMP, with a 5 percent threshold, came into effect for the 1996 election. The party system immediately fragmented into five serious parties. The center-right National–NZ First coalition government that ensued proved much less aggressive about change than its National-only predecessor. The 1999 election returned a center-left coalition government committed to a cautious expansion of the formal welfare state. Just as in the prior election in Victoria, Australia, rural losers from the marketization of public services decisively swung to left parties.

3.6.2. Australia

Australia has single-member districts and transferable votes for the lower federal house but quasi-proportional representation in the upper house. It is also a federal system. Unlike Labour in New Zealand, the ALP could not simply legislate change. Instead, the ALP used its control over the
federal government to lead by example and used block grants to the states as bribes/threats. Though the ALP moved more cautiously than New Zealand Labour, co-opting opponents of reorganization, Australian Labor moved just as systematically.

As in New Zealand, bureaucrats played a crucial enabling role, despite being somewhat hostile to change. The Reserve Bank’s head in 1983 favored fixed exchange rates, as did his immediate successor. But Treasury, under Keating, and Finance, under John Dawkins, strongly favored marketization. The Finance Ministry and the Department of Prime Minister and Cabinet originated plans for public sector reorganization only slightly less comprehensive than those in New Zealand.

The ALP also skillfully balanced the competing interests of public sector/unskilled workers and private sector/skilled workers. Strong employment gains and a more pragmatic approach to privatization prevented a split among the public–private and sheltered–exposed cleavages until union voter defections sank the ALP’s electoral ship in 1996. Unionized workers also defected from unions, which lost about one-third of their share of the workforce from 1982 to 1996. Still, it is notable that the Liberal–National coalition in 1996 ran on a fairly moderate platform rather than on a program as overtly neo-liberal, and losing, as its 1993 platform. Like Labour and National in New Zealand, the Coalition surprised everyone with its radicalism in deregulating the labor market. Here, Australia’s two-house legislature proved an impediment to the actual implementation of change. The coalition lacked a majority in the Senate and had to compromise with a minor centrist/greenish party.

Federalism has also impeded change. Both the ALP in the 1990s and the Liberal–National coalition after 1996 faced hostile state-level governments in some of the larger states. Moreover state elections have sent strong signals about voter resistance to change. The unexpected Labor Party victory in Victoria in September 1999 both eviscerated the most neo-liberal of the state governments and induced more moderation in the federal government’s neo-liberalism.

### 3.7. Conclusions

Divergent politics and policy reforms in Australia and New Zealand, as well as the contrast with Britain, suggest that there is no common Anglo-Saxon path in response to fairly similar economic vulnerabilities. Different collective bargaining institutions, different experiences with incomes policy, and different moral economies produced quite different policy choices in the 1980s and 1990s. Australian workers and their unions had less to fear from entrusting wages and employment to central institutions. In the 1980s autonomous state wage-setting institutions in Australia made a ‘Blairite’ path possible and preferable to a ‘Thatcherite’ path. Arguably, Hawke’s example made Blair possible. The outcome of reforms also strongly suggests that neo-liberal reforms are not particularly conducive to successful employment or social policy.

Ironically, both of the Australasian political strategies have returned to post-Thatcher Britain. Blair absorbed and campaigned on the government’s promises and party discipline demonstrated first by the Hawke ALP government. Conservative party leader Hague meanwhile has absorbed the policy messages first demonstrated in New Zealand and then refined in Alberta, Canada and Ontario, Canada; Hague even adopted the campaign slogan of a ‘Common Sense Revolution’ from Ontario’s Conservative government.

Despite the substantial transformations of their postwar models, both economies remain vulnerable to the international economy. While some of the older dynamics that generated current account deficits are gone, they have been replaced by new ones. For Australia, and even more so New Zealand, high levels of foreign debt have become a substantial burden, requiring ever larger trade surpluses. While their successfully reorganized models mean that they are both better positioned to supply manufactured exports to world (and particularly Asian) markets, they remain hostage to growth in those markets, just as they were hostage to growth in their nineteenth-century markets for wool and foods.

At the same time, reorganization has clearly shifted the burden of market risks away from capital and onto workers. Both Australia and (even more so) New Zealand have replaced systems of informal welfare with formal welfare. Open unemployment and employment at market-defined wages have replaced hidden unemployment at socially defined wages. The hidden unemployment of the postwar model imposed a burden on profit levels, particularly for export producers. Wages and mandatory benefits had to be paid first, then shareholders. The displacement of covert by overt unemployment means that firms can more easily externalize world market pressures by firing workers. This has placed additional burdens on these countries’ public treasuries as people turn to formal welfare to ameliorate those risks. In Australia this motivated the Liberals’ politically costly, but successful effort to replace income taxes with an exporter-friendly GST (i.e. VAT). In New Zealand, legislation binds the state to low wages, low inflation, and low deficits, significantly constraining any effort to expand formal welfare.

What about these countries in relation to each other and to the international environment? By the 1990s, subsequent—although perhaps not
consequent—to their reforms and public sector reorganization, Australia and New Zealand were performing at or better than the OECD average in terms of fiscal deficits, inflation, unemployment, and GDP growth. Only their current account deficits were higher than the OECD average. Moreover, from 1981 through 1993, as Table 3.6 shows, Australia’s and (to a lesser extent) New Zealand’s export performance were well above OECD averages. This suggests that efforts to change the old models certainly undid some of the dynamics generating excessive import growth. And per capita GDP grew significantly faster in both Australia and New Zealand after 1990 compared to rates in both the OECD in general and OECD Europe. However, Australia clearly did much better than New Zealand, growing at an average of 3.0 percent annually from 1984 to 1992 and 4.2 percent from 1992 to 1998, whereas New Zealand only grew 0.4 percent and 3.3 percent per annum, respectively. If New Zealand had grown at Australian rates, its GDP would have been 20 percent higher in 1992 than it actually was (Dalziel 1999).

