

STATE OF THE NATION

AN AGENDA FOR CHANGE

Edited by **JENNIFER BUCKINGHAM**

There is much to celebrate in Australia's progress. We have an unprecedented level of individual wealth and are living longer. Current levels of health and wealth have been built on stability, work and creativity. For this we can thank the institutions of our liberal democratic society, which have fostered a steady pace of reform and change. But much remains to be done. *State of the Nation* offers valuable insights into issues vital to Australia's present and future and sets out an agenda for change.

This fourth edition of *State of the Nation* covers a lot of ground, with chapters on population change, families and fertility, civil society and social capital, education, health, welfare, poverty and taxation, labour markets, economic performance, and aid and development. The connections between trends in these seemingly separate areas of life are explored and some key messages emerge.

The first is that we have become too dependent on government and less free as a result. The second is that governments must become more accountable. Australians cannot afford to be complacent about the way public money is spent, either at home or abroad.

This book uses data and research evidence to present a compelling and cohesive perspective on the sorts of reforms that must take place if Australia is to continue to prosper and if its citizens are to maintain and improve their quality of life. It should be read and referred to by policy makers, politicians, journalists, academics, teachers, students, and indeed anyone with an interest in social and economic affairs and the future of our nation.



Jennifer Buckingham is a Policy Analyst at The Centre for Independent Studies. She is co-author of *State of the Nation* (1999, 2001) and author of *Boy Troubles: Understanding Rising Suicide, Rising Crime and Educational Failure* (2000), *Families, Freedom and Education: Why School Choice Makes Sense* (2001) and *Schools in the Spotlight: School Performance Reporting and Public Accountability* (2003).

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INTRODUCTION

In many respects, Australia has come a long way. Australians are wealthier and healthier than ever before. Our best measure of quality of life is quantity of life, and Australians born today can expect to live for 80 years—longer than any generation before them, while per capita income has risen to unprecedented levels over the past decade.

Current levels of health and wealth have been built on stability, work and creativity. For this we can thank the key institutions of our liberal democratic society, including the marriage-based family, democratically elected and limited government, reasonably secure private property rights, free markets, the right to work, reasonably good education, and the rule of law that protects individual freedom and responsibility. These have fostered a steady pace of reform and social change.

Policy reform is, however, a double-edged sword. The intended benefits of many policies have been accompanied by unanticipated and destructive consequences. For example, the introduction of no-fault divorce law in 1975 has not just made it easier to dissolve harmful marriages, but also to prematurely abandon difficult ones. Welfare payments to alleviate poverty have increased welfare dependency. Medicare has improved health coverage, but has been a disincentive for people to plan for their own health costs. The result is an ever expanding public health budget and a system that provides the most benefits to those who need them least.

Government policies and legislation designed to alleviate existing problems have created new ones and as governments seek to resolve these new problems, it leads to the expansion of the state into our everyday lives. Expansive government is also expensive government. Developments detailed throughout this book have led governments to appropriate more and more money through taxes. The less money people have in their pockets, the more they rely upon government services and welfare payments. Individual effort and risk taking becomes unrewarding, establishing a dependency and intervention spiral than threatens to escalate out of control.

Australians must make some tough decisions. The authors of the following chapters in this book spell out the problems before us and the choices we face.

In Chapter 1, Helen Hughes shows that population growth slowed over the second half of the 20th century, with low fertility making immigration increasingly necessary. Australians have, for the most part, accepted and even embraced the effect immigration has had on Australian society. Illegal immigration has not been a significant problem, but instability and the failure of development in many countries has the potential to draw illegal immigrants to Australia. Government policy, however discomfiting, has been an effective deterrent to illegal immigration and people smuggling, which has become a serious problem for most other liberal democracies.

Australia's declining fertility rate will have social and economic consequences. Fewer babies mean a smaller, older Australian-born population. Higher immigration, whether by enlarging legal immigration intakes or by relaxing border controls, may increase

Australia's population, and will indelibly change its character. It must be decided whether this is what Australians want, and plans made accordingly.

Fertility is inextricably linked to the status of the family. From a complex web of cause and effect, Barry Maley teases out some of the factors involved in the retreat from marriage-for-life in Chapter 2.

Research suggests that most people still consider stable marriage to be the best environment for raising children. Unfortunately, many children are denied this opportunity. Rising ex-nuptial birth rates and high divorce rates have resulted in an increasing number of children being raised without one of their natural parents. While there may be debate about how bad this is for children, most people acknowledge that it is not ideal. It is partly for this reason, Maley suggests, that women are having fewer children, or none at all. If women and men cannot rely on the marriage contract to ensure their spouse's ongoing commitment to them and their children, they will seek to minimise the cost of its failure. Increasing education and higher status employment for women have also played a role in delaying marriage, reducing the window of opportunity for children to be born.

The family, and the successful raising of children to be productive and responsible citizens, is vital to a society's future and quality of life. A strong civil society allows people to interact freely and to feel safe in their homes and communities, with citizens maintaining and observing the law.

As Caspar Conde shows in Chapter 3, there has been an increase in criminality in the last 40 years and police numbers have not risen to meet the demand set by higher crime rates. Effective policing is crucial for detection and imprisonment which reduces crime by acting as a deterrent and by keeping offenders out of society. Crime is not the only measure of the smooth functioning of a society, but it is the most tangible, affecting other aspects such as social capital—loosely defined as trust and cooperation between individuals in a society. High crime rates undermine this trust and so diminish civil society. There is less voluntary and mutually beneficial interaction between people and organisations which necessitates greater state intervention, less privacy and less freedom. This is not a desirable road to take.

The education of its citizens is a task all developed countries take seriously. To ensure universal access to education in Australia, all children are entitled to a school education at public expense. Unfortunately, government funding of schooling has translated into government provision of schooling, and parents who choose a non-government school for their children must do so without the financial support they would enjoy in the public system. In Chapter 4, Jennifer Buckingham shows that despite this obstacle, significant and growing numbers of children attend non-government schools. If public school systems do not learn to compete, they will become unsustainable.

Trends in education are often symptomatic of wider social movements. Women's liberation and feminism pushed girls' education to the fore. But, as with changes to divorce law, another case of a double-edged policy reform, changes that helped girls seem to have disadvantaged boys. Boys have not kept up with girls' progress, and there is evidence that their education may have even declined. The gap between boys' and girls'

levels of literacy grows while they are at primary school and becomes a chasm in Year 12. Declining numbers of male teachers are implicated in this trend.

With a larger proportion of children now completing six years of secondary school, there is increasing pressure on the higher education system to accommodate them. In Chapter 5, Andrew Norton shows there is strong growth in higher education enrolments and an overall increase in educational achievement among the population. The demand for higher education has put strain on university budgets which cannot accommodate all prospective students in Commonwealth-funded places. New arrangements allowing students to pay for their education will alleviate this somewhat, but will not go far enough to ensure that both students and universities benefit.

Public opinion polls show that—alongside education—health care is important to voters. Both are seen as fundamental citizen rights which should be accessible to everyone. No one should be denied good health care on the basis of income. Helen Hughes and Peter Saunders demonstrate in Chapter 6 that Australians have, in general, good health and a reasonable standard of health care. However the money spent on health is not always used as efficiently as it should and could be. This makes for very little accountability, poor working conditions and chronic staffing problems.

Public spending on health care is rising, and this will accelerate as the population ages unless the health system becomes more efficient. People must take more responsibility for their own health, both by observing healthy lifestyles and being prepared for illness or injury. Over-reliance on the public health system by people who can afford to look after themselves has severely burdened a system already crippled by ineffective management, sometimes with fatal consequences.

The welfare and social security system tells a similar story in Chapter 7. People are more dependent on the state than ever before, ironically at a time of high prosperity and relatively low unemployment. Most of the increase in welfare dependency has been in the numbers of disability pensioners and single parent pensioners. Within a matter of decades, there will be more people not working than there are working and the shrinking proportion of taxpayers will be unable to fully support the young as well as the growing ageing population.

Peter Saunders argues that unabated expansion of the welfare state is not only an economic disaster but detrimental to the wellbeing of individuals and society. Reform is vital. More people must be prepared to support themselves in retirement out of their own lifetime savings. Within the working age population, people who can work should work. Eligibility for welfare should be tightened and conditions strictly enforced.

Social security and state welfare ostensibly arose as a way to alleviate poverty and to help people through temporary periods of hardship. They have evolved into a monolithic income redistribution mechanism. In Chapter 8, Saunders examines the notion of poverty and shows how different definitions create widely disparate claims of the extent of poverty in Australia. Poverty is relative, and must be separated from income inequality. Just because one person has much more income or wealth than another doesn't make the latter poor. The conflation of poverty with inequality, and the desire to redistribute money from the top to the bottom, has led to excessive income

taxation which is now levied not just on the wealthy, but on people with incomes just above average. Those who are taxed to fund the welfare and health care system are largely those who end up requiring it.

Not even advocates of the welfare state claim that people living on unemployment benefits have a good life. While some propose that benefits be increased to reduce poverty and improve quality of life, statistics show that the people least likely to be poor are those with jobs. The solution, clearly, is to move people from welfare to work. In Chapter 9, Kayoko Tsumori presents a picture of the labour market and notes its strengths and weaknesses. She argues that many people are locked out of the labour market by regulations that make hiring expensive and risky for employers.

Minimum wages restrict job creation by making low-skilled workers unappealing to employers, while unfair dismissal laws deter employers from giving a chance to people who need one. Both employers and the unemployed are disadvantaged. Some freedom to negotiate wages and conditions has been introduced in the last decade or so, and it has not had the dire consequences predicted. Tsumori argues that the best way to improve the prospects of workers is to make the labour market an employee's market and apply the rules of the common law. The more jobs there are, the more workers will be in demand, and the greater their bargaining power.

A robust and dynamic labour market is one of the linchpins of a strong economy. In Chapter 10, Wolfgang Kasper assesses the short and long-term performance of the Australian economy with reference to key policy goals. Inflation has abated, at least for the time being, but we still do not enjoy complete price-level stability. Unemployment has slowly come off the peaks reached a decade ago, but remains unnecessarily high. The business cycle has been relatively stable over the past decade, which can be attributed to deregulation and the opening of the economy. Kasper explains that all economies go through some cyclical fluctuations as the demand for products utilises the economy's growing supply potential to varying degrees. The external balance—broadly speaking, exports minus imports of goods and services—has also become more predictable, once again thanks to enhanced flexibility, particularly in the exchange rate of Australian dollars. However, imports are running ahead of exports, so that foreign debt is increasing in possibly unsustainable ways.

After many decades of constrained economic growth, per capita incomes and productivity have accelerated over the past decade. Long term economic growth in Australia had been extraordinary in the 19th century, but was then increasingly weakened by industry protection and excessive regulation for most of the 20th century. The reforms of the mid-1980s and early 1990s did away with some of the obstacles to Australian enterprise, and robust economic growth and a new social optimism were the welcome results.

In Chapter 11, Wolfgang Kasper reports on measures of economic freedom that are linked to long-term economic performance. The benefits of economic freedom are manifold, apart from being a value in its own right. Countries with secure property rights, free markets and equality before the law tend to experience the highest rates of economic growth, the highest life expectancy and the least absolute poverty.

Australia still has one of the freest economies in the world, but could easily be better. Its international rating, according to estimates by the Fraser Institute and The Centre for Independent Studies, has slipped in recent years. This is largely due to excessively regulated labour markets and large government. Each decade an increasing share of the nation's GDP has gone toward financing government activities, including the imposition of thousands of new pieces of legislation and regulation by Commonwealth and State governments.

As one of the freest and therefore wealthiest countries in the world, Australia has committed billions of dollars to foreign aid. People in poor 'developing' countries have been victims of repressive and often corrupt governments. It has become apparent that in many cases, our beneficence has not reached the intended recipients and has often been counterproductive.

In Chapter 12, Helen Hughes draws attention to the failure of most developing countries to take advantage of opportunities to catch up with the standards of living in liberal democracies. Moreover, growth has been inversely related to aid. Most aid, notably to the South Pacific, has been appropriated by elites in urban centres. This builds a strong case for a mutual commitment to conditional aid—that countries receiving aid show their determination to develop in regularly assessed ways before aid is disbursed.

Two key messages emerge from *State of the Nation*.

We have become too reliant on the state. This has resulted in an ever-expanding government that is intruding into more and more areas of our lives. This becomes self-fulfilling; the less individual responsibility we take, and the more we expect of governments, the more government we get, and the less freedom we have. It happens incrementally, and before we know it, we can no longer take responsibility for things we would like to. Once freedom has been lost, it is hard to get back.

Also, governments must be more accountable. In two of the most important areas of public spending—education and health—little or no information is available to the people who pay for it through their taxes. The demands on the public purse are becoming so great that Australia cannot afford to be complacent about the way public money is spent, either at home or abroad.

There is much to celebrate in Australia's progress, but much remains to be done. *State of the Nation* sets out an agenda for change to ensure that Australians continue to enjoy a high quality of life that is the envy of much of the world.

ABOUT THE AUTHORS

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1. POPULATION & IMMIGRATION

HELEN HUGHES

Introduction

Population and immigration policies are central both to Australia's place in the world and to the welfare of its citizens. Policy views range widely—some would like to see Australia's population shrink on ecological grounds to perhaps four or five million people; others consider a population of 40 to 50 million essential to Australia's ability to protect itself against threats of invasion ranging from many thousands of boat people to armies.

These are extreme views. Technological advances, together with Australia's capacity for investment in environmental preservation and enhancement, can guarantee a sustainable, ecologically rich environment for a growing population.

Population growth has two components: the fertility rates of the resident population and net (immigration minus emigration) overseas migration.

Fertility rates are determined by social and economic trends. There has been a demographic transition from high birth and high death rates (with expectations of life typically around 40 years at birth in poor developing countries) to low death and low fertility rates (with an expectation of life of upwards of 80 years in wealthy countries, such as Australia).

Although economic growth has been disappointingly low in most developing countries, nutrition and water supplies have improved sufficiently, together with medical advances, so that the demographic transition is now worldwide. After the unprecedented world population growth from the 1950s to the 1970s, by 2010 (or even earlier), a majority of the world's people will live where fertility is below replacement levels. Given the cohorts of youthful populations left by past rapid population growth, the world's population is likely to settle between eight and nine billion people by 2050 and then decline.

In contrast to Europe, beset with large numbers of asylum seekers, Australia's remoteness and the relatively strong economic performance of its East Asian neighbours have limited illegal immigrant arrivals. Even small numbers, however, have created deep divisions in Australian society.

Unfortunately, repression and slow growth in developing countries (see Figure 12.1, p.150) suggest that the pressure for emigration from developing countries is not declining. Modern communications disseminate information about differences in living standards and economic opportunities between developing and developed countries, contributing to a pent-up demand of at least 10 million would-be emigrants from developing countries. If migration became easier, the numbers of potential emigrants would explode.

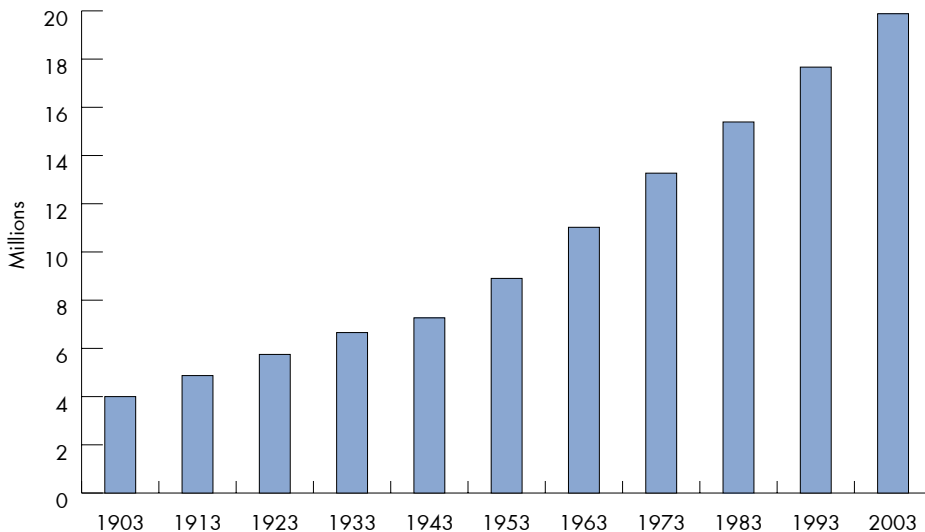
Australian Population

Rapid immigration, mainly from Great Britain and Ireland, created the Australian colonies in the 19th century. Unemployment in the first half of the 20th century reduced immigration to intermittent and modest flows. Post World War II labour shortages renewed rapid immigration, sourced first from Europe, and then also from the Middle East, Asia and the Pacific. Fertility rates were also high in the post World War II years with a peak of 3.4 births per woman, and Australia’s population doubled from 10 million in 1960 to 20 million in 2003.

High immigration stimulated economic growth, transforming Australia from a small to medium sized economy, and helped to change it from a lagging to a leading industrial economy. New multicultural strands greatly enriched everyday life for all residents. New arrivals and resident Australians found work and earned incomes that enabled them to live comfortably: buying houses and cars, exploring Australia in their holidays, travelling abroad, and educating their children, all while improved health standards extended life expectancy at birth to some 80 years. Some newcomers as well as residents contributed markedly to science and public debate, professional life, business, the arts, and sport, establishing international reputations. The children of immigrants became better educated than their parents, exceeding the norms for previous generations.

1.1 Australian Resident Population, 1903-2003

Millions of people (as at 30 June)



Source: ABS, *Australian Demographic Statistics*, Cat. 3101.0 (Canberra: ABS, various years).

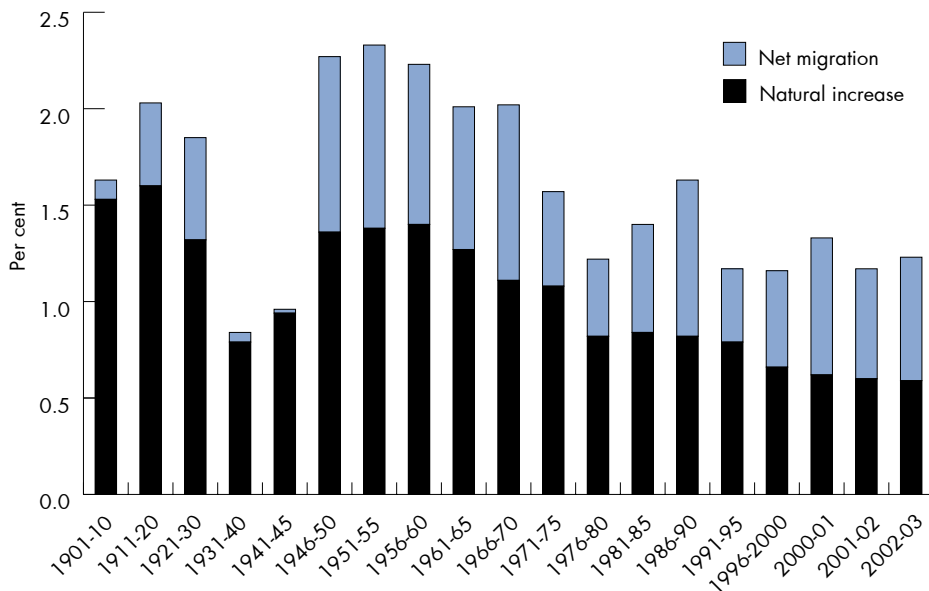
Components of Population Change

Figure 1.2 shows the average annual increase in Australian population from 1901-2002 in total, by natural increase and by immigration. The annual increase slowed throughout the 20th century, first as net overseas migration fell and then as fertility rates declined. The period 1951-1955 had the highest rate of immigration, but the period 1986-1990 had the highest proportion of growth by immigration.

Natural increase is the amount by which the number of births exceeds the number of deaths. In each five year period the contribution to population growth by natural increase was greater than by immigration.

Because of its past immigration, Australia has a relatively young population compared with other industrial countries. But in the most recent period, 1996-2000 as well as during 2001-2002, fertility rates have fallen to such an extent that almost as much of the growth in population resulted from net immigration as from natural increase of the Australian resident population. Nowadays, a considerable proportion of women are committed to working to achieve social and economic independence, and women are marrying later or not at all. They are having fewer children to be able to balance their commitments to family and work (see Chapter 2).

1.2 Population Increase, 1901-2003
Natural increase, net overseas migration and total increase



Note: Discrepancies between the sum of the rate of growth due to natural increase and net migration and the rate of total growth are due to intercensal adjustments.

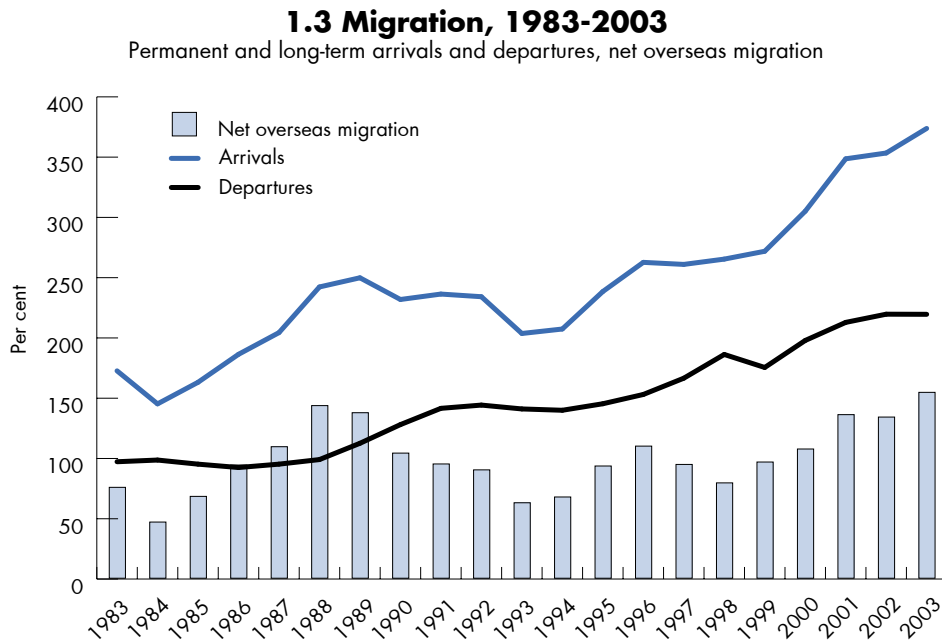
Sources: ABS, *Yearbook*, Cat. 1301.0; *Australian Demographic Statistics*, Cat. 3101.0 (Canberra: ABS, various years).

Migration

Legal immigration to industrial countries totals nearly three million people annually. Immigrants to industrial countries include about 50,000 refugees (as defined by the 1951 Refugee Convention) fleeing repression in developing countries. An additional 500,000 ‘asylum seekers’ from developing countries succeed in entering industrial countries annually. Less than 12% of these on average—50,000 a year—have been granted refugee status on arrival in industrial countries. Another four million illegal immigrants, not all of them long term, make up a total flow of some 7.5 million migrants annually to industrial countries.

Australia’s distance from other countries, backed with rigorous though non-discriminatory and transparent immigration rules, has largely confined immigrants to those seeking legal entry.

Net overseas migration includes the annual excess of ‘permanent’ (including economic, family reunion and refugee/humanitarian) and ‘long stay’ (mainly student and business) arrivals over departures. These definitions are necessarily fuzzy. Both emigrants and immigrants often change the intention stated at the time of departure or arrival. Figure 1.3 shows that net overseas migration to Australia has fluctuated.



Source: ABS, *Overseas Arrivals and Departures*, Cat. 3401.0 (Canberra: ABS, various years).

Asylum Seekers

Asylum seekers are principally economic and social emigrants thwarted by limited Western immigration places and consequently long immigration queues. With increasing numbers of middle and upper income earners wanting to emigrate from repressive and stagnating developing countries, criminal syndicates focus on migrants with financial resources. They assist potential migrants with forged documents and coach them to improve their chances of successful entry. Children are often introduced into asylum seeking groups to enhance receptiveness.

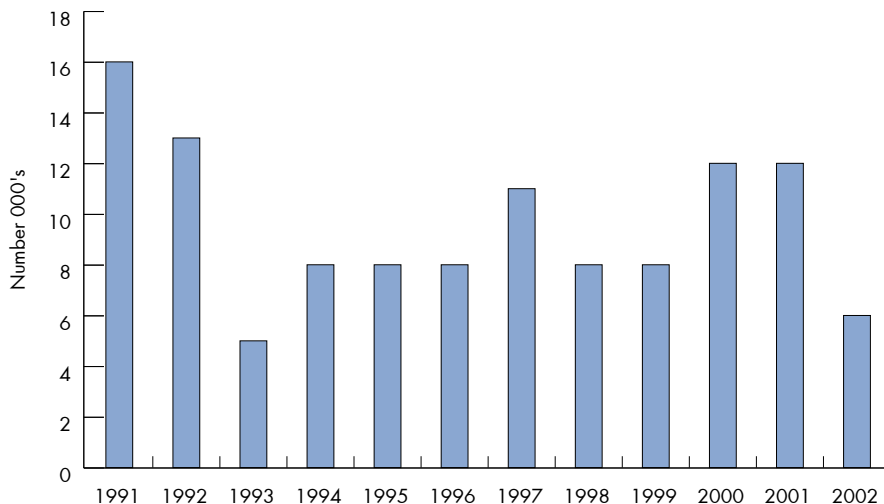
People smugglers are totally unscrupulous in extorting money for fares and collecting it from families in home countries and earnings in destination countries. They frequently fail to deliver the results they promise, resulting in multiple fatalities.

Repressive regimes have destroyed the economies of many developing and transitional countries, encouraging emigration. Ethnic and religious minorities suffer even greater repression in such countries. Liberal Western democracies, including Australia, are sympathetic to these victims of repression. They try to find room for them in their immigration programmes, but they cannot accommodate the large numbers attempting to better their lives through emigration without jeopardising the very lifestyle and institutions to which the immigrants are attracted.

Because successful 'asylum seeking' encourages people smugglers, liberal Western democracies have taken draconian measures, returning immigrants without legal entry papers at borders and imprisoning many in common jails pending deportation. Mandatory detention, however regrettable, has substantially reduced people smuggling to Australia.

1.4 Asylum Seekers Arriving in Australia, 1991-2002

Number each year (thousands)



Sources: OECD, *Trends in International Migration* (Paris: OECD, 2001, 2002, 2003); ABS, *Overseas Arrivals and Departures*, Cat. 3401.0 (Canberra: ABS, various years).

Refugees

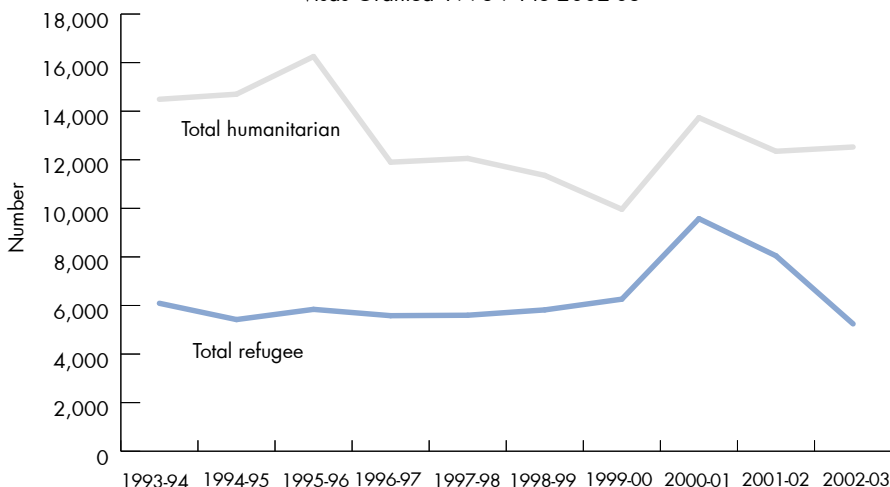
Refugees are a distinct group. Australia is committed to an annual intake of 12,000 refugees. In 2002-2003, Australia took 8,146 refugees as defined by the 1951 Convention on Refugees in consultation with the UN High Commissioner for Refugees. The others applied through Australian Embassies and High Commissioners abroad under the humanitarian programme provisions. Australia's resettlement programme for refugees provides welfare entitlements not available to other immigrants.

Asylum seekers claiming to be refugees have, however, created a problem. Only 20% of the asylum seekers arriving in Australia between 1990-2002 were recognised as refugees under the 1951 Refugee Convention. The Australian government's compassion led to the granting of 'Temporary Protection Visas' to most asylum seekers. These do not confer refugee status and are temporary in the hope that genuine asylum seekers will return to their home countries when repression lifts. But 'Temporary Protection Visas' unfortunately encouraged people smugglers to see Australia as a 'soft' destination. Hence the introduction of the 'Pacific solution' to prevent those without immigration documents from landing in Australia.

Refugees have, in the main, had to leave their countries because they have attracted the attention of domestic 'security' forces, usually by being active opponents of repressive regimes, or working for liberal and democratic reforms or equal rights for women and minorities. Refugees have not created the illegal immigration and 'forum shopping' problems that are leading to harsh border controls. The refugees who flee repressive governments annually are negligible in relation to the more than 35 million persons, within countries and across national borders, mainly in Africa, displaced as a result of man-made and natural disasters and civil and international wars. Refugees also differ from asylum seekers who are social and economic migrants and so want to emigrate permanently. Many refugees want to return to their home countries when changes of government permit to help to rebuild them.

1.5 Humanitarian Programme Outcomes

Visas Granted 1993-94 to 2002-03



Source: Commonwealth Department of Immigration and Indigenous Affairs, December 2003, unpublished data.

Public Opinion on Immigration

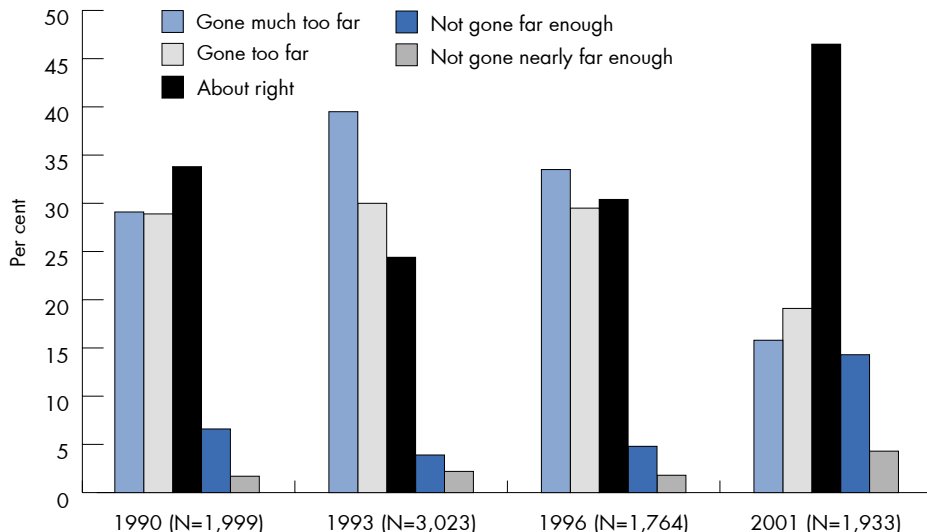
The Australian Election Study is an opinion survey conducted after each Federal election. Questions about immigration and immigrants have increased between 1987-2001. In 1987, 1990 and 1993 there were only one or two questions about immigration. In 1996 there were seven and in 2001 there were 21 questions about immigration, reflecting the prominence of asylum seekers in political debate.

Public attitudes toward immigration have been changing. The graph below shows responses for years in which exactly the same question was asked (in 1987 and 1998 the questions were slightly different). In 1990, only 8% of people thought that immigration levels were not high enough and that Australia should accept more immigrants. The majority (58%) thought that immigration was too high or much too high. In 2001, a larger proportion of people favoured more immigration (18%) and the most frequent response (45%) was that immigration was about right.

With low unemployment rates, support for current levels of immigration is quite high. If low fertility rates and limited immigration persist, slow population growth is likely to result in between 25-27 million people in Australia by 2050. Whether, and in which circumstances, voters would support the substantially higher rates of immigration of some 300,000 and more immigrants a year needed to reach populations of 40 to 50 million by 2050 is moot.

1.6 Public Opinion on Immigration, 1990-2001

Per cent of people surveyed



Source: Australian Social Science Data Archives, *Australian Election Surveys* (Canberra: ANU, 1990, 1993, 1996, 2001).

Summary

The population debate has historically been largely latent in Australia, with little discussion of immigration numbers and the integration of immigrants into Australian society. Changed internal and external circumstances brought population issues to the policy forefront in the 21st century.

After years of struggle, women, like men, can now choose to work and earn an income and save against ill health, unemployment risks and for their old age. They can lead independent lives. At the same time, they can also choose to marry and raise a family and enjoy the pleasure and satisfaction of having children and grandchildren. Adjusting to these changed opportunities is complex and has created many personal and social strains for men and women. It has led to the delay and sometimes forfeit of marriage and family life. The result is reduced fertility.

Even if Australian society considers present (and likely) fertility rates too low, they cannot be raised merely by government policies that support families, important though these are. Men and women have to become aware that a stable family life with children has very high rewards that are worth pursuing even though they also incur personal costs.

An informed immigration debate is equally important. The environmental improvements possible with new technologies must be demonstrated. The economic benefits of immigration and its ability to provide strategic economies of scale are powerful. Even present levels of immigration depend on healthy economic performance that creates jobs and on open industrial relations that enable them to be filled.

Australia's non-discriminatory 'points' selection for immigrants is much more transparent than the immigration procedures of most other countries. But post-migration policies that integrate newcomers into Australian society are less clear though they are essential to the maintenance of present levels and potential increases in the migrant intake. Australians, including recent newcomers, want to preserve the qualities that have made Australia not only a materially prosperous, but also a pleasant, civilised country in which to live.

2. FAMILY, MARRIAGE & FERTILITY

BARRY MALEY

Introduction

There is wide agreement that the family—understood as mother, father, children, and close relatives—is the institutional foundation for social and cultural renewal and continuity. It is arguably the most important contributor to the growth of the ‘human capital’ of a nation’s children. A family is an economic unit in its own right, with substantial division of labour yielding welfare benefits for its members. It is within family life that some of our most important social and emotional needs are met, and some of our most satisfying fulfilments achieved and recognised.

To carry out their functions, families need to hold together over several years so that children can be adequately cared for, socialised, educated, and raised to maturity. Marriage is the institution that has arisen to establish a degree of durability and predictability while these tasks are carried out.

As the centre of reproduction, the family’s vigour and steadiness are crucial in creating a safe and dependable environment within which women and men may have children to sustain or increase the nation’s population. A society and its culture will eventually fade away if its birth rate stays below an average of about 2.1 children per woman. Massive immigration may slow this process, but it will not halt it. As its age structure steadily moves towards an overwhelming preponderance of aged people incapable of sustained work and self-support (see Figure 7.1, p.80), recovery becomes ever more difficult, and, finally, impossible. The future of the nation is therefore inseparable from the strength of the family and its fertility.

The Australian family has grown weaker on a number of measures and its changing structure, or ‘diversity’ as it is euphemistically put, is part of the evidence. Marriages are more fragile than ever before, and more and more children are being born outside a marital relationship. Fertility has fallen to its lowest recorded level. The consequences are adult and child unhappiness and reduced wellbeing, more social disorder arising from more poorly socialised children, and the prospect of a diminishing population over the long term. Recovery requires a range of reforms without which the downward spiral and its consequences will continue.

Fertility

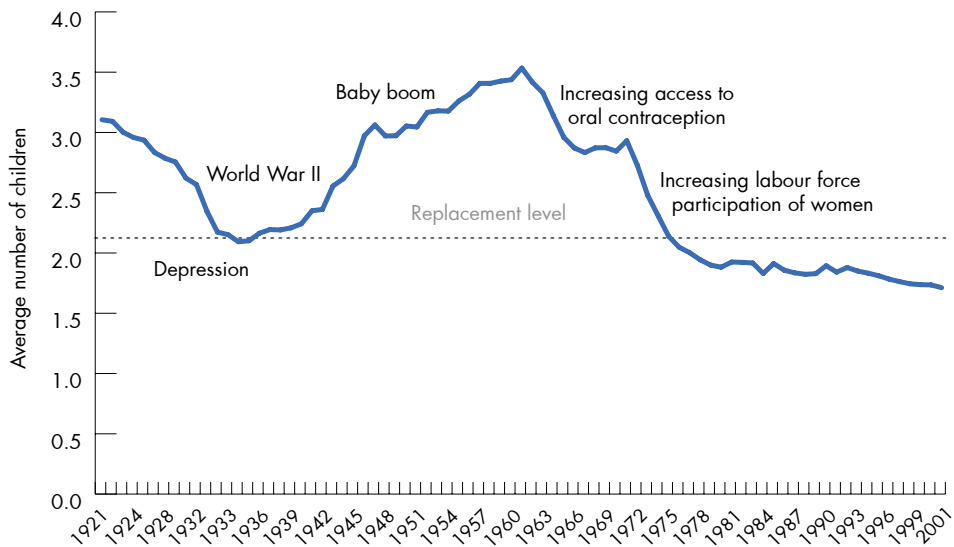
Australia's fertility rate has fluctuated over the last 80 years in statistical association with a variety of social, economic and cultural changes, but proving causal connections and giving weight to the various factors which influence fertility is very difficult.

We are dealing with a complex and interacting configuration of factors varying in salience over time. Figure 2.1 below gives a broad summary of some of these connections. For example, it seems fairly clear that the severe economic depression of the 1930s (when unemployment affected 25% or more of the workforce) lowered birth rates. But it is less plausible that the increasing labour force participation of women in the 1980s and 1990s is the major cause of the falling birth rate over that time. Many other possible factors—such as the declining value of family taxation concessions and allowances—have changed over the same period.

Figure 2.1 shows the 'replacement level', or the birth rate of 2.1 children per woman, below which the population will eventually begin to fall in the absence of substantial and continuing immigration.

2.1 Fertility of Women, 1921-2001

Average number of children in a lifetime

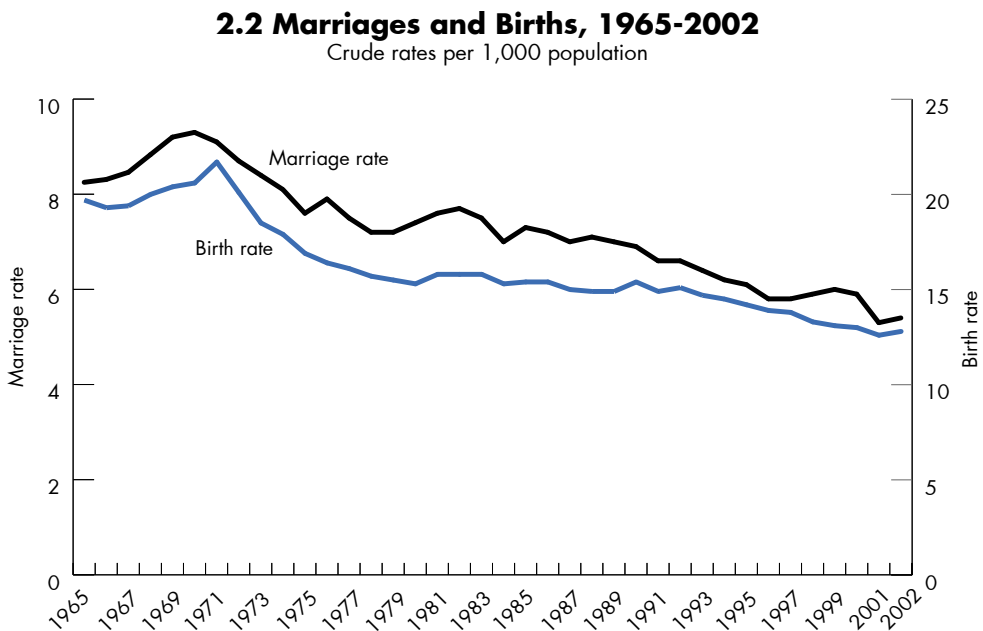


Source: ABS figures, but presentation adopted from *Family Matters* 63 (Spring/Summer 2002), 15.

Marriage and Fertility

The great majority of children are born within marriage. It seems that couples value marriage as a more secure environment within which to undertake the long-term responsibility of having and rearing children. That being so, if men and women significantly delay marriage, the 'window of opportunity' within which they may have children contracts and, other things being equal, the birth rate would be affected.

The marriage rate is falling in lock-step with the birth rate, as shown in Figure 2.2. The correlation coefficient between the two is .95. This does not necessarily indicate a causal connection since each may be an effect of other causes. For example, many more married women nowadays face a choice between having children and giving up a valued job and its income. This raises the 'opportunity costs' of children. Also, concessions in the tax system for children have decreased significantly over the last 30 years and existing allowances are means-tested and begin to cut out at comparatively low levels of family income, further raising the costs of children. This provides an incentive for mothers to work to support any children they might have but would tend to discourage having more children.



Sources: ABS, *Marriages and Divorces*, Cat. 3310.0; *Births*, Cat. 3301.0 (Canberra: ABS, various years).

Divorce and Fertility

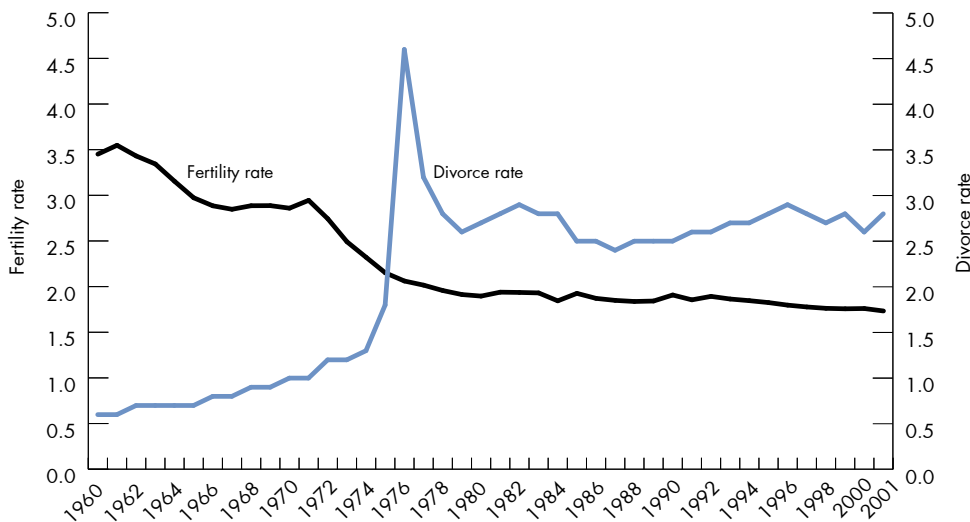
The divorce rate has quadrupled in the last 40 years. A major legal change, the advent of no-fault divorce via the Family Law Act 1975, made it easier and quicker to end a marriage and removed the previous requirement to prove serious marital misconduct, or ‘fault’, as a condition of a divorce settlement. A marriage under the new rules could be ended by one year’s separation of the spouses. There was an immediate and massive rise in the divorce rate between 1976-1977 as spouses ‘waiting’ to divorce rushed to take advantage of the new rules.

Marriage is now a much more uncertain enterprise than it used to be, and a married woman is vulnerable to suddenly finding herself facing divorce and relative impoverishment after divorce, particularly if she has sacrificed work opportunities to raise children. Women might think twice about having children, or at least reduce the number of children they might otherwise have had. If a woman is divorced while still in her reproductive years, in most cases her post-divorce circumstances will strongly militate against her having an additional or first child.

Theoretically, we might predict that a society with an increasing divorce rate will tend to have a decreasing fertility rate. Figure 2.3 shows a close statistical connection between an increasing divorce rate and a decreasing fertility rate from 1960-2001. The correlation coefficient is .89, significant at the $p < 0.01$ level. But as suggested in relation to fertility and marriage rates (see Figure 2.2), we are dealing with a complex interaction of factors, and weighing their relative importance and the causal paths between them is very difficult.

2.3 Divorce and Fertility, 1960-2001

Crude divorce rate per 1,000 population
Total fertility rate per woman



Sources: ABS, *Marriages and Divorces*, Cat. 3310.0; *Births*, Cat. 3301.0 (Canberra: ABS, various years).

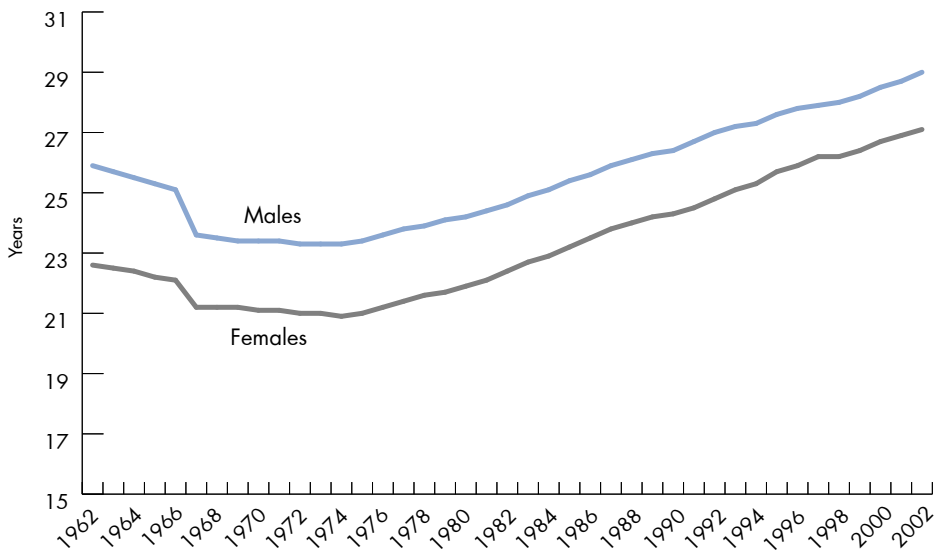
Age at Marriage

Age at marriage for both men and women has risen continually over the last 20 years. In 1970 the median age at first marriage was 23 for men and 21 for women. In 2002 it was 29 for men and 27 for women. This is higher than ages at marriage at the beginning of the 20th century.

The Australian Bureau of Statistics estimates, on the basis of present trends, that 29% of men and 23% of women will never marry.¹ These figures represent increases of about 35% and 65% respectively in the space of just 12 years.

Overall, these trends indicate a major social change in the status of marriage and attitudes towards it.

2.4 Median Age at First Marriage, 1962-2002



Sources: ABS, *Marriages and Divorces*, Cat. 3310.0; *Marriages*, Cat. 3306.0 (Canberra: ABS, 2002).

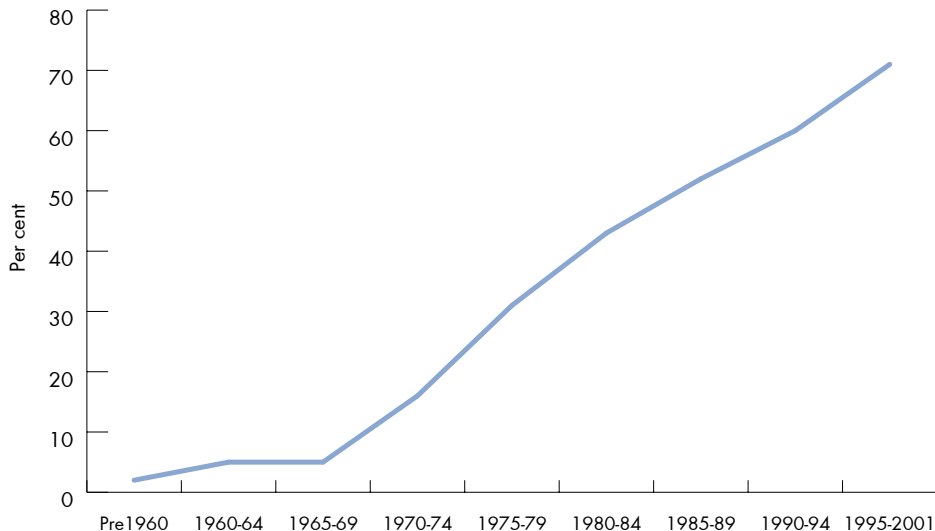
Cohabitation and De Facto Relationships

‘Cohabitation’ and ‘de facto relationship’ are virtually interchangeable terms referring to couples living together; except that ‘de facto’ has the connotation of a ‘marriage-like’ relationship in the absence of formal or registered marriage.

‘Living together’, or cohabitation, by unmarried couples was frowned upon as immoral and reprehensible until the 1960s and 1970s. From then on, as the ‘sexual revolution’ gathered force, it rapidly became acceptable. Today it is almost routine for a great many young (and sometimes older) men and women to cohabit before marriage, or to extend the period of cohabitation indefinitely as a substitute for marriage.

De facto couples now comprise more than 12% of all couple families.²

2.5 Proportion of First Marriages Preceded by Cohabitation, Pre 1960-2001



Source: Household Income and Labour Dynamics in Australia Survey 2001 taken from ‘Premarital Cohabitation and Subsequent Marital Stability’, *Family Matters* 65 (Winter 2003), 35.

Cohabitation and Marital Stability

As the rate of cohabitation before marriage began to rise in the 1970s, one of the justifications offered was that pre-marital cohabitation would lead to stronger marriages. A couple would get to know each other better before taking the serious step to marriage, discover points of incompatibility, and end a relationship that might otherwise have finished in divorce.

By the 1990s evidence had accumulated to suggest that this sanguine view was misplaced, and that divorce rates were higher among pre-marital cohabiters than among those who had not cohabited before marriage.

This conclusion has been challenged recently by researchers at the Australian Institute of Family Studies.³ They hypothesised that couples who cohabited before it became widely acceptable were more unconventional and had backgrounds and values that increased their chances of divorcing. However, as cohabitation has become more normal, cohabiting couples are attitudinally more diverse and no longer share characteristics that may lead them to more unstable marriages. Also, since separation or divorce becomes more likely the longer a couple is together, those who had first cohabited then married were together for longer periods and more likely to show higher rates of divorce/separation than those married couples who had not cohabited.

The study results suggested that the survival rate of marriages preceded by cohabitation is poorer than for marriages of non-cohabiting couples, but the difference has become smaller as pre-marital cohabitation has become normal. If one measures the period of 'union' (that is, cohabitation plus marriage), rather than the period of marriage alone, the difference narrows further. Difficulties of measurement and control of variables has made firm conclusions unattainable.

2.6 Proportion of Couples Divorcing Within 5, 10, 20 Years of Marriage

	<i>Within 5 years</i>	<i>Within 10 years</i>	<i>Within 20 years</i>
Cohabiting	13%	26%	56%
Non-cohabiting	6%	14%	27%

Source: Commonwealth of Australia, *To Have And To Hold*, House of Representatives Standing Committee on Legal and Constitutional Affairs (June 1998).

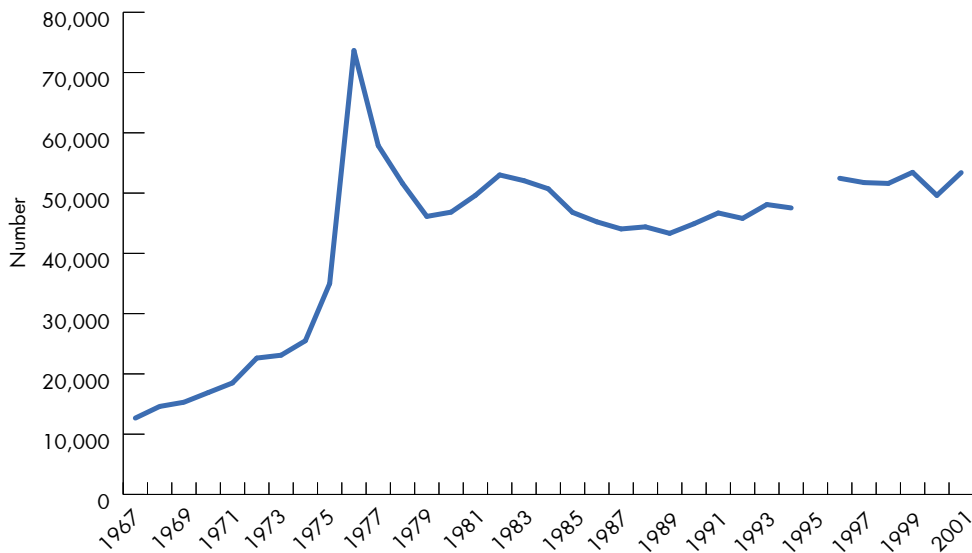
Children and Divorce

If there is a causal connection, as there seems to be, between the stability of the bond between natural parents and the wellbeing of their children, then divorce and separation are threats to that wellbeing.⁴

As the divorce rate has risen (see Figure 2.3), so has the number of children affected by divorce. In 2001, there were 55,330 divorces involving 53,396 children. To this must be added the children affected by the separation of their cohabiting, unmarried parents.

Almost 30% of dependent children are separated from one of their natural parents, and divorce is the reason in about two-thirds of these cases. In about 90% of cases, it is the father who is living elsewhere. Recent research has confirmed what common sense suggests—that father-absence is, on average, associated with emotional loss and behavioural problems of children.⁵

2.7 Children and Divorce, 1967-2001
Annual number of children (0-17years) whose parents divorced*



*1995 figure not available

Sources: ABS, *Yearbook Australia*, Cat.1301.0; *Marriages and Divorces*, Cat. 3310.0 (Canberra: ABS, various years).

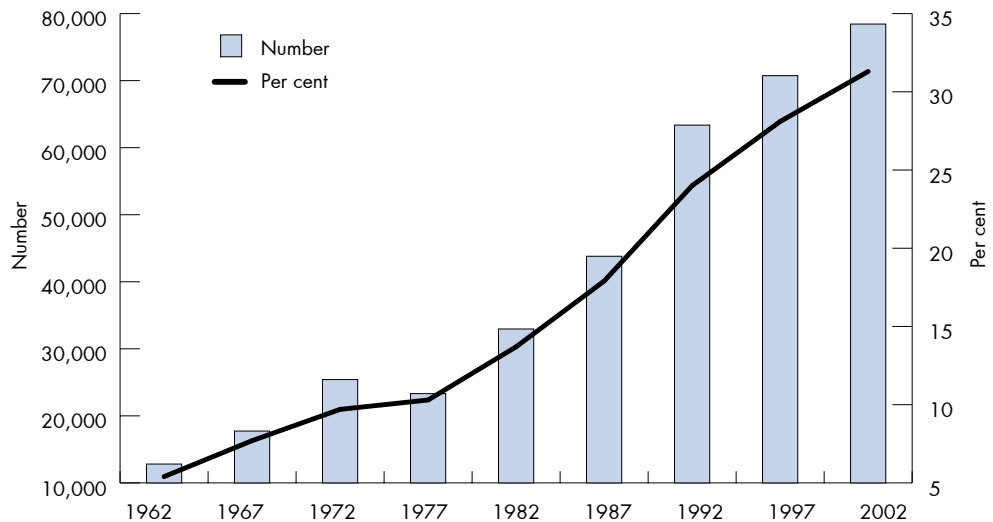
Ex-nuptial Births and Paternity

For the first 50 years of the 20th century ex-nuptial births averaged about 5% of all births. In 2002 there were 78,438 ex-nuptial births, constituting a fraction over 30% of all births. Given the availability of effective, inexpensive, convenient, and reliable contraception, it would appear that in the great majority of cases, having a child out of wedlock is a conscious, voluntary decision. This reflects the normalisation of unmarried cohabitation and the disappearance of the former stigma attached to unmarried motherhood.

Since almost 90% of fathers acknowledge their paternity on the birth certificate of children born ex-nuptially,⁶ it is clear that many of the parents of these children are in cohabiting/de facto relationships.

2.8 Ex-nuptial Births, 1962-2002

Number and proportion of all births



Source: ABS, *Births Australia*, Cat. 3310.0 (Canberra: ABS, various years).

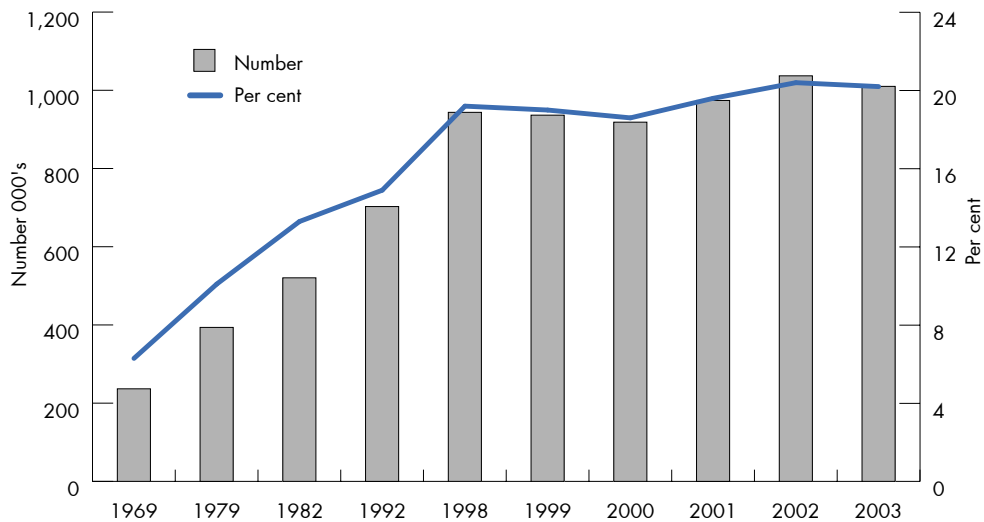
Children in Single Parent Families

As one would expect, the increase in divorce and separation and the legitimization of unmarried motherhood have combined to raise very rapidly the percentage and absolute numbers of children living with a single parent (usually the mother). The availability of adequate government support for single parents since the 1970s has lessened the disincentives to single parenthood and made it more viable than used to be the case.

Divorce or separation are responsible for about two-thirds of single parent families. Never-married single parents constitute about 30% of all single parents.

2.9 Dependent Children in Single Parent Families, 1969-2003

Children aged 0-14 years and full-time students aged 15-24 years



Source: ABS, *Labour Force Status and Other Characteristics of Families*, Cat. 6224.0 (Canberra: ABS, various years).

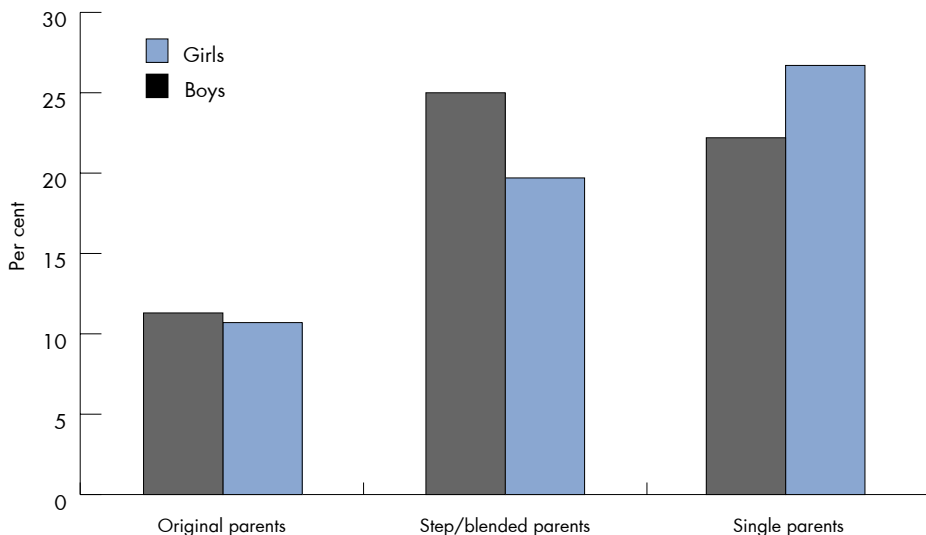
Changing Family Structure and Child Wellbeing

There is a significant statistical relationship between the type of family in which a child is raised and the child's wellbeing. Children can be well raised by a parent or parents in difficult circumstances, but across a large population there are noticeable variations in child wellbeing as family structure changes. On average, children raised to maturity by their married, natural parents fare better on a number of measures. A very large body of research on the connections between family structure and child wellbeing has concluded that children in sole parent and step/blended families are, on average, at greatest risk of mental health and behavioural problems, are more likely to be abused and neglected, and are more likely to underperform educationally.⁷

From the 1970s until the present, the percentage of children raised by their married natural parents has been declining. This is an entrenched trend reflecting major social, cultural, legal, and economic changes. Combining with and reinforcing each other, such developments have led to what seems to be a permanent change in the frequency of family types other than married natural parents and their children.

2.10 Children With Mental Health Problems by Family Type, 1998

Per cent of boys and girls in each family type



Source: M.G. Sawyer, et al., *The Mental Health of Young People in Australia* (Canberra: AGPS, 2000).

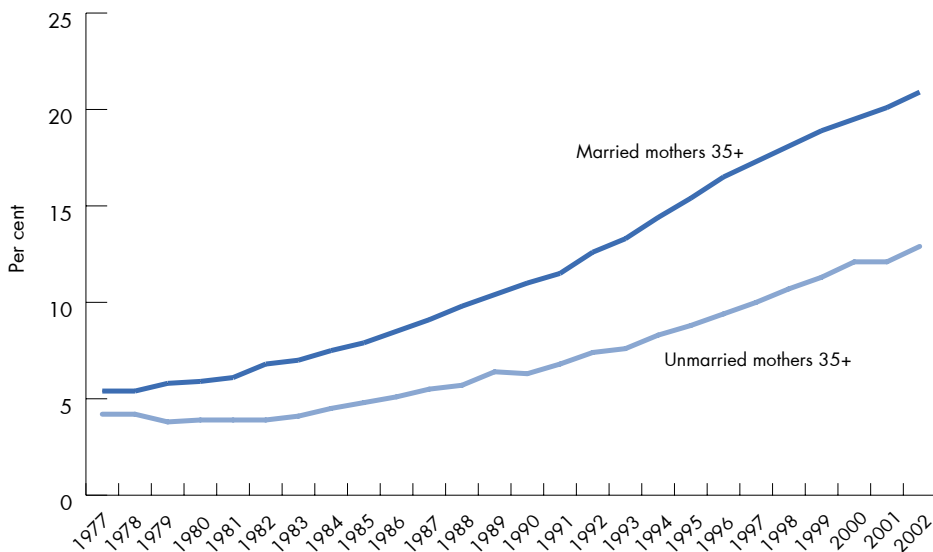
Older Mothers

As marriage and parenting for both men and women is delayed, the percentage of older mothers, both married and unmarried, has grown steadily. Since unmarried mothers tend to give birth at younger ages than married mothers, the percentage of unmarried mothers having children when more than age 35 is lower than the percentage of married mothers over 35.

Overall, the trend towards delaying parenthood brings more and more women into older age groups where being able to conceive a child becomes more difficult, which is likely to be a factor in declining fertility.

2.11 Mothers Aged 35 Years or Over, 1977-2002

Proportion of nuptial and ex-nuptial pregnancies



Source: ABS, *Births Australia*, Cat. 3310.0 (Canberra: ABS, various years).

Working Mothers

One of the outstanding facts of family life is the high proportion of mothers of dependent children in couple families who are working part-time or full-time (35 hours or more per week).

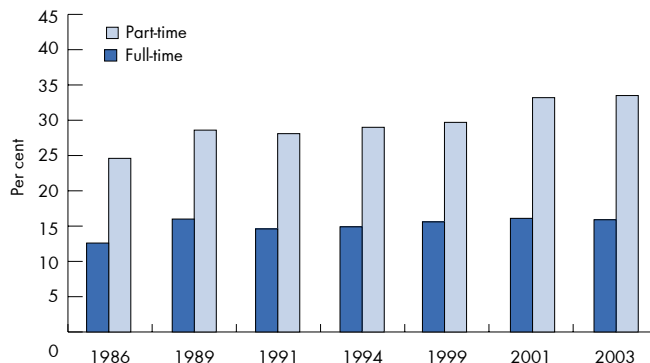
In general, mothers with dependent children increase their workforce participation as their children get older. This is apparent from the two figures below.

As we might expect, mothers with school age children (5-14 years) are more strongly represented in the workforce than mothers of pre-school age children. At the present time, 70% of mothers of school age children are in the workforce, mostly part-time.

The pattern of work force participation by mothers in couple families with pre-school children is rather different. For this group of mothers, about half of them are not in the workforce at all, and about one-third work part-time. This suggests that the great majority of mothers with pre-school children are living a traditional or 'semi-traditional' (division between a paid job and domesticity) way of life.

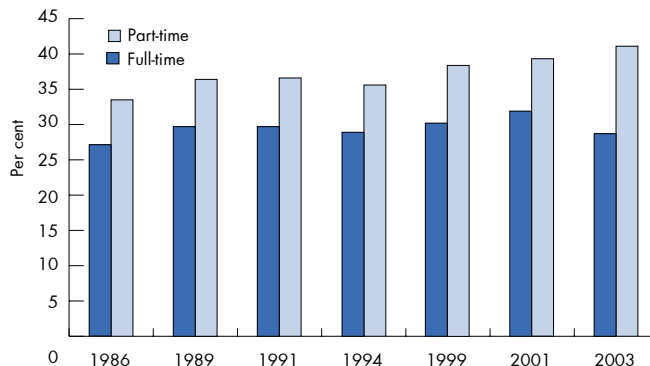
2.12a Working Mothers of 0-4 Year Olds, 1986-2003

per cent of mothers in couple families working full-time or part-time



2.12b Working Mothers of 5-14 Year Olds, 1986-2003

Per cent of mothers in couple families working full-time or part-time



Source: ABS, *Labour Force Status and Other Characteristics of Families*, Cat. 6224.0 (Canberra: ABS, various years).

Families With Dependent Children and No Parent Employed

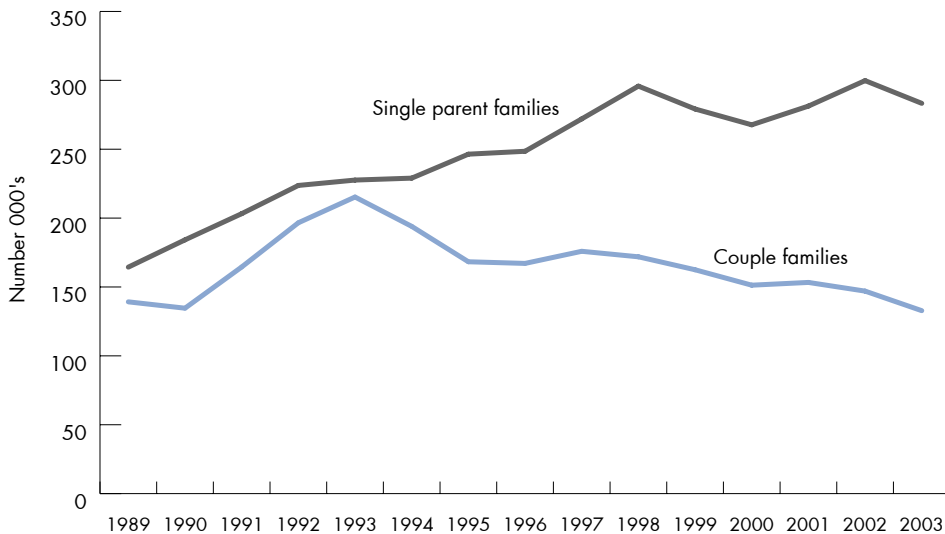
A large part of the cost of welfare is support for families where no parent is employed, whether in a couple family or a single parent family, and whether looking for work or not looking for work (see Figure 7.6, p.85).

Apart from the difficulties faced by unemployed families and their children, the model of unemployed and perhaps demoralised adulthood, especially for extended periods, is not ideal for children.

For couple families, unemployment rose towards the peak of the recession in the early 1990s and has declined steadily since. For single parents, unemployment has risen relentlessly until 1998, reaching a plateau from then until the present.

2.13 Families With No Parent Employed, 1989-2003

Couple families and single parent families with dependent children



Sources: ABS, *Labour Force Status and Other Characteristics of Families*, Cat. 6224.0; *Labour Force Australia*, Cat. 6291.0.55.001 (Canberra: ABS, various years).

Summary

The Australian family has changed dramatically over the last 30 to 40 years, from when the overwhelming family type was the 'traditional' unit of formally married mother and father and their natural children, to far more mixed families, where approximately one-third of families are either single parent or step and blended families. High rates of divorce, separation of couples, and a growing retreat from marriage lie behind this transformation. It has been attended by significant deterioration in the wellbeing of many adults and children. Australian society will be less vigorous, stable and prosperous so long as the family falters in the performance of its unique and indispensable functions.

A variety of social, legal, cultural and economic changes have contributed to this deterioration. Family taxation is too high, largely because working families are carrying the tax burden of a welfare state that has been greatly extended because of changes in family structure. Divorce law changes in 1975 removed some former disincentives to divorce and separation while creating incentives for spouses to exploit each other through easy, unilateral divorce. Relatively generous support for single parent families has removed a deterrent to unmarried motherhood and separation of couples. Entrenched unemployment has made many young men unmarriageable.

Restoring the strength of the family system is an immense and varied task. There are two points of attack which promise readily attainable improvements. The first is reform of the family tax system by providing greater recognition and compensation for the greatly increased costs of children, either in the form of taxation concessions or allowances. The second is changes in divorce law to remove unilateralism—the opportunity for one spouse to impose a divorce on another—and, further, to establish the opportunity for proven serious misconduct in marriage to be raised as an issue in divorce settlements. Such changes would strengthen the family's financial position and help stabilise marriages.

3. CIVIL SOCIETY

CASPAR CONDE

Introduction

Societies function best when there are high levels of social order and cohesion. That is, when each member feels encouraged and empowered to participate in, and contribute to, their given society and its greater good.

Three important indicators of social order and cohesion are crime, litigiousness and social capital. Taken together, they provide an insight into levels of personal responsibility and respect for civic bodies and institutions.

Despite a recent decrease, the rate of serious crime in Australia increased sevenfold in the last 40 years. This is due primarily to increases in common and sexual assault, but also to the other elements constituting serious crime—homicide offences, robbery, burglary and motor vehicle theft. Similar trends exist in the United Kingdom but not in the United States. America has managed to curtail dramatic rises in serious crime through greater police numbers and increased imprisonment. Thus those who seek to undermine social order through crime face the twin disincentives of detection and incarceration.

Litigiousness goes to the core issue of personal responsibility. Everyone ought to feel entitled to pursue claims for restitution, but abuse of those processes reflects a disregard for the larger needs of society and may contribute to crises such as those seen recently in the insurance industry. The increasing litigiousness of the United States is well documented, but that of Australia is less so. Despite fears that Australia may be starting to mirror the United States, there are structural and statistical differences to note.

Social capital is an emerging field of analysis and is difficult to quantify. Studies indicate that high levels of social capital tend to generate greater economic and social wellbeing. Australia's social capital is at an average level by international standards, and is comparable to countries that are politically and economically similar.

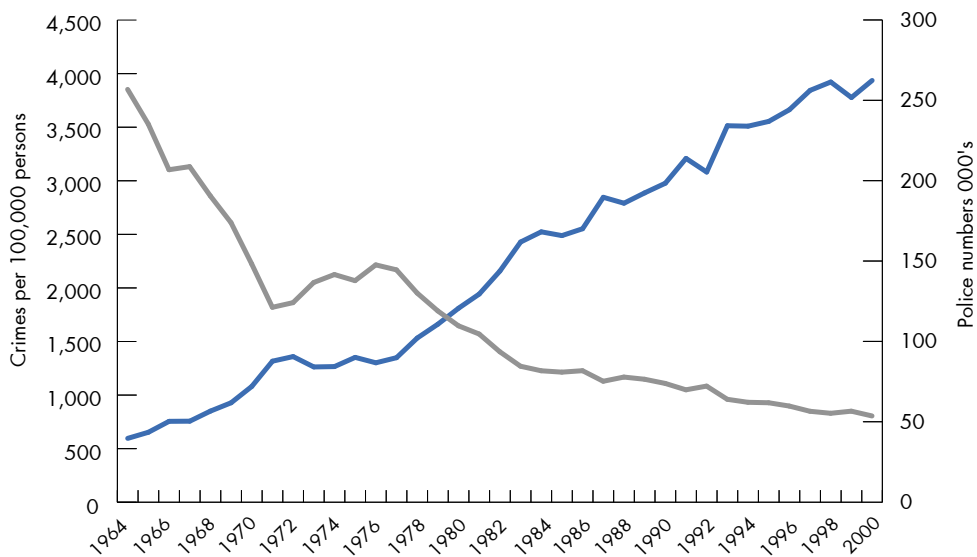
Serious Crime and Police Numbers

It seems straightforward that the more resources given to law enforcement officers, the more the law will be enforced. There are other considerations such as bureaucratic efficiency, changes in technology and the effectiveness of techniques used in fighting crime. However, at a general level, an inverse relationship is observed between increases and decreases in police numbers and the rate of serious crime.

The graph below compares serious crime on a per capita basis with police numbers per 1,000 serious crimes.

Raising police numbers increases the likelihood of detection, and incarceration has the twofold effect of acting as a disincentive to prospective criminals and removing those who have offended, often repeatedly, from society. Figures illustrating the relationship between serious crime and prisoners are in later pages.

3.1 Police Numbers and Serious Crime, 1964-2000



Police Source: ABS, *Year Book Australia* (Canberra: ABS, various years).

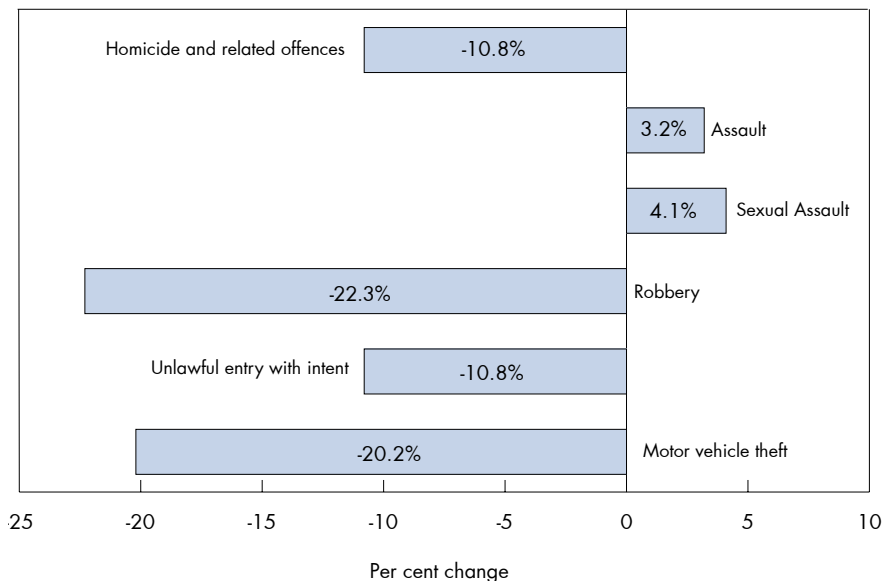
Crime Sources: AIC *Sourcebook*, NSW Recorded Crime, Victoria Police *Crime Statistics*, Crime and Justice in SA, Queensland Police *Statistical Review*, ABS *Year Book Queensland*, Western Australia Police Service Statistics, ABS *Year Book Western Australia*, Tasmania Police *Annual Reports*, AFP *Annual Reports*, NT Police *Annual Reports* (for full Statistical Sources, see p.157).

Recent Serious Crime in Australia

A recent Australian Bureau of Statistics publication reported an overall decline in serious crime in Australia between 2001 and 2002. Homicide and related offences dropped 11%; robbery fell by 22%; unlawful entry with intent by 11%; and motor vehicle theft by 20%. There were small increases in the rates of assault and sexual assault, of 3% and 4% respectively.

This contrasts with the trend over the last 40 years in Australia of rising crime, as seen in Figure 3.1 (opposite). Comparable and recent data to help explain this fall is as yet unavailable, however analysis of such statistics over previous decades suggests that the observed fall in 2002 is due to increases in police officers and/or prisoners. A study by the NSW Bureau of Crime Statistics and Research also showed a link between the availability of heroin and robbery. A recent drop in heroin availability has corresponded with the decrease in robbery as shown below.¹

3.2 Change in Serious Crime Rate Per 100,000 Persons, 2001-2002



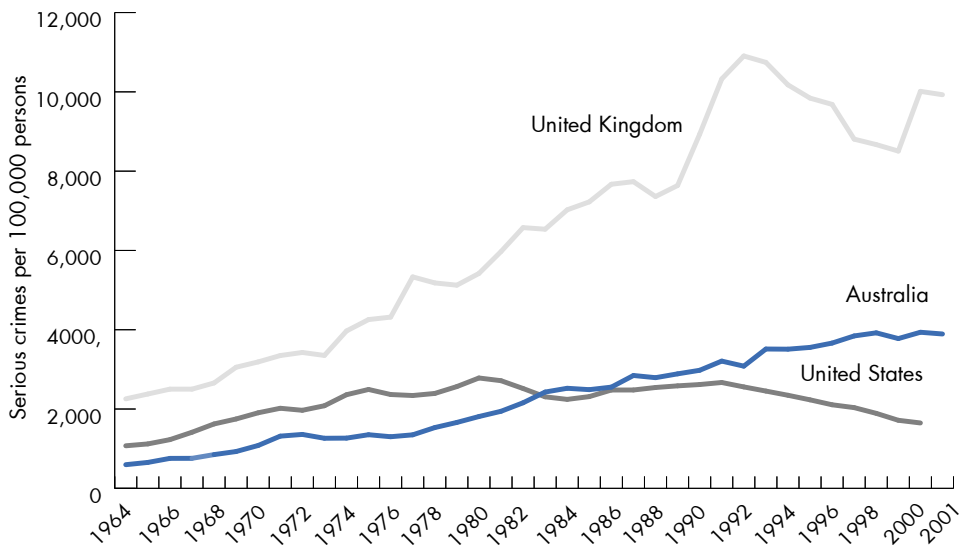
Source: ABS, *Recorded Crime, Australia*, Cat. 4510 (Canberra: ABS, 2003).

Serious Crime Over Time: Australia, US and UK

Since the 1960s, despite the aforementioned recent improvements, serious crime in Australia (taking account of population growth) has increased sevenfold. This seems to have been led by increases in common and sexual assault offences, which continue to rise today, along with motor vehicle theft. In England and Wales the increase in the serious crime rate over the last 40 years is fourfold. In the United States, however, the serious crime rate has been arrested and is back to only one and a half times its level in the 1960s.

Why has the United States been so successful in reducing serious crime rates? It is often suggested that this is the result of factors external to direct, crime-fighting policies, such as economic growth and the corresponding rise in employment opportunities. Were this completely true, both Australia and the United Kingdom would expect to have seen similar results. Two reasons are posited for the United States' success. The first is increased imprisonment, and the second is the implementation of 'Broken Windows' policing, as advocated by George Kelling and as seen in New York under Mayor Rudolph Giuliani. The theory argues that minor disorders left unchecked (such as a broken window) pave the way for more serious crimes to occur.

3.3 Serious Crime Rates, Australia, US and UK, 1964-2001



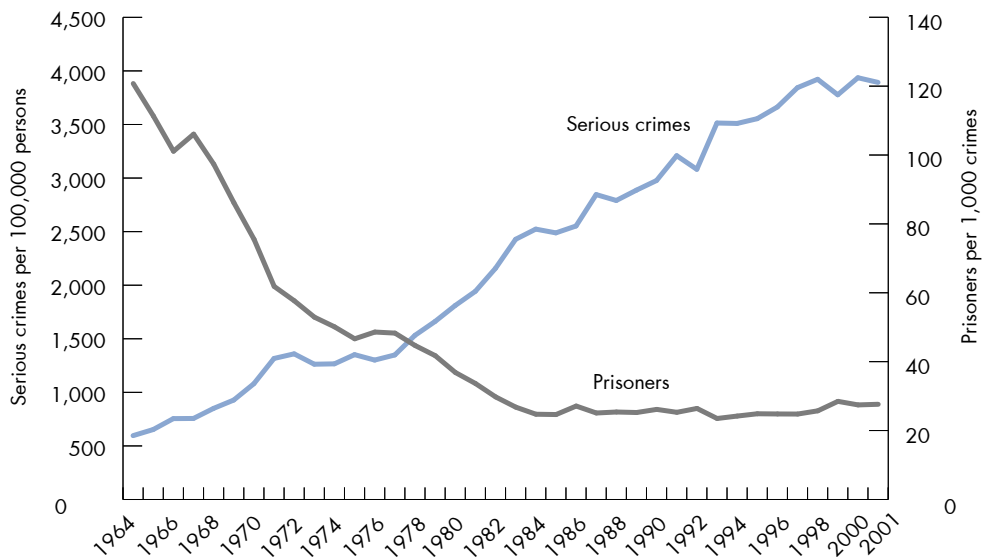
Sources for Figure 3.3, 3.4a, 3.4b, 3.4c: ABS, *National Crime Statistics*, Cat. 4510; *Corrective Services*, Cat. 4512; *Population: Time Series Spreadsheet*, Cat. 3201; *Yearbook*, Cat. 1301 (Canberra: ABS, various years); ABS *National Correction Statistics*, Cat. 4512 (Canberra: ABS, 1996); AIC *Australian Prison Trends* (Canberra: AIC, various years); S. Mukherjee et al., *Source Book of Australia: Criminal and Social Statistics 1804-1988* (Canberra: Australian Institute of Criminology, 1989); J. Walker, 'Trends in Crime and Criminal Justice' in (cont'd next page)

Serious Crime and Imprisonment: Australia, US and UK

The increased imprisonment rates in the United States have corresponded with a decrease in serious crime rates. Observing this relationship, an article in *Policy* magazine, *Does Prison Work?*² compared prison population figures with serious crime rates in the United Kingdom, the United States and Australia.

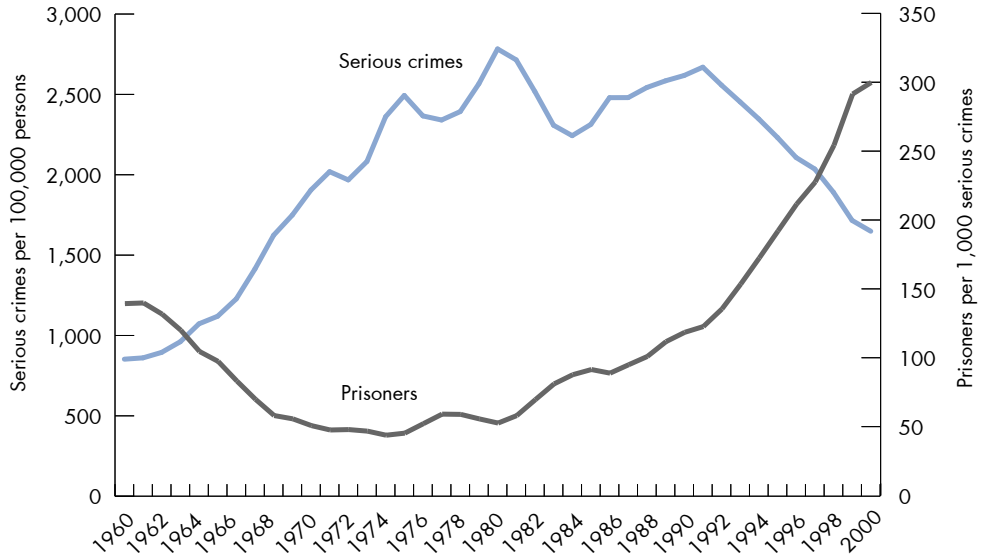
For all three countries an inverse relationship was found between numbers in incarceration and rates of serious crime. Whilst it is important to be wary of making conclusions based on a simple correlation, the below trends are consistent over four decades. It is arguable that such a sustained correlation does indicate effectiveness. Gaol serves to reduce crime by removing offenders from society and also by deterring potential criminals from offending in the first place.

3.4a Australia, 1964-2001

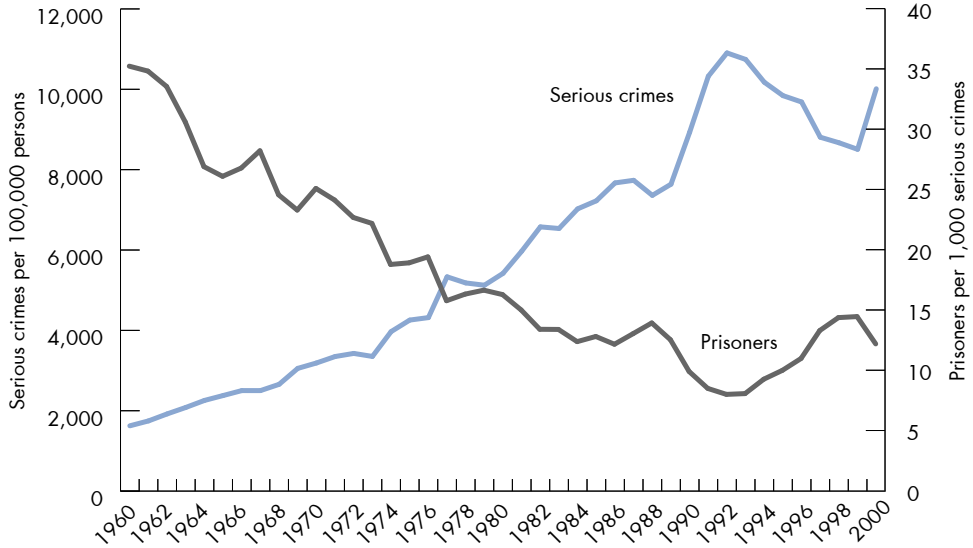


(Sources cont'd) D. Chappell and P. Wilson (eds), *The Australian Criminal Justice System: The Mid 1990s* (Sydney: Butterworths, 1994); Home Office, www.homeoffice.gov.uk (London: Her Majesty's Stationery Office, various years); Census Bureau, Population estimates, www.census.gov (Washington: Census Bureau, various years); Department of Justice, Bureau of Justice statistics online, www.ojp.usdoj.gov/bjs (Washington: Department of Justice, various years).

3.4b United States, 1960-2000



3.4c United Kingdom, 1960-2000



Sources: see p.34-35.

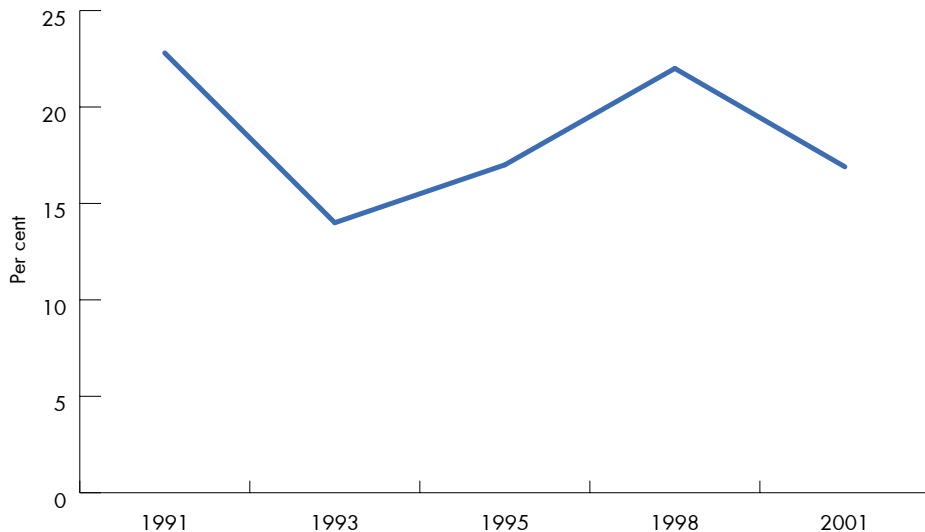
Illicit Drugs

A February 2003 report from the Australian Institute of Health and Welfare found that between the years 1991 and 2001, the use of illicit drugs in Australia by those aged over 14 years decreased by 26%. However, this was not a steady decline, with the proportion of illicit drug users fluctuating between 14% and 22% before settling to 17% in 2001. The graph below charts illicit drug use as a proportion of the population.

Since illicit drug use is a crime, data on the number of users is inherently unreliable. Even if guaranteed anonymity, people will be reluctant to admit to breaking the law. Those already in gaol may be more forthcoming. The report found that 70.4% of male prisoners had used an illicit drug in the six months prior to their arrest; 43.5% of male prisoners reported ongoing addiction; and 36.4% of those incarcerated for violent offences reported addiction.

3.5 Illicit Drug Use, Australia, 1991-2001

Per cent of people who used illicit drugs in the last 12 months



Source: Australian Institute of Health and Welfare, *Statistics on Drug Use in Australia 2002* (Canberra: AIHW, 2003).

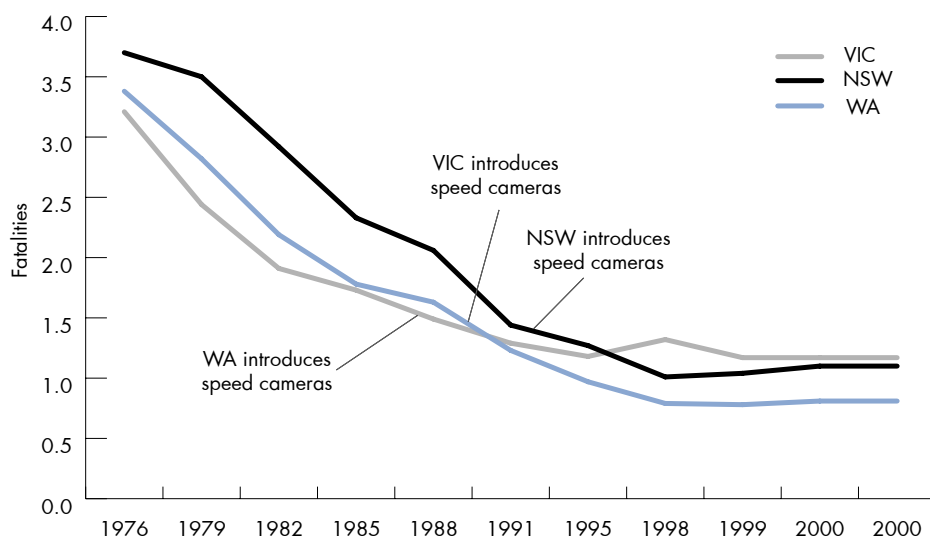
Speed Cameras Are No Substitute for Policing

Speed cameras are a perennial source of irritation for motorists but are justified by regulators on two grounds: that they save lives and save money. However, this claim is called into question by the associated statistics.

Figure 3.6 compares the number of fatalities per 100 million kilometres travelled in New South Wales, Victoria and Western Australia. A broad reduction in fatalities can be observed across the three states, despite the fact that cameras were introduced in different years. New South Wales in particular saw a major reduction in fatalities, even though it employed speed cameras comparatively late in the time period examined. Other factors such as improvements in car safety, road surfaces, increased driver awareness and anti-drink driving policies may all be greater contributors to the observed overall fall in deaths on Australian roads.

It is claimed that speed cameras free police resources for other purposes. Yet this neglects other important aspects of policing the roads. Speed cameras only measure how fast a vehicle is travelling, not whether it is being driven dangerously, under the influence of alcohol, or by an unlicensed driver. The 'Broken Windows' principle (see p.34) would further suggest that people driving in such a manner may be guilty of other more serious offences. Fewer police on the roads means such people are less likely to be caught.

3.6 Fatalities Per 100 Million Km Travelled, 1976-2000



Sources: Australian Transport Safety Bureau (ATSB), *Road Fatalities Australia: Statistical Summary* (Canberra: ATSB, 2002); ATSB, *Road Fatalities Australia: Monthly Bulletin* (Canberra: ATSB, June 2003).

Litigiousness

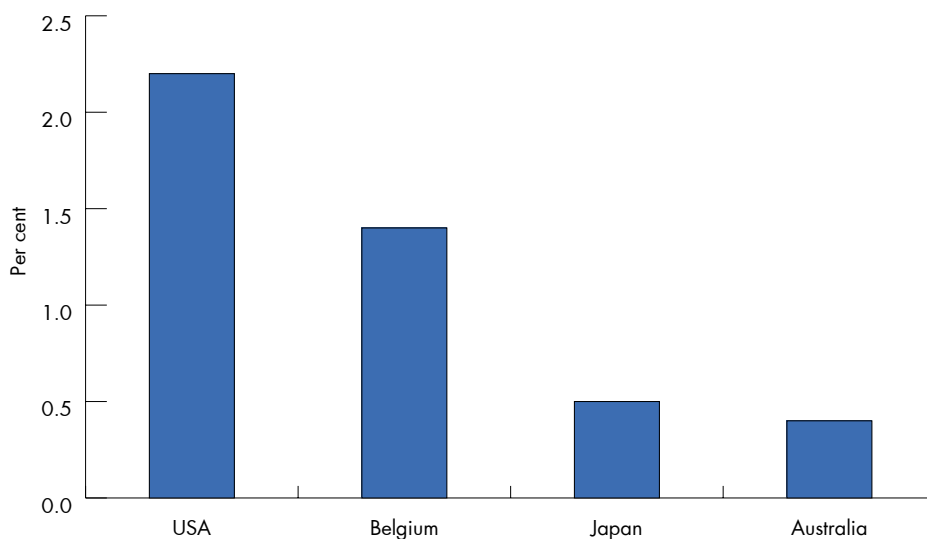
In July 2003 the High Court of Australia ruled a doctor was liable for the expenses of rearing an unwanted child to the age of 18 in the case of *Cattanach v Melchior*.³ Dr. Cattanach was found negligent in his advice and failure to warn after a sterilisation procedure he performed failed. Setting aside other objections, the case raises broader questions as to the litigious nature of Australian society and whether it may be following trends seen abroad. In the United States, for example, the cost of litigation over the last 50 years has increased by more than 100 times.⁴

Australian policymakers need not panic just yet. There are important structural and numeric differences that would encourage speculative litigation in the United States that are not found in Australia. Firstly, civil jury trials prevail in the United States, whereas in Australia the cases will often be heard by a solitary judge; secondly, in the United States the losing party is not responsible for the legal fees and costs of the winner; and thirdly American law puts no limits on contingency fees.

It is difficult to obtain statistical evidence for the Australian tort system. In 2002 the Commonwealth Government commissioned the Ipp report on negligence, which wrote of a 'dearth of hard evidence' surrounding the law of tort and thus the authors resorted to their 'collective sense of fairness' when making policy recommendations.⁵ A study by Tillinghast has Australia performing strongly in the international sphere of tort law. Figure 3.7 shows the United States and Belgium had the largest tort cost as a percentage of GNP and the Japan and Australia had the smallest tort cost.

3.7 Tort Cost in Selected Countries, 1995

As a percentage of GNP



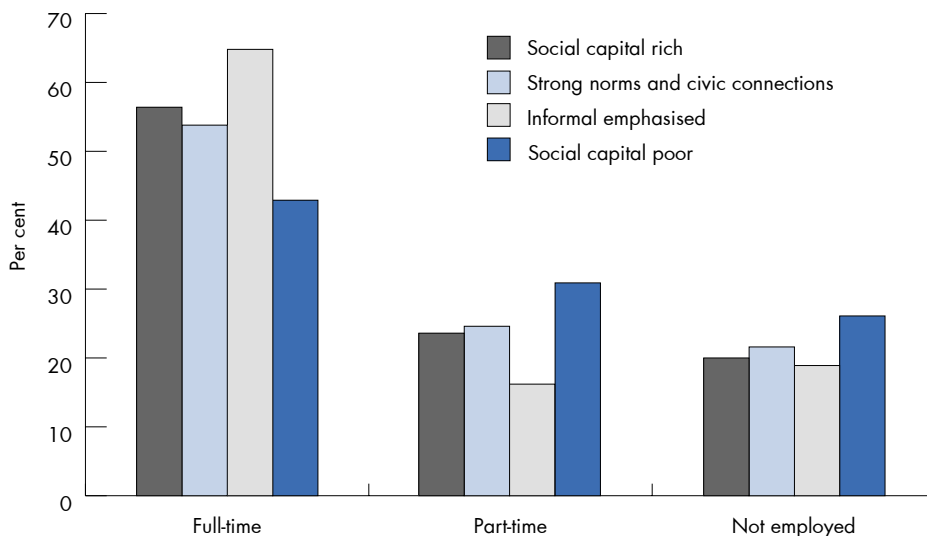
Source: Tillinghast-Towers Perrin, *Tort Cost Trends: An International Perspective*, 3rd ed, (New York: Tillinghast-Towers Perrin, 1995), 14, 16.

Social Capital in Australia

Social capital can be defined as ‘networks of social relations which are characterised by norms of trust and reciprocity and which lead to outcomes of mutual benefit’.⁶ It is ‘not simply the sum of institutions which underpin society, it is also the glue that holds them together’.⁷ An enhancement of social capital is relevant to discussions of crime, litigiousness and even traffic offences because it can be associated with ‘lower crime rates ... and improved governmental responsiveness and efficiency’.⁸

A recent Australian Institute of Family Studies research paper observed a relationship between social capital and labour market outcomes. Some 1,500 randomly selected Australians were surveyed and divided into four groups: social capital rich; strong norms and civic connections (people involved in their community but with few family and friends); informal emphasised (those with family and friends but who are not heavily involved in the community); and social capital poor. It is notable that the ‘social capital poor’ have a lesser likelihood of being employed full-time, affecting their wellbeing and that of those around them.

3.8 Predicted Labour Force Status by Social Capital Type

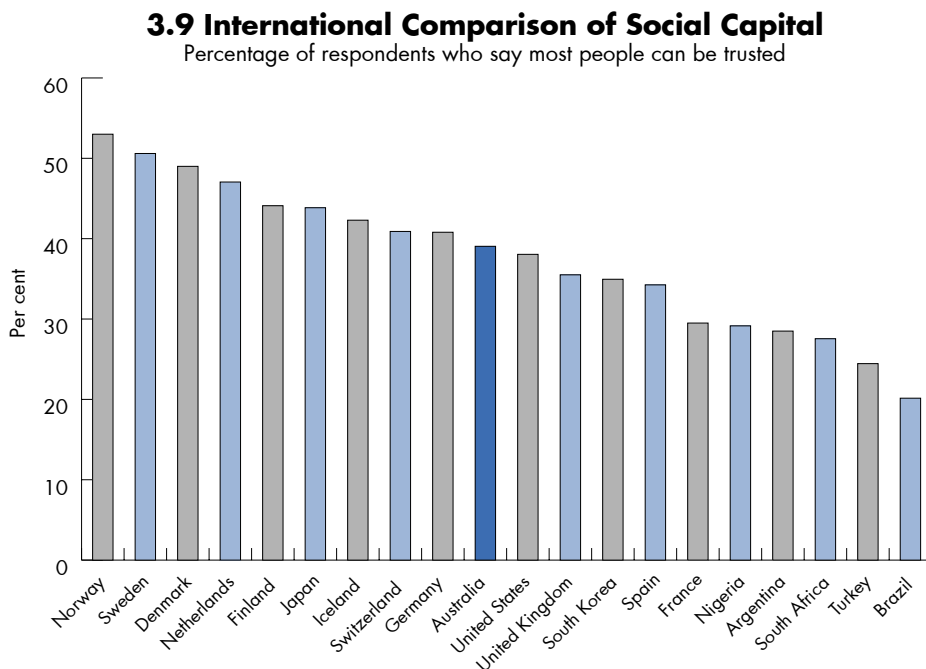


Source: W. Stone, M. Grey and J. Hughes, *Social Capital at Work: How Family, Friends and Civic Ties Relate to Labour Market Outcomes*, Research Paper No. 31 (Melbourne: Australian Institute of Family Studies, 2003).

Social Capital: An International Comparison

A recent Productivity Commission research paper provided values for the amount of civic cooperation and trust in given countries. By averaging these figures countries can be ranked. Amongst those surveyed, Australia's social capital is in the medium range.

From the graph below, it appears that countries that are geographically, economically and/or politically similar have comparable amounts of social capital. Scandinavian countries perform particularly well. This gives rise to one of the criticisms of the concept of social capital—that it is difficult to determine whether it is ‘either a cause or a consequence (or both) of high levels of social and economic wellbeing’.



Source: Productivity Commission, *Social Capital: Reviewing the Concept and its Policy Implications*, Commission Research Paper (Melbourne: PC, 2003), 27, xii.

Summary

Crime is probably the most important indicator of social order and cohesion, since high levels of crime signify individuals prioritising personal gain over society's wellbeing and, more generally, a disengagement from the community. In Australia, there are clear avenues in policy for improvement in the rates of serious crime.

Serious crime in Australia has increased dramatically over the last 40 years, but decreased in recent years. The serious crime rates of Australia, the United Kingdom and the United States are inversely related to both numbers of police officers and numbers of prisoners. This correlation does not imply causation, although the sustained nature of the inversion would suggest such a relationship.

One possible explanation for criminals' civic disengagement is the prevalent use of illicit drugs. A majority of prisoners used an illicit drug six months prior to their offence, and a near-majority of prisoners report ongoing addiction. It is unclear though whether targeting drug use will reduce crime, since illicit drug use in the last ten years has fluctuated whilst the serious crime rate has not. Perhaps drug use is more a symptom of social disorder than a cause, and it may be inferred that increases to numbers of police and prisoners will do more to reduce serious crime than anti-drugs strategies.

The Australian level of litigiousness is unlikely to match that of the United States. There are fewer incentives for Australians to litigate speculatively than in the United States, with fewer jury trials and different cost arrangements.

Australia's level of social capital can be described as average by world standards. An individual's social capital grouping was shown to have a tangible effect on his or her employment status, or more likely, vice versa. This is but one of the many reasons labour market reform to increase employment must remain a priority (see Chapter 9).

4. SCHOOL EDUCATION

JENNIFER BUCKINGHAM

Introduction

Schooling in Australia has changed markedly in the last 50 years. Three trends are apparent: an increasing preference for non-government schools; a large increase in students choosing to study to year 12; and a decline in boys' educational performance.

At the beginning of last century, around 80% of children attended government schools. Almost all of the other 20% were in Catholic schools. In the 1950s, Catholic schools began to struggle financially, as the religious teaching orders could no longer meet the demand created by increasing enrolments. In the 1970s, government grants were extended to all non-government schools on the basis of need.

Enrolments in Catholic systemic schools have changed little since then, but they have become increasingly dependent on government funding. The number and enrolment share of other non-government schools, however, have increased substantially over the same period. In the 45 years to 2002, the number of independent schools more than doubled while numbers of state and Catholic schools declined.

This expansion of the independent sector, supported by increasingly generous government funding, put non-government schools within the reach of a larger group of families. Non-government schooling became both more desirable and more accessible.

Another massive change also occurred between 1967 and 2002: the proportion of students continuing to Year 12 (the retention rate) tripled. Most of the increase was during the 1980s, when youth unemployment was high, and there have been only minor fluctuations since then. Schools are now expected to provide for a broad range of abilities and interests, and many changes have occurred, including the addition of vocational subjects to the senior school qualifications and the introduction of continuous assessment.

How these changes, as well as concurrent social changes, have influenced patterns of student achievement has come to light in the last few years. Before the 1990s, the gender gap in student achievement was small, however during the 1990s, several things combined to increase the gender gap in favour of girls. There was a concerted effort to increase girls' participation and achievement, and curriculum and assessment began to emphasise skills better suited to the strengths of girls—language, communication and introspection. Additionally, the number of male teachers declined, particularly in primary schools where the foundations of literacy and numeracy are built.

The dearth of male teachers, as well as the predicted shortage of maths and science teachers in the near future, is often blamed on low teacher salaries. This is only partly true. Starting salaries for teaching graduates are comparable to other professions in Australia and starting teachers in other countries. Yet the maximum salary for classroom teachers in Australia is artificially low and is dependent on years of experience rather than performance or the difficulty of conditions.

The Growth of Non-Government Schooling

a) Students

Australia has a long history of non-government schooling. Up until the 1970s, when non-government schools began receiving annual recurrent and capital grants from government, the size of the non-government sector fluctuated between 20-25% of all students. Since then there has been a steady increase in the number of non-government school students, reflected as a growing proportion of all students, while the number of state (public) school students has changed little.

Around 70% of students at a national level still attend state schools, but this conceals substantial variation between residential areas. Census data from 2001 shows that state school students are the minority in some metropolitan suburbs.

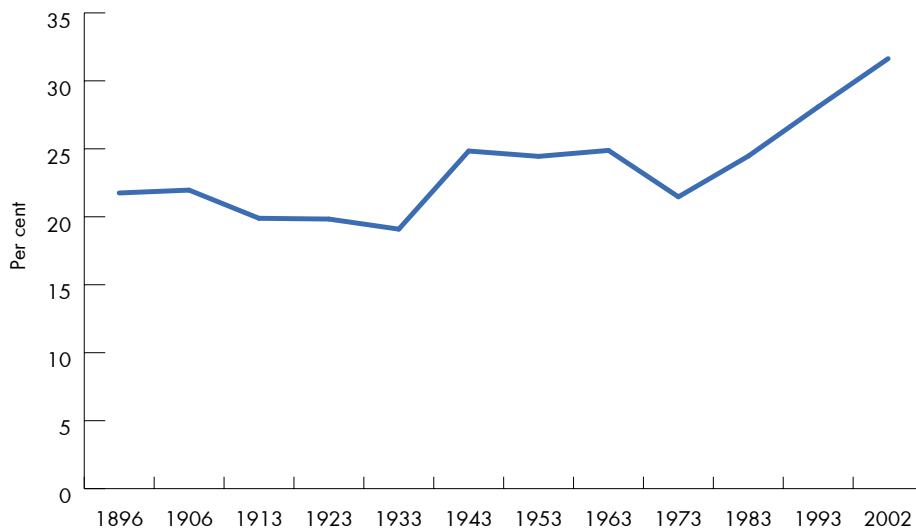
Likewise, there are important differences between the relative sizes of the school sectors in primary and secondary schools. The state school sector educates only six in ten secondary school students and the independent sector is much larger at the secondary level than at the primary level.

Proportion of Students by Level of Education, 2002

	<i>State</i>	<i>Catholic</i>	<i>Independent</i>
Primary	72%	18%	10%
Secondary	63%	21%	16%

4.1a Students in Non-Government Schools, 1896-2002

Proportion of all students



Sources: ABS, *Yearbook, Australia* Cat 1301.0; *Schools, Australia* Cat. 4221.0 (Canberra: ABS, various years).

b) Schools

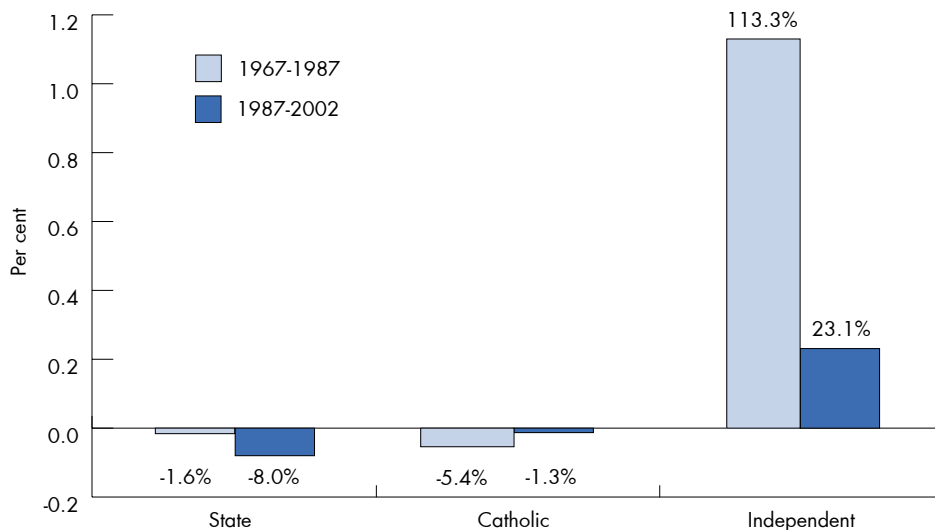
Over the 45 year period from 1967 to 2002, the school-age population increased by 700,000 children. These children were increasingly accommodated in non-government schools, and the number of state schools declined by 8%.

The increase in the non-government sector, traditionally dominated by Catholic systemic schools, was almost entirely due to the large number of new independent schools, particularly low fee, non-denominational Christian schools.

Independent schools tend to be small compared to state and Catholic schools, so the increase in the number of these schools slightly exceeds the increase in students. It suggests that the independent sector has the ability and flexibility to expand according to demand.

4.1b Growth of State and Non-Government School Sectors, 1967-2002

Per cent change in the number of state, Catholic and independent schools



Source: ABS, *Yearbook, Australia; Schools, Australia*, Cat.No. 4221.0 (Canberra: ABS, various years).

Sources for Figure 4.2, p.48: ABS, *Education and Training Indicators*, Cat. 4230.0 (Canberra: ABS, 2002); Ministerial Council on Education, Employment, Training and Youth Affairs, *National Report on Schooling in Australia, 2001* (Melbourne: MCEETYA, 2002); Steering Committee for the Review of Commonwealth/State Service Provision (SCRCSSP), *Report on Government Services* (Melbourne: PC, 2003); ABS, *Education and Training Indicators*, Cat. 4230.0 (Canberra: ABS, 2002).

School Funding

State governments are primarily responsible for the funding of state schools, while the Commonwealth government provides most of the public funding for non-government schools. In order to be eligible for government grants, non-government schools must meet state regulations regarding teachers, curricula, and school premises.

Non-government schools are provided with government funding on a per student basis according to a measure of the average socioeconomic status of the school population. Schools with the most students from low income families are eligible for the highest level of funding.

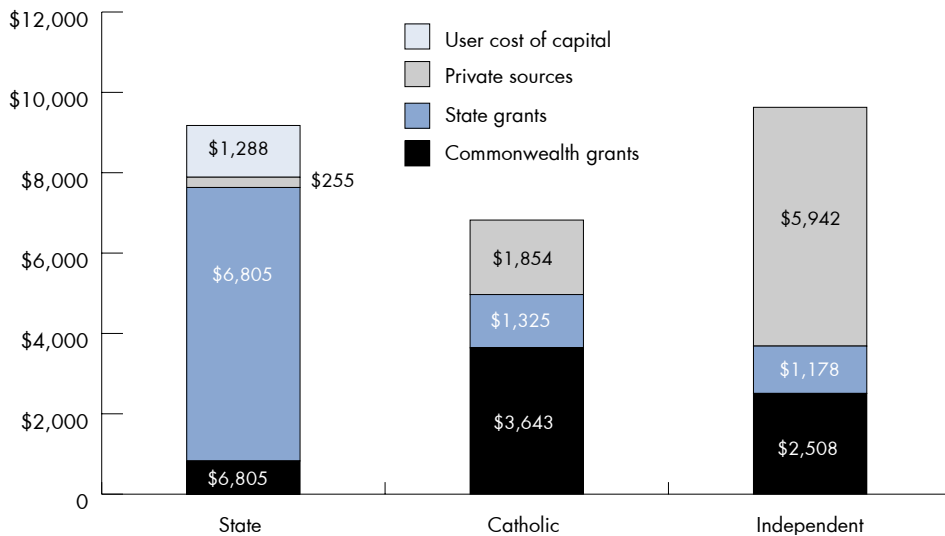
Students in non-government schools receive less government funding than students in state schools. This means that non-government schools relieve governments and taxpayers of a significant financial burden at the expense of the families who use them. Non-government schools supplement their incomes with tuition fees of their own determination, which generally range between \$1,000 to \$16,000 per annum. The vast majority of schools fall at the lower end of the scale.

When all aspects of income and expenditure, such as the user cost of capital*, are included, the average cost of a state school education (\$9,176) approaches that of an independent school education (\$9,628), especially considering that independent schools educate a larger proportion of more expensive senior school students. Catholic schools' average income per student is several thousand dollars less (\$6,822).

* the opportunity cost of using funds to provide services rather than investing or debt servicing

4.2 School Income Per Capita

State schools 2000-01 and non-government schools 2001



Note: The figure of \$255 per student for the private income of state schools is from the 1998-99 Household Expenditure Survey (ABS) so would probably be higher in 2001.

Sources: see p.47.

School Type and Household Income

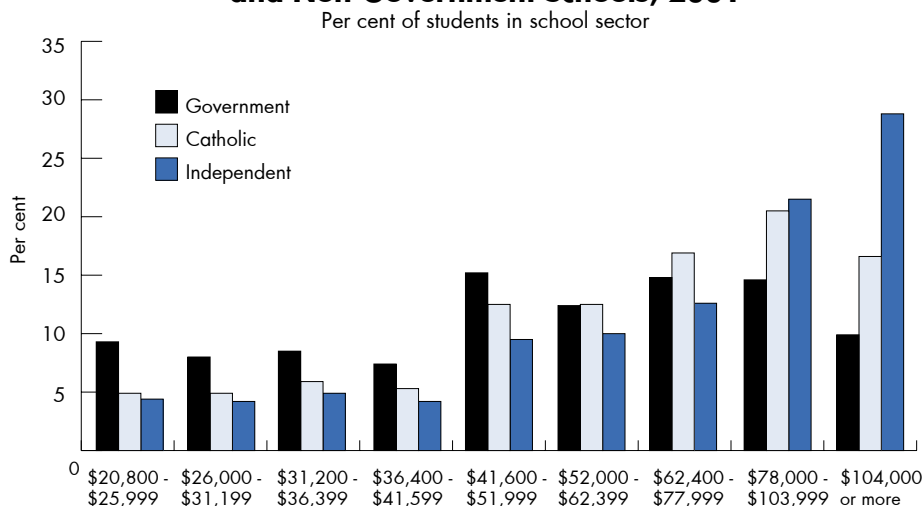
Figure 4.3 below shows the proportion of children from various income groups within each school sector. For example, children from households with incomes ranging from \$26,000 to \$31,199 make up 8% of government school students, 5% of Catholic school students and 4% of independent school students.

These data come from the 2001 Census, with two exclusions: households not providing income data and households with reported incomes below \$20,800 per annum. The latter exclusion is because there is reason to believe that these income data are unreliable. Each household with a child in school must by definition consist of at least one adult and one child. According to the Melbourne Institute for Economic Research, the minimum income such a household would be entitled to when social security payments are included is \$370 per week or \$19,240 per annum. This suggests that household incomes lower than this are underestimates. The Australian Bureau of Statistics has published advice to this effect.

Children from all income groups are represented in all three school sectors. The greatest differences are at the extremes. As would be expected, a greater proportion of government school students come from the lowest income groups, and a larger proportion of non-government students come from high income groups.

There are, however, two important points to note: First, the number of children in government schools from households with incomes below average weekly earnings (the bottom three income brackets) is only one third less than the number of children from households in the top three income brackets. Second, almost 30% of families with incomes below average weekly earnings have children attending non-government schools, challenging the stereotype that non-government schools are exclusively for the wealthy.

4.3 Household Income of Students in Government and Non-Government Schools, 2001



Source: ABS, Census 2001, unpublished data.

Retention to Year 12

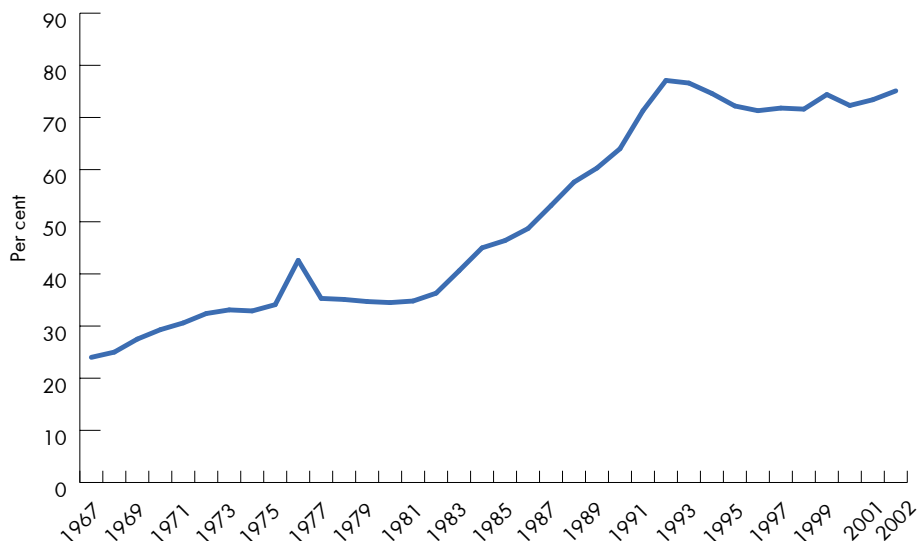
The apparent retention rate is the proportion of students who continue to Year 12, expressed as a percentage of their Year 7 or Year 8 cohort group (the first year of secondary school, depending on the state or territory). The retention rate is a measure of participation in post-compulsory schooling, since most students pass the compulsory school age in Year 10.

The retention rate is affected by a number of factors. One is the labour market. A lack of employment opportunities will result in a larger number of students staying at school. Another is the availability of educational alternatives, such as TAFE. Yet another is the quality of schooling and how well schools are engaging students.

High retention rates are generally seen as positive, yet they can be a symptom of high youth unemployment, as seen during the 1980s. Evidence of the value of completing Year 12 is also mixed. Data from the Household Income and Labour Dynamics in Australia (HILDA) Project released in 2002 by the Commonwealth government showed that early school-leavers were at a strong disadvantage in the labour market. However, a study by the Australian Council for Educational Research in 2003, the Longitudinal Surveys of Australian Youth (LSAY) Research Report 31, found that the relationship between early school leaving and unemployment is largely mediated by socioeconomic status and other variables. The study also found that non-completing students who left after starting Year 12 had higher rates of unemployment than those leaving during or at the end of Year 10. The majority of early school leavers gave employment as their reason for leaving rather than dissatisfaction with school.

4.4 Year 12 Retention, 1967-2002

Apparent retention rate Year 7/8 to Year 12, all schools



Source: ABS, *Schools Australia*, Cat. 4221.0 (Canberra: ABS, 2002).

Literacy and Numeracy of Boys and Girls

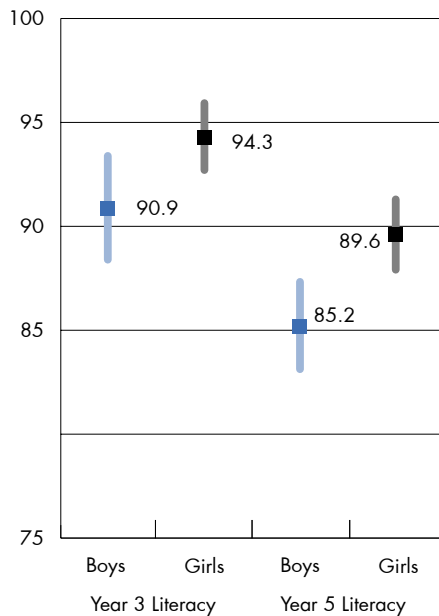
Each state and territory assesses literacy and numeracy in Years 3 and 5. All government schools must participate in the testing programmes, and most non-government schools participate voluntarily.

Children's achievement in the state and territory testing programmes is assessed against common and agreed national benchmarks to determine the proportion of children nationally and within each jurisdiction who have reached an adequate level of proficiency in these skills.

The 2000 National Benchmark Results also demonstrate the widening gap between boys and girls. The error bars in the graphs below denote the range within which the true average score is likely to fall. If the error bars of boys' and girls' scores overlap, their average scores are not statistically significantly different. In Year 3, boys were not significantly different to girls in either literacy or numeracy. In Year 5, however, the gap widened to the extent that girls' mean literacy performance was significantly higher.

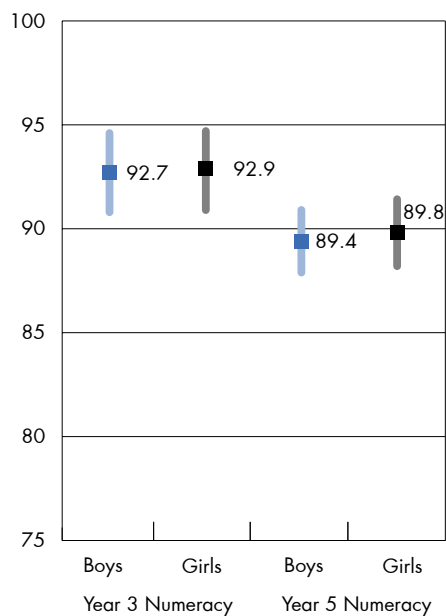
4.5a Literacy in Year 3 & 5, 2000

Per cent achieving reading benchmark



4.5b Numeracy in Year 3 & 5, 2000

Per cent achieving numeracy benchmark



Sources: MCEETYA, *National Report on Schooling in Australia 2000: National Benchmark Results, Literacy and Numeracy, Years 3 and 5* (Melbourne: MCEETYA, 2000), see www.curriculum.edu.au/mctyapdf/2000_benchmarks.pdf

Year 12 Performance of Boys and Girls

Boys' educational disadvantage has become a particular area for concern, especially for the Commonwealth government, in the last several years. Boys, on average, perform worse than girls in most secondary subjects, and this is strongly related to their lower literacy levels in primary school. The gap between boys and girls widens as they progress through school.

In all states and territories for which information is published, girls outperform boys in Year 12. The table below is based on final marks in senior school subjects that are either publicly examined or externally moderated for the most recent year available. They do not include vocational studies or subjects that are school assessed.

Girls record higher achievement than boys in the majority of subjects, however the size of this majority differs substantially. In New South Wales, boys' average marks were lower than girls' in all but four subjects, where they were equal. In Western Australia, girls' advantage was not as large—girls outperformed boys in 15 of 27 subjects—and in this state the differences between the means were much smaller. The reason for these discrepancies is not clear, but warrants investigation.

4.6 Comparison of Boys' and Girls' Year 12 Performance

Number of subjects

<i>State/Territory</i>	<i>Year</i>	<i>Girls Higher</i>	<i>Boys Higher</i>	<i>Equal</i>	<i>Total Subjects</i>
NSW	2000	62	0	4	66
VIC	2002	57	9	2	68
QLD	2002	38	3	3	44
SA/NT	2002	31	1	2	34
WA	2002	15	4	8	27
ACT	2002	25	6	1	32

Notes:

- Includes only subjects with at least 100 candidates
- NSW, WA, ACT: Mean scores
- VIC, QLD, SA: Per cent of boys and girls in top two achievement bands
- Equal performance if difference is 1%

Sources: NSW Board Of Studies; Victorian Curriculum & Assessment Authority; Queensland Studies Authority; South Australian Board of Senior Secondary School Assessment; Western Australian Curriculum Council; ACT Board of Senior Secondary Studies.

Male Teachers

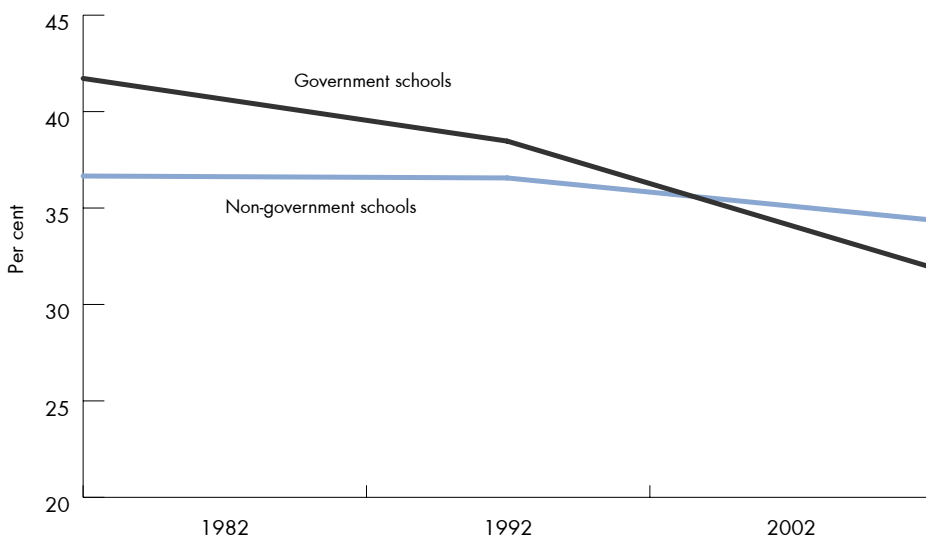
The decreasing number of male teachers among an expanding teaching workforce is now well known. The biggest decrease has been in the government sector and the lowest proportion of male teachers is found in government primary schools—one in five in 2002, down from one in four in 1992.

Whether or not the low numbers of male teachers is a problem and, if so, how to rectify it, is under debate. Teachers' unions argue that the gender of teachers is irrelevant. Yet prominent educationists, such as Professor Peter West of the University of Western Sydney, claim that more male teachers are needed, at least in part because of the increasing number of boys with no consistent male role models in their home lives.¹ The recent Commonwealth Government Parliamentary Inquiry also found that attracting and retaining male teachers, especially in primary schools, was a priority.

Factors that may have resulted in the decline in male teachers include: inflexible, stunted salary scales for classroom teachers; centralised recruitment and employment in some states, so that teachers have little say over where they teach; child protection issues; the strong influence of feminism in teacher education courses; and the self-perpetuating cycle where men avoid professions in which they are the minority.

4.7 Male Teachers, 1982-2002

Percentage of all full-time equivalent (FTE) teachers



Sources: ABS, *Yearbook Australia*, Cat. 1301.0 (Canberra: ABS, 1984); ABS, *Schools Australia*, Cat. 4221.0 (Canberra: ABS, 2002).

Teacher Salaries

Almost 70% of teachers are employed in government schools. Their salaries are centrally negotiated by teachers unions and state governments. Starting salaries for classroom teachers range from \$38,000 to \$41,000 per annum, depending on the state or territory.

The maximum salary available to classroom teachers varies much more. Teachers progress on the salary scale according to years of experience. In most states, they are entitled to the top salary—between \$55,000 to \$58,000 per annum—after around eight to ten years. In some states, however, there are additional categories of classroom teacher, such as Leading Teachers in Victoria, which extend the salary scale to more than \$66,000 per annum.

The table below gives starting teacher salaries (in US\$ Purchasing Power Parity) for a selection of OECD countries in 2000, plus the mean for all OECD countries. It also shows the ratio of the top teacher salary to starting salary. In Australia, the average starting salary is well above the OECD mean. The top salary, however, is only 42% higher than the starting salary, well below the OECD mean increase of 70%.

Australian teachers, along with those in England and Denmark, reach the top of the salary scale within the shortest period of time of all OECD countries—an average of eight years. The OECD average is 25 years, and in some countries, it is as much as 40 years. This suggests that Australian teachers could most reasonably argue for an extension of the pay scale in order to retain and reward experienced teachers, rather than an increase across the board.

4.8 Starting and Top Teacher Salaries in Some OECD Countries, 2000

Country	Start \$US (PPP)*	Top: Start	Country	Start \$US (PPP)*	Top: Start
Switzerland	41,048	1.55	Japan	22,670	2.41
Germany	34,891	1.32	Italy	22,657	1.48
Denmark	29,116	1.13	Austria	22,574	2.08
Netherlands	28,443	1.53	England	22,428	1.58
United States	27,643	1.73	France	22,358	1.89
Spain	27,046	1.47	Finland	20,270	1.45
Australia	26,946	1.42	Sweden	19,893	
Korea	26,148	2.66	New Zealand	17,354	1.94
Norway	23,752	1.22	Czech Republic	7,043	1.78
OECD Mean	22,727	1.7	Hungary	6,086	1.94

*Purchasing Power Parity is a rate of exchange that accounts for price differences across countries allowing international comparisons of real incomes. At the PPP US\$ rate, PPP US\$1 has the same purchasing power in the domestic economy as \$1 has in the United States.

Source: OECD, *Education At A Glance 2002* (Paris: OECD, 2002), Table D6.1.

Summary

Australian families are increasingly exercising their right to choose a school for their children. Unfortunately, despite greater financial support provided by the Commonwealth to non-government schools, choice is still unavailable to many families. There are still significant private costs involved in non-government schooling that many parents cannot meet. Those who can often do so by making sacrifices such as taking an extra job or working longer hours. Meanwhile, large numbers of wealthy families send their children to state schools, making very little direct contribution to the cost of their children's education.

The current funding system is divisive and inequitable. The entitlement of all children to an education, and the commitment of a society to ensure its availability through public funding, should not be interpreted as the state's entitlement to monopolise its provision. There is simply no good reason why school funding should be contingent on the type of school.

In all schools, boys are still underachieving relative to girls, with the widest disparities at the most senior levels. This is not necessarily cause for despair, as many of the insights into the causes of this problem, and the programmes and reforms developed to remedy them, are quite recent. Nonetheless, there is no room for complacency. Researchers and educators have now identified and agreed upon a number of key features of quality teaching for boys—the single most important predictor of their achievement—and no time should be wasted in adopting them.

An important part of this process is to get more men into schools and classrooms. Few would argue that male teachers are a magic cure for all boys' educational ills. Male teachers do, however, bring different and valuable qualities. If the gender balance of the teaching force were the opposite, the lack of female teachers would be seen as a great cause for concern. The low and diminishing number of male teachers ought to be viewed as equally lamentable.

Low teacher pay and stunted career prospects have played a part in this development. The solution is not to raise teacher salaries across the board, but to extend the career ladder for classroom teachers, and to offer rewards for excellence.

Another culprit is the central recruitment and deployment of teachers. If teaching is to be regarded and respected as a profession, teachers must be given responsibility for their employment instead of letting bureaucrats decide when and where they teach and under what conditions.

Child-centred school funding, where government education grants follow children to the school of their choice, would allow this to happen. Under such a system, money would go directly to schools, giving them the ability to spend funds in the way that best meets the needs of their students—including employing the most suitable teachers. In education as in most areas of life, the less government involvement, the better.

5. HIGHER EDUCATION

ANDREW NORTON

Introduction

Australia's universities have regularly been seen as troubled. In the National Library's catalogue there are publications on the 'crisis' in universities published in 1952, 1965, 1970, 1980, 1994, and 2001. In the last 25 years universities have been caught between demand for mass higher education, prompted by a huge increase in the number of jobs requiring university credentials, and fiscal constraint, as governments struggled to meet ever increasing calls on the public purse. Unlike schools, there is only a very small private higher education sector, so problems in the public sector affect almost every student and academic.

Since the 1990s, there has been a higher education policy stalemate. Pro-market reformers have been unable to build a large enough constituency for change, while advocates of more public funding have failed to secure any significant increases in per student funding. The stalemate was partly broken in 2003, when higher education reforms to take effect in 2005 promised both limited price deregulation and increasing public funding. However, with the Australian Labor Party promising to abolish these reforms if it wins the 2004 election, the structural problems that have plagued universities for decades may be reinstated.

Despite all these problems, it would be wrong to say that the system has completely failed to cope. As the following sections will detail, many more students have been enrolled with fewer negative consequences for key indicators than someone who read only the 'crisis' literature would predict.

Note for Figure 5.1 (overleaf): Before 2001 the annual count was based on first semester enrolments. Since this missed students who enrolled later in the year the method has been changed, increasing total numbers by around 100,000. We have shown first semester enrolments and total enrolments for 2001-2003 to show both actual numbers and numbers collected on a consistent basis.

Sources: Department of Education, Science and Training, *Higher Education Time Series Tables 2000*, Table 1; *Students 2003 (First Half Year) Selected Higher Education Statistics*, Table 19; *Higher Education Report for the 2004 to 2006 Triennium*, Table 2.1 (Canberra: DEST, various years).

Growing Student Numbers

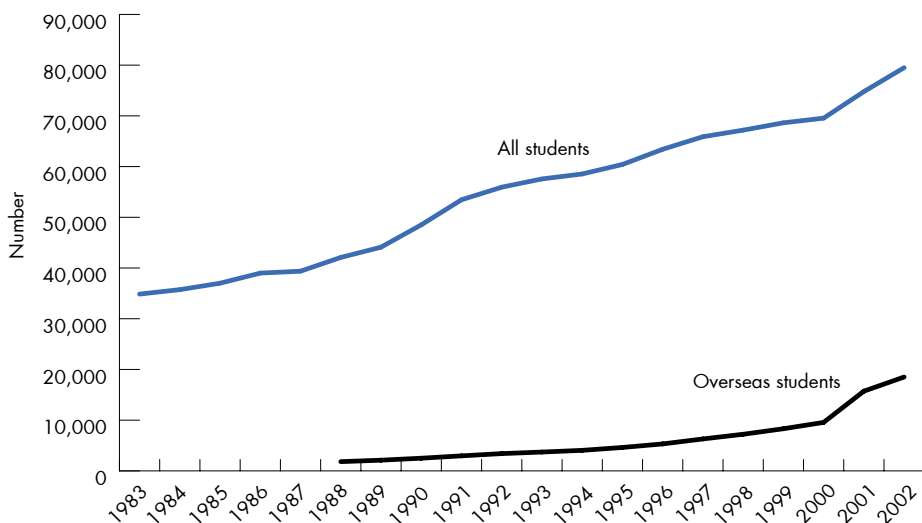
Higher education is a growth industry. Figure 5.1 shows that student numbers have more than doubled in less than 20 years and that expansion continues unabated. The extra students added in the first part of this decade roughly match the early 1990s boom. These raw statistics, however, conceal major changes. While growth is a constant, the nature of that growth changes over time.

Previous rapid increases in HECS-liable undergraduates, the stereotypical university student, eased in the mid-1990s. In recent years, the number of these students commencing their studies has actually declined. The reason for this is not that demand has dropped off, but that for these students supply and demand have very little to do with each other. Places for HECS-liable undergraduates are allocated to universities by the Commonwealth government. The numbers reflect historical enrolment patterns and the Commonwealth's overall budgetary situation more than student demand, labour market requirements, or universities' strategic priorities.

The ongoing growth in student numbers has been in students enrolled outside this policy framework. The biggest increase has been in students from overseas. Their proportion of the total student body more than tripled between 1992 and 2002, reaching 23.2%. There has also been strong growth in Australian students taking up fee-paying postgraduate studies, with universities doubling their student places since 1997.¹ Since 1998, Australian students have been allowed to enrol in full-fee undergraduate courses. Their numbers grew from 1,340 in 1998 to 9,303 in 2002. The contrast between the dynamism of the market-driven sector and the stagnation of the Commonwealth-driven sector is striking. It is likely that this contrast will sharpen further from 2005, when a new funding system takes effect.

5.1 University Students, 1983-2002

All students and overseas students



Sources: see p.59.

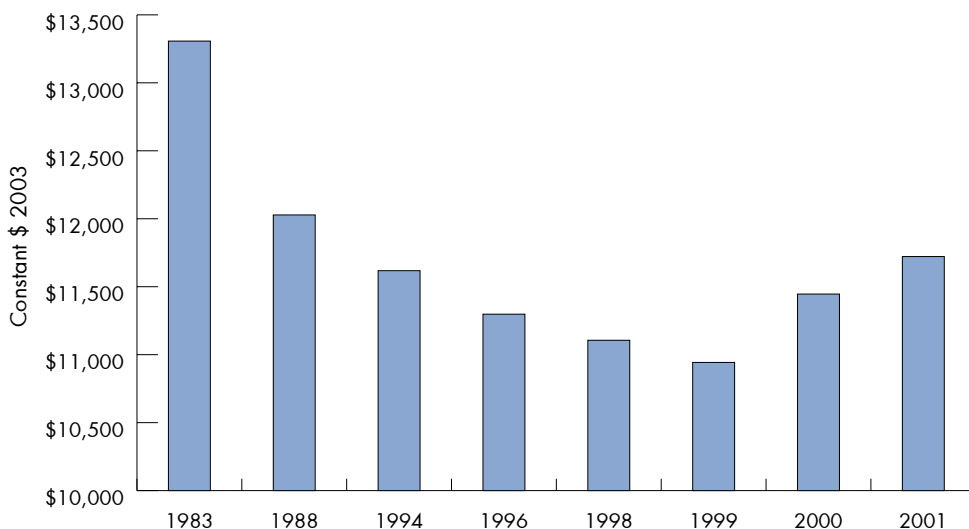
Revenue Restrictions

Along with restrictions on numbers, universities have faced severe revenue restrictions for their Commonwealth funded students. Claims that the Howard government has cut higher education funding by billions of dollars are untrue, but funding per student has been remained stable during the 1990s while costs have risen.

Figure 5.2 shows funding per full-time student. The small fluctuations are mainly due to universities exceeding their Commonwealth target numbers, thus spreading Commonwealth funding more thinly over the total number of students. Though students are charged a fee under the Higher Education Contribution Scheme (HECS), this money goes to the government, not the universities. Since universities have not been allowed to levy tuition charges on HECS students, they have faced severe financial difficulties.

Universities finances should improve from 2005. In that year, commencing students will no longer pay anything to the Commonwealth government. Instead, they will pay a student contribution amount set by the university which will go to the university. The maximum amount will be 25% more than existing HECS charges. Students can still defer payments until they earn an income, as with the current HECS system. Also, universities meeting conditions set by the Commonwealth government will receive higher subsidies.

5.2 Government Funding Per HECS-liable Student, 1983-2001



Source: Australian Vice-Chancellors' Committee, *Funding Tables* (Sydney: AVCC, 2003), Table 4.

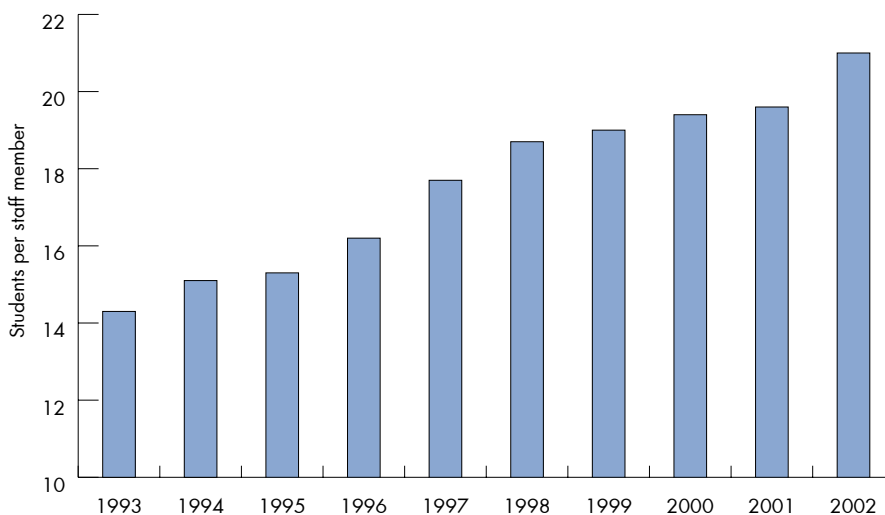
Problems For Students

The rapid expansion in fee-paying students has been one response to universities' financial difficulties. To some extent, fee-paying students cross-subsidise HECS students. Higher student to staff ratios have been another major consequence of costs increasing more quickly than revenue. Figure 5.3 shows that these have increased by nearly 50% since 1993. Some disciplines are more likely to have high student to staff ratios than others. Business courses tend to have the highest ratios, followed by information technology courses. These courses are popular with overseas students, suggesting that staff numbers have risen less quickly than student numbers.

Dissatisfaction on this aspect of university life is evident in the Course Experience Questionnaire, a survey sent to all completing university students. For students who completed in 2001, only 33% of students agreed that 'the staff put a lot of time into commenting on my work' and 45% that 'teaching staff normally gave me helpful feedback on how I was going'.²

Staff numbers are not the only issue, however. Universities have two main outputs, graduates and research, and it is research that ranks more highly in the staff culture. A 1999 survey of academics found that 91% thought that their research and scholarly activity would assist their promotion prospects, while just 44% thought that their effectiveness as a teacher would help.³ This culture is reinforced by the fact that the government financially rewards research achievements, but not teaching quality. As well as providing more staff, incentives for research and teaching need to be made more equal. Fee-paying students have started this process, and it will be reinforced by government-subsidised students also making direct payments to universities from 2005.

5.3 Ratio of Students to Staff, 1993-2002



Source: Australian Vice-Chancellors' Committee, *Resource Analysis 2003* (Sydney: AVCC, 2003), Table 2.

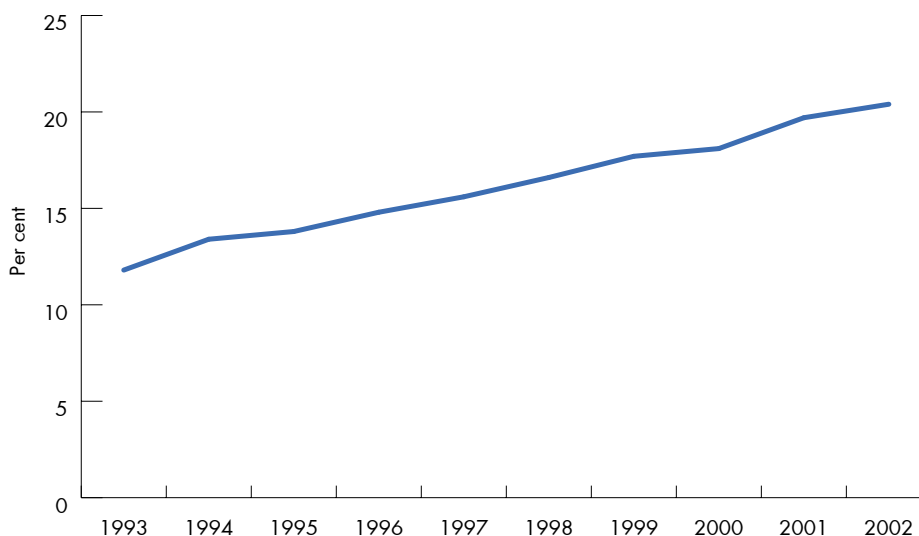
Graduate Employment

Though growth in domestic undergraduate numbers has now stalled, the huge increases prior to the late 1990s, plus immigration rules that favour graduates, have meant that the percentage of adults with university qualifications has risen rapidly. Figure 5.4 shows the increase. As less educated people move into retirement and are replaced by more educated young people, the trend to a more educated workforce will continue despite the plateau in Australian student numbers.

Contrary to some concerns, the large increase in university-qualified workers has not had obvious adverse effects on graduates' employment prospects. Unemployment for graduates is below 3%.⁴ Though around 20% of graduates are working in jobs that do not require degrees, this is only slightly more than was the case in the late 1970s and early 1980s, well before the rapid expansion that began in the late 1980s.⁵ However, that rapid expansion did increase the number of recent graduates still looking for full-time work several months after completion. While some graduates struggle to find suitable jobs, in other areas there are labour market shortages, such as the health sector.⁶ This mismatch partly reflects the inability of the centrally controlled higher education system to shift resources to where they are needed.

5.4 Persons with Bachelor Degree and Above, 1993-2002

Per cent of population aged 25-64



Source: Australian Bureau of Statistics, *Australian Social Trends* (Canberra: ABS, 2003), 84.

Summary

Universities have survived a very poor policy environment remarkably well. Though some universities are in a weak financial position, they have been able to cut costs and recruit sufficient numbers of full-fee students to stave off bankruptcy. Student satisfaction has been stable and graduate employment rates have generally been high.

It is not clear, however, that these trends could continue in the absence of major policy changes. The international market for students is highly competitive. Australia's main advantages have been its relatively low fees and its proximity to the main source of students, Asia. While the geographic advantage is constant, the cost advantage is vulnerable to a rising dollar. It also limits universities' capacity to increase revenue per student. On top of this, university cost-cutting is probably near, or even beyond, its limit. Further reductions in staff numbers would exacerbate what is already a major source of student dissatisfaction. Maintenance and capital works can often be postponed in the short term, but not the long term.

What universities ought to be doing will vary over time, and their huge expansion in the last few decades reflects a growing need for people with tertiary qualifications. The most pressing requirements now are ensuring spending per student more closely reflects optimal human capital investment, avoiding chronic shortages of graduates in certain fields, and increasing student satisfaction with teaching. The end of recurrent university budget shortfalls would come as a result of increasing per student expenditure to appropriate levels.

Many people argue that universities need more public funding. However, the argument that public funding is the only answer to universities' financial problems is not a credible position. Reliance on public funding has been the cause of universities' current problems, and any sustainable reform must find ways of financing undergraduate education that do not depend on the Commonwealth government. This does not preclude additional public funding, but it must be one source among others.

Some labour market shortages, such as for dentistry and pharmacy courses, could be fixed simply by letting market forces operate more freely. Other shortages, such as for nurses and teachers in some disciplines, are more complex, because relatively poor conditions for these workers make these careers less attractive than other options, and significant fee increases would make them even less appealing. Here there may be a role for state governments, which are the major employers of teachers and nurses.

Improving student satisfaction is best done indirectly by improving the incentives universities face for undergraduates. Under the current system, universities receive the same number of students and the same amount of money whether they do a good job or not. Setting student numbers and income through the market—that is, according to what people want to study and how much they are prepared to pay—should cause universities to re-focus on undergraduate teaching.

It remains to be seen how well the new reforms, to take effect in 2005, will achieve these goals. University finances will certainly improve, and there are added financial incentives to focus on quality teaching. The less flexible system of allocating government-

subsidised places to universities will, however, reduce responsiveness to student demand. The reforms are simultaneously more market-oriented and more state-interventionist than the current system.

6. HEALTH

PETER SAUNDERS & HELEN HUGHES

Introduction

Australia has an excellent health record, as our low infant mortality and high longevity rates confirm. Health expenditures are a large and rapidly growing component of Commonwealth and State government budgets, but there is increasing dissatisfaction with the quality and efficiency of public hospitals, and a growing awareness that the mainly publicly financed health system is skewed against lower income groups.

Public health spending is being pushed up by an ageing population (older people use up more medical resources), the cost of new drugs and medical technologies, as well as growing inefficiency, notably in the dominant public sector. The evidence is in hours of waiting in emergency departments, days of waiting for hospital beds, and months of waiting for operations. At the margin, elderly patients in public health facilities do not always receive the care they require and deserve. Other areas of concern are outer suburban and rural health facilities, mental health and Aboriginal health. In extreme cases, poor standards of care have threatened and even cost patients' lives.

The Australian health system is inequitable. People of low socioeconomic status die younger than people of high socioeconomic status. This is partly the result of lower educational attainments with consequent lower attention to healthy lifestyles, but higher socioeconomic status groups also access 'free' public health care more intensively. The generous intention of giving all Australians free health services through Medicare is turning into a nightmare of inequality because the taxation costs of providing 'free' services for all are hidden.

Only 30% of Australia's health bill is paid for privately and numbers taking out private medical insurance are falling. Projections of present trends in health care point to rapidly rising taxation requirements. Without reforms that encourage Australians to take responsibility for their health, particularly as they age, and the introduction of greater competitiveness from private to public health facilities, the public costs of health will escalate, leading to even more inefficiency, inequality and steep tax increases that will greatly affect low and middle income earners.

Infant Mortality and Life Expectancy

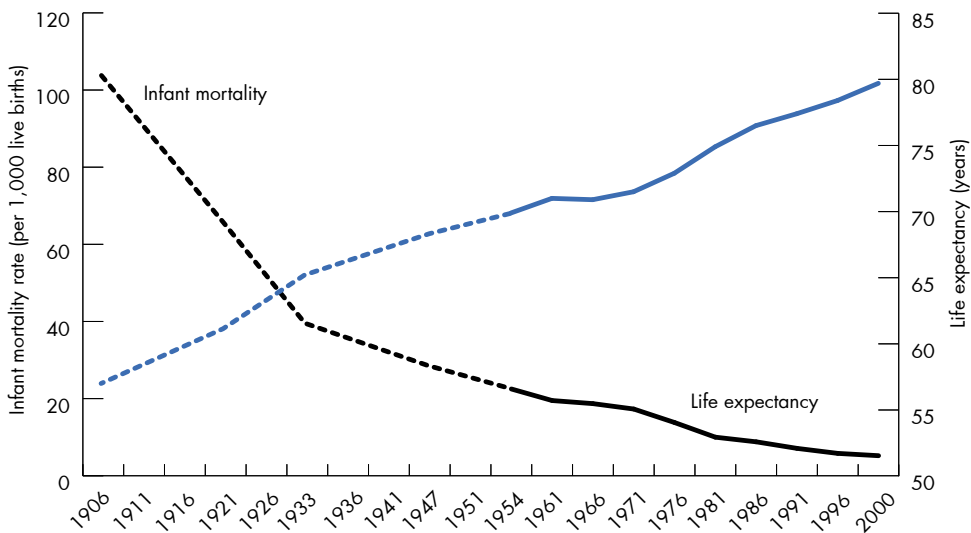
A hundred years ago, one baby in ten died before reaching her or his first birthday. Today, this is true of only five in every 1,000.

Australian men born 100 years ago could expect to live to age 55, women to age 59. Men born today, by contrast, have a life expectancy of 77 years, and women enjoy a life expectancy of 82 years. Australians have a higher average life expectancy than Americans, Britons, New Zealanders, Canadians, Italians and Germans, let alone people living in transitional (former communist) and developing countries.

The huge reductions in infant mortality rates, coupled with the extraordinary lengthening of average life expectancies, are only partly due to advances in medical science. Lower infant mortality and increased life expectancy result much more from improvements in diet, housing, working conditions and other material aspects of everyday life that have accompanied economic growth.

We have grown used to these improvements and tend to take them for granted. Some commentators would have us believe that life is getting worse and that progress has stopped or even gone into reverse. But the opportunity to live a long life is arguably the best single measure of a society's progress. With further growth the falling trend in infant mortality and the rising trend of life expectancy will continue. The two lines in Figure 6.1 represent the greatest triumphs recorded by Western capitalism over the last 100 years.

6.1 Infant Mortality Rate and Life Expectancy at Birth, 1906-2000



Source: ABS, *Yearbook Australia* (Canberra: ABS, 2003).

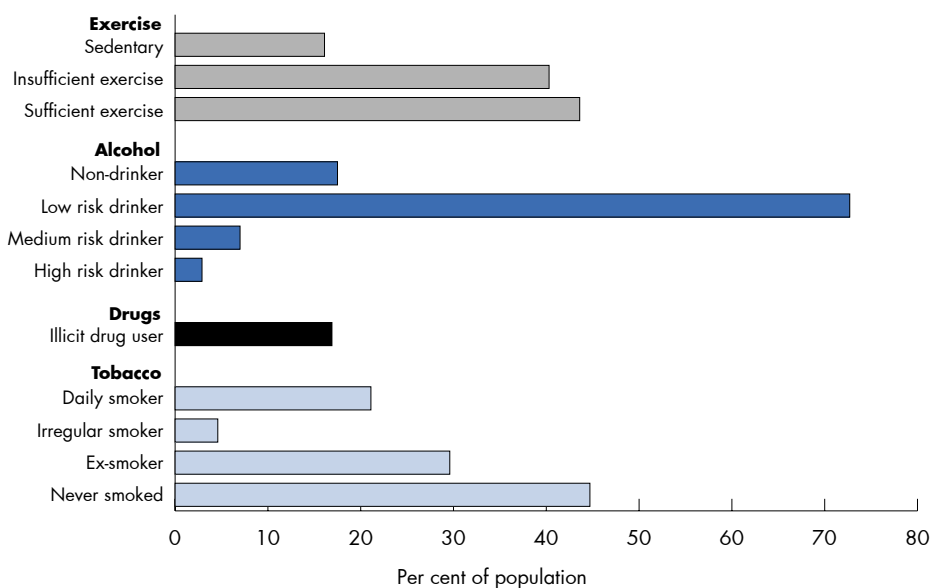
Accepting Responsibility for Health: Lifestyle Changes

The escalating costs of health care can be met in one of three ways. Firstly, the government could keep increasing taxes, but Chapter 8 shows that Australians are already overtaxed. Secondly, the quality of care could be reduced, or access to services could be rationed by queuing, but such measures would be harsh and unpalatable. Thirdly, Australians could be encouraged to take more responsibility for their own health, thereby reducing the public finances required to maintain and improve the efficiency and equity of the health system.

This third strategy clearly makes the most sense. Australians must take more responsibility for maintaining their own health and fitness by exercising more, smoking and drinking less, and taking more care with their diet.

Some harmful behaviour patterns have declined markedly in recent years. At the end of World War II, about half the population smoked tobacco. Today less than one quarter smoke. But some other harmful behaviour has increased. The use of illicit drugs is now fairly common. Only around half of Australians are reckoned to do 'sufficient' exercise to maintain a healthy life, and one in six is classified as 'sedentary'. If people had to contribute more directly to their medical costs, they would be more likely to take greater responsibility for behaviour that affects their health.

6.2 Smoking, Drinking and Exercise, 2001



Sources: Australian Institute of Health & Welfare, *2001 National Drug Strategy Household Survey* (Canberra: AIHW, 2002); AIHW, *The Active Australia Survey* (Canberra: AIHW, 2003).

Accepting Responsibility for Health: Private Health Insurance

Australian governments picked up 70% of the total \$66.6 million health spending in 2001-2002. Medicare makes huge paperwork demands on health professionals, but has failed to introduce cost accounting as an essential management and quality of care tool in public hospitals. Competitive private health facilities help to raise standards of management, but they are at present too limited to affect the public sector.

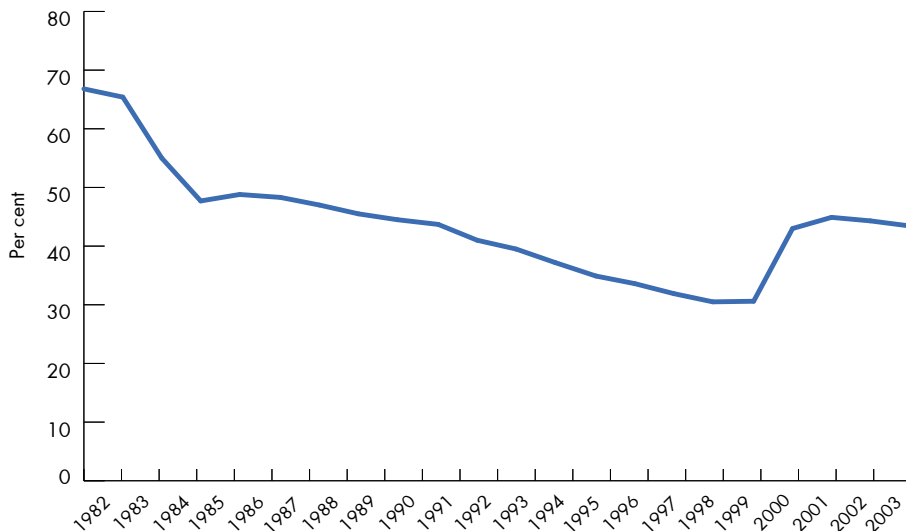
Before Medicare, two-thirds of Australians had private medical insurance, but this proportion fell precipitously as the government’s compulsory scheme ‘crowded out’ voluntary self-provisioning. Since the introduction of Medicare in 1982, many Australians have come to think that since they pay a 1.5% Medicare levy on taxable income, they need not insure themselves against illness. But the Medicare levy pays for less than one-eighth of government health spending. The rest is paid out of general tax revenue and lacks the checks and balances that would encourage efficiency and equity.

In 1999 the Commonwealth government introduced a 30% tax rebate on private health insurance premiums, and in 2000 set a deadline of 30 years of age for new members to avoid age-graded increments in premiums. The proportion of the population with private cover shot up as a result, but it is now slowly declining again as the average cost of premiums outstrips inflation. In the absence of an emphasis on productivity as well as the quality of care, new medical technology raises health costs.

Some welfare groups want the government to scrap the private health insurance rebate. Scrapping the rebate would escalate demands on public health so that public spending on health would have to rise even faster than it is now.

6.3 Private Health Insurance, 1982-2003

Proportion of population insured



Sources: Private Health Insurance Administrative Council, *Quarterly Coverage Statistics*, see www.phiac.gov.au; ABS, *Australian Social Trends*, Cat. 4102.0 (Canberra: ABS, various years).

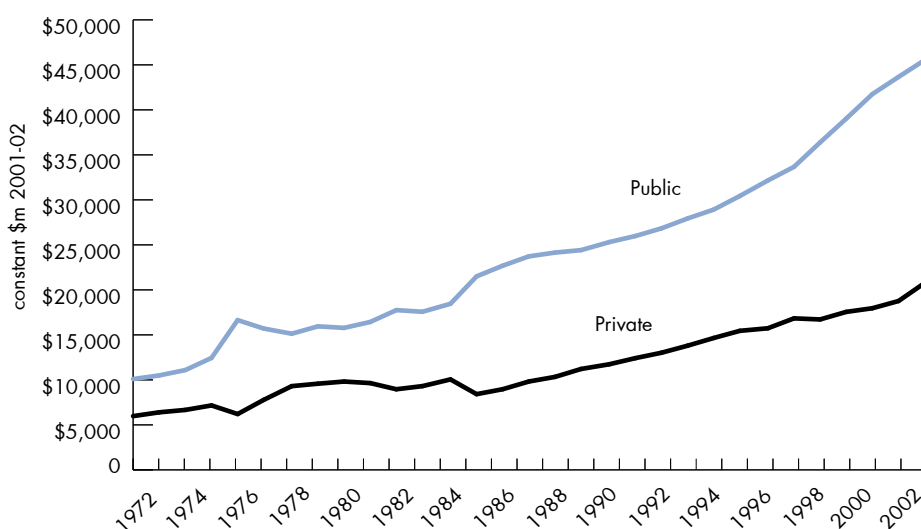
Expenditure Trends in Health

Under the Australian Constitution, the Commonwealth government's health responsibilities are limited to quarantine and war veterans. Over the years, however, the Commonwealth's health role has been greatly extended, both directly and by the centralisation of taxation. Thus, although health remains primarily a State and Territory responsibility, the Commonwealth government now intervenes directly through the pervasive Medicare and Pharmaceutical Benefits Scheme (PBS) in pharmaceutical, sickness and hospital benefits as well as in the provision of dental and medical services. The share of private in total health expenditures fell from 37% in 1971-1972 to 31% in 2001-2002.

On the positive side, Medicare and PBS have provided a floor of health care to all Australians. At the same time, patients' ability to choose among health care providers underpins the high quality of Australian health care. On the negative side, Medicare and PBS, by divorcing health services from health costs, have not always encouraged Australians to use health services responsibly. Medicare also fails to provide data that would enable the cost and quality of health procedures and institutions to be compared and thus put pressure on management for efficiency. Hopefully the *Eclipse* information system, to be introduced by the Health Commission, will simplify and facilitate this process.

Training limitations, restrictive practices and limited management skills have led to shortages of medical staff at all levels of medical practice, notably in outer suburban and rural areas. Specialists are in such short supply that though many work long hours, waiting times for their services can run into months. Shortages of nursing and other staff often mean that hospital beds cannot be fully used. Expensive equipment is rarely utilised to its potential. Greater efficiency would pay for more equipment and higher salaries without raising costs.

6.4 Public and Private Health Expenditure, 1972-2002



Source: Australian Institute of Health and Welfare, online datacubes, see www.aihw.gov.au

International Comparisons

In 2001 Australian health expenditures ranked in the middle of industrial countries in terms of the share of GDP (8.6%), the amount spent per person (\$3,397) and in the government share of total health expenditure (70%), but showed the fastest annual growth in health expenditure (4.6%) during the past decade.

Unfortunately these indicators do not shed any light on how health services meet the needs of their populations or the extent to which existing standards are sustainable. The United States, with the lowest government share of total health expenditures (44% in 2001), had the highest total health expenditure (13% of GDP). It has some of the most advanced medical facilities in the world, but this reflects the large size of its economy and its high per capita income, as well as the high proportion of private expenditures in health and health research funding. Health services for low income earners, generally not covered by employer (public or private) insurance, are notoriously inadequate. Nor has the large private insurance coverage resulted in greater fitness and health of the United States population.

The United Kingdom's predominantly public health system, at the other end of the public/private spectrum, is in crisis, with not only low, but also middle income earners shortchanged by overcrowded general practitioner (GP) services and months of waiting for hospital procedures. There is no ideal health system to which Australia can turn. It has to develop its own health standards and health policies.

6.5 International Health Expenditure Comparisons, 2001

	<i>Health expenditure as a % of GDP</i>	<i>Health expenditure per person A\$ (PPP*)</i>	<i>Real annual % growth in health expenditure 1991-2001</i>	<i>Government health expenditure as a % of total health expenditure</i>
Australia	8.6	3,397	4.6	67.8
Canada	9.4	3,741	3.8	71.7
France	9.3	3,432	3.6	76.2
Germany	10.5	3,763	n.a.	75.9
Japan	6.8	n.a.	4.1	78.4
Netherlands	8.5	3,519	4.0	68.0
New Zealand	7.6	2,322	4.0	77.8
Sweden	8.3	3,042	n.a.	86.5
United Kingdom	7.0	2,669	2.8	82.5
United States	13.1	6,549	2.9	44.1

* Purchasing Power Parity

Source: Australian Institute of Health and Welfare, *Health Expenditure Australia, 2001-02* (Canberra: AIHW, 2002).

Summary

Australians are extremely fortunate to have a climate and sporting tradition that encourages exercise, and excellent food for healthy and enjoyable eating. Australians must take advantage of this and care for themselves by adopting healthy lifestyles. Community values, advanced through the media, schools, civic organisations and private health insurance companies should play a vital role in promoting health. Check ups with opticians, dentists, and GPs are essential and freedom of choice in access to these services is the cornerstone of a quality system for both patients and practitioners. Illness can strike at any time, but as Australians age, we must expect to have to use advanced medical procedures more intensively. Medical insurance is thus both a responsibility and assurance of a comfortable old age.

Limitations on the training of health professionals, restrictive practices and poor management have created shortages in the health system. Although there has been much discussion of the inadequate remuneration for medical staff, it continues to lag, particularly in public institutions, and has led to increased staff shortages. Poor management, combined with an antiquated industrial relations structure, makes for such poor working conditions that nurses, in particular, leave public hospitals.

Innovation and technology continue to push back mortality when ill health strikes. Australia has contributed to the development of medical science and as one of the world's dozen wealthiest countries it can afford to access the latest medical technology. Greater efficiency and improvements in the management of scarce medical resources, notably in the more intensive use of high cost equipment, would ease rising costs.

Reducing the high costs of indemnity insurance is primarily a State responsibility because it reflects legal, not medical problems. Unless indemnity problems are addressed, Australia will lose medical capacity in key areas, notably obstetrics.

Australia can be proud of the health system, but rising costs will make the present structure untenable without steep taxation increases. Improving management and resource utilisation, particularly in hospitals, is essential for higher productivity. Australians must also take greater responsibility for their own health costs, raising the private component of total health expenditures for greater efficiency, a more equitable distribution of health resources and higher quality care for an ageing population.

7. WELFARE

PETER SAUNDERS

Introduction

Welfare (social security) is the biggest item in the public sector budget, followed by health, and both will become even more expensive in the future.

Like health, welfare spending is increasing with the ageing population because more people now live on the Age Pension for longer. But welfare spending on the working age population has also spiralled upwards since the 1960s. The proportion of adults aged 15 to 65 claiming unemployment assistance, disability benefits or single parent payment is at least five times higher than it was 40 years ago, and this upward trend shows no sign of reversing.

Perhaps the most extraordinary statistic is that the proportion of the working-age population living on the Disability Support Pension has more than doubled in 20 years—at a time when the general level of health and fitness in the population has been improving steadily.

Given that the two biggest public sector budget items are becoming more expensive in real terms every year, it is obvious that governments are going to face severe and mounting financial difficulties in the years ahead unless some of the cost can be taken up by individual consumers. The introduction of the compulsory Superannuation Guarantee has taken some of the pressure off the Age Pension, but not much. The demands and expectations crowding in on government spending continue to rise.

The rising financial cost of welfare is not the only reason to be concerned. Welfare dependency also affects quality of life, not only of adults, but also of children growing up in jobless households. As many of these are single parent households, children may never have a working role model and are more likely to become welfare dependent later in life, thus perpetuating the cycle.

The Ageing Population and the Future of the Age Pension

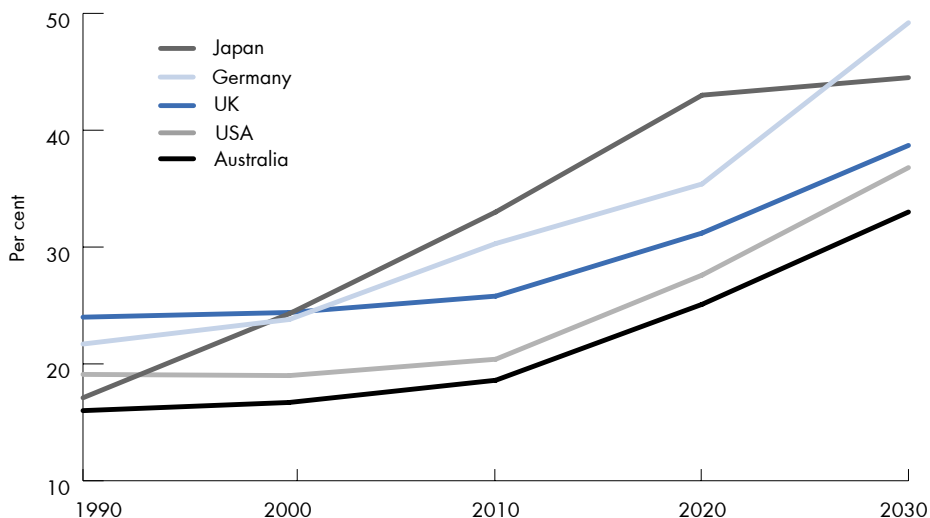
Over the next 30 years, most Western countries will have to cope with a much smaller proportion of working-age people supporting a much larger proportion of retired people. This trend towards an 'ageing population' has been caused by two main factors. Firstly, the post-World War II birth bulge (the so-called 'baby boomer' generation) is now approaching retirement. Secondly, the birth rate has dropped since the 1970s, so succeeding age cohorts are much smaller. The result is an increase in what demographers call the 'elderly dependency ratio' (the number of people of retirement age expressed as a proportion of the working age population).

Australia has a relatively young population compared with Europe and Japan. Our fertility rate has not fallen as far or as fast, and we continue to attract young migrants. Nevertheless, in 2030 there will be twice as many retired people for every worker as there were in 2000, and this will almost certainly mean a big rise in taxation.

Fortunately, Australia does now have in place a compulsory Superannuation Guarantee (SG) scheme which will take some of the pressure off the taxpayer funded Age Pension. However, the SG has not been running long enough to provide most baby boomers with an adequate retirement income, and the National Centre for Social and Economic Modelling predicts that the cost of the government Age Pension will rise from around \$10 billion in 1990 to nearly \$25 billion in 2030 to meet the shortfall.

7.1 Elderly Dependency Ratios, 1990-2030

Retirement age population as a proportion of working age population



Source: Simon Kelly, Ann Harding and Richard Percival, 'Live Long and Prosper?', Paper presented at the 2002 Australian Conference of Economists Business Symposium, available from the National Centre for Social and Economic Modelling website, see www.natsem.canberra.edu.au

Welfare Dependency Among Working-Age Adults

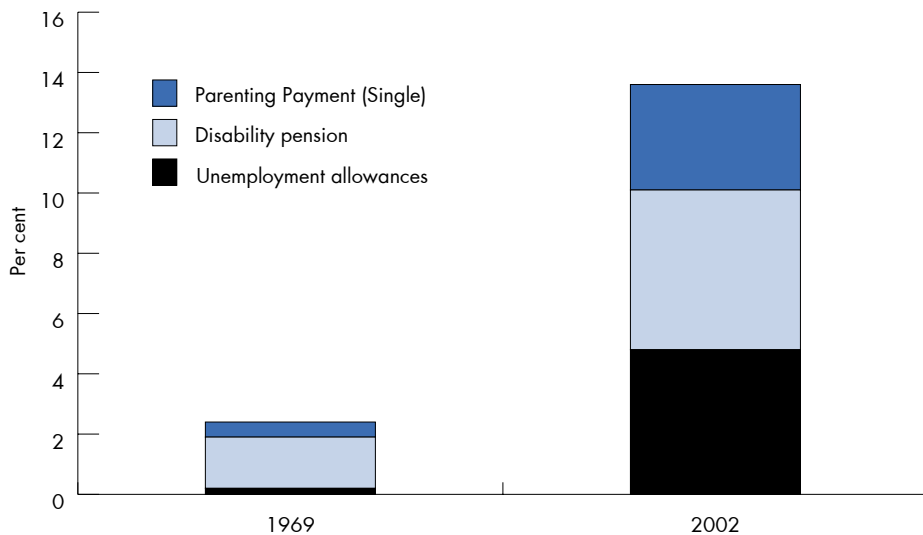
There has been a staggering increase in the proportion of the working-age population (15-64 years) reliant wholly or partly on Income Support payments. As recently as 1969, fewer than one in 20 adults below retirement age were drawing welfare payments. Thirty years later it was 21%, and still rising.

Not all of these people rely entirely on government handouts. In recent years it has become common for people to live on a mixture of wages and welfare benefits. But recent estimates suggest that about one in six working-age adults are dependent on welfare for at least 90% of their income.

Welfare dependency is concentrated in three main groups. First, the unemployed were a negligible proportion in the late 1960s, yet now at least 5% of all adults below retirement age are drawing unemployment allowances (Newstart or Youth Training). Second, 5% draw the Disability Support Pension. Although people are now healthier and live longer than ever before, the proportion of working-age adults receiving the disability payment has ballooned from 2% to 5% since 1980. Third, a large proportion of welfare recipients are single parents who claim Parenting Payment Single (see Figure 7.5, p.84).

7.2 Welfare Dependency, 1969 & 2002

Proportion of working-age population receiving unemployment, disability and single parent allowances



Sources: ABS, *Australian Social Trends 2001: Income and Expenditure, Income Support Among People of Workforce Age* (Canberra: ABS, 2002); ABS, *Yearbook Australia*, Cat. 1301.0 (Canberra: ABS, 2003).

Willingness to Work

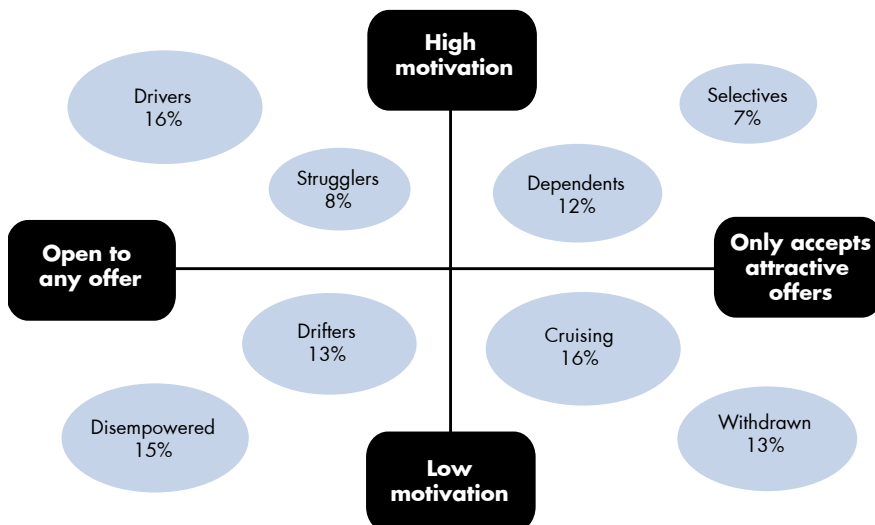
Half of those registering as unemployed find a job within eight weeks, but Department of Family and Community Services records suggest that more than half of those on unemployment allowances have been claiming benefits for more than a year.

Most unemployed Australians believe there are jobs available (only three in ten deny it),¹ but many are reluctant to accept jobs paying less than they earned previously, and two-thirds are unwilling to move within their own State or Territory to take a job.

Interviews with 3,500 jobseekers in 2002 found that only 16% were optimistic about finding a job and willing to take anything suitable (classified as 'drivers'). 'Strugglers' were motivated but lacked confidence, and 'selectives' and 'dependents' were people who wanted to find work but who were picky about what they would accept. 'Drifters' didn't know what they wanted and the 'disempowered' had given up looking, while 'cruisers' had no desire to get off welfare, and the 'withdrawn' claimed they were incapable of working.

This study suggests that over half of those on unemployment assistance are not actively searching for work. These findings are consistent with American policy analyst Lawrence Mead's argument that claimants may need 'hassle' as well as 'help' if they are to move from welfare to work.

7.3 Orientation to Job Search of People on Unemployment Allowances, 2002



Sources: Colmar Brunton Social Research, *Job Seeker Attitudinal Segmentation: An Australian Model* (report for the Department of Employment & Workplace Relations, 2002); and Labour Market Policy Group, *Job Seeker Attitudinal Segmentation* (Department of Employment & Workplace Relations, May 2002).

The Disability Support Pension

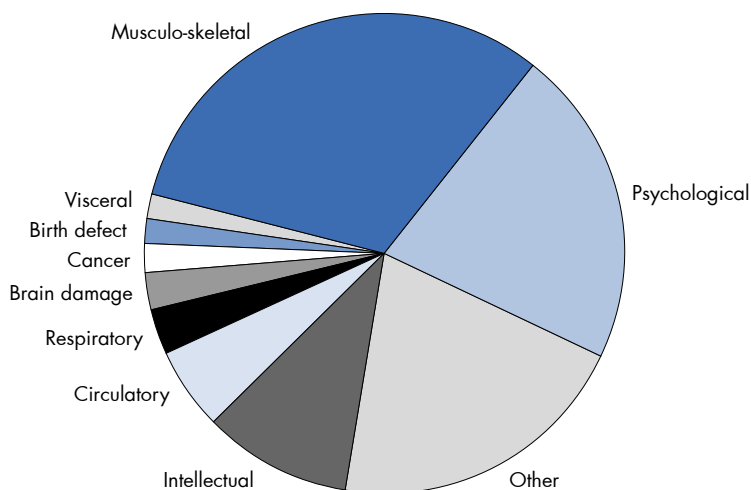
Australia's social security system provides a considerable incentive for unemployed people to have themselves reclassified as 'disabled'. Unlike the unemployed, people on Disability Support Pension (DSP) are not required to undertake any mutual obligation activities, receive a higher rate of payment and are subject to a more lenient income test. They also get left alone (once on the DSP, they normally stay there through to retirement age and the Age Pension).²

Half of all disability pensioners have moved directly from the unemployment rolls where they experienced an average of more than one year on unemployment benefits before transferring.³ While some do suffer from major impairments, many could be supporting themselves by working. A majority suffer from bad backs ('musculo-skeletal' problems) or depression—conditions that are difficult to assess and which rarely rule out any future employment.

The switch from unemployment into disability payments has been happening throughout OECD countries. Some European countries (notably the Netherlands and the Scandinavian nations) have much higher levels of disability payment dependency than we do—8% to 9% of working-age adults compared with our 5%. This explains how these countries have managed to get their unemployment figures down: they have simply shifted their long-term unemployed workforce onto disability payments.

7.4 Disability Support Pension Recipients, 2000

Main disability recorded



Source: ABS, *Australian Social Trends 2002: Income and Expenditure, Income Support, Trends in Disability Support* (Canberra: ABS