Table 3.6 Export growth, annual percentage change, 1981–1993

<table>
<thead>
<tr>
<th></th>
<th>Goods</th>
<th></th>
<th></th>
<th>Services</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Exports</td>
<td>Imports</td>
<td>Net growth</td>
<td>Exports</td>
<td>Imports</td>
<td>Net growth</td>
</tr>
<tr>
<td>Australia</td>
<td>10.6</td>
<td>9.7</td>
<td>0.9</td>
<td>12.2</td>
<td>9.3</td>
<td>2.9</td>
</tr>
<tr>
<td>New Zealand</td>
<td>9.2</td>
<td>8.7</td>
<td>0.5</td>
<td>10.6</td>
<td>9.3</td>
<td>1.3</td>
</tr>
<tr>
<td>Smaller OECDa</td>
<td>6.5</td>
<td>5.6</td>
<td>0.9</td>
<td>7.6</td>
<td>7.5</td>
<td>0.1</td>
</tr>
</tbody>
</table>

aNon-G7 OECD.


3.7.2. Australia: The New Model

The ‘new’ Australian model strongly resembles the old. Socially defined wage minima, the most distinctive feature of the old model, remain an important part of the institutional landscape. Market principles mark major parts of the welfare state, but without compromising equal access. The welfare state was rationalized by adjustments that accommodated the rising share of part-timers and women in the labor force, not by downsizing. Unlike New Zealand, public spending and revenues have been constant relative to GDP since 1985, although the introduction of a GST (VAT) in 1998 marked the beginning of a shift away from income taxes. But import substitution via ‘protection all around’ is clearly gone, as is comparative wage justice.

Has Australia discovered a viable version of the ‘decent’ competitive welfare state? Economically, the persistence of non-market wage setting under the ambit of the arbitration court(s) conflicts with liberal macroeconomic, trade, and industrial policies, although the arbitration courts’ coverage has shrunk to roughly two-thirds of the workforce. Continued wage minima and pockets of resistance to increased productivity arguably explain why Australia’s open unemployment rate remains higher than New Zealand’s or Britain’s (and high by Australian historical standards, although not by comparison to Continental Europe). But despite higher unemployment the model has avoided the extreme poverty seen in both places, where work has been redistributed between winners and losers. Despite the explicit link between wage and productivity gains, the arbitration court retains the ability to shift part of the productivity gain out of firms and into the rest of the economy, avoiding the widening income gyre seen in New Zealand. This ability precisely mirrors the capacity of European governments to redistribute income through taxation, and with about the same degree of opacity.
Consequently, the political burdens of adjustment to international economic pressures fall harder on Australian workers’ organizations than on unions in either New Zealand or Britain. Arbitration and efforts to maintain a social wage mean that competitiveness rests on some workers’ willingness to accept lower wages than their underlying productivity merits. As Sweden in the 1980s shows, this is difficult over the long term. By 1996 it became clear that union members did not find this deal acceptable; union density fell considerably and union members did not support the ALP in 1996 in numbers large enough to win the election. Still, the ALP and ACTU clearly did a better job of ameliorating those tensions than did New Zealand Labour, which split in 1989, or New Zealand unions, which split in 1991. While the defecting groups were small, factionalization in New Zealand and Britain gave parties on the right parliamentary majorities and power. Later in Britain, by contrast, Blair’s Australianization of Labour returned it to power.

Economically, Australia continues to accumulate foreign debt, which now stands at over 40 percent of GDP. But most of this is private debt, and so falls on business. For some time it looked as if Australia was repeating New Zealand’s error from the 1970s and delaying adjustment by borrowing. But New Zealand’s ongoing and growing reliance on foreign investment indicates that both countries continue to rely on foreign capital for growth. In this respect, nothing has changed since the nineteenth century.

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Switzerland
Adjustment Politics within Institutional Constraints

GIULIANO BONOLI AND ANDRÉ MACH

For much of the twentieth century, Switzerland has been an exemplar of political and economic stability. The events that shattered people's lives in its European neighbors like wars, recessions, or political unrest, affected this country only marginally. In the late 1990s, Switzerland was still displaying patterns of political stability and economic prosperity that were unusual by international standards. Nevertheless, the solidity of the Swiss political and economic model does seem to have suffered somewhat over the last decade. Several developments have combined to undermine the economic, political, and social underpinnings of Swiss stability: the emergence of unemployment, a social problem that was virtually unknown in postwar Switzerland before the early 1990s; an increase in public budget deficits; and the pressures induced by changes in the country's international environment.

The magnitude of social and economic problems that Switzerland is currently facing remains low by European standards. With an unemployment rate of less than 4 percent, the country ranks among the best in Europe. Even though social problems are on the rise, developments like large-scale social exclusion remain virtually unknown. The budget deficits of the 1990s, although they stand out in historical data series, are moderate by European standards, and Switzerland would have qualified for membership in the EMU. Moreover, unlike the way it was in other European countries earlier, the recession of the early 1990s and ongoing trends toward economic internationalization have not resulted in dramatic losses of business confidence.

Deteriorating socio-economic conditions have probably not been the most significant development of the 1990s. Instead, the landmark change has been a decline in the level of support for the traditional postwar model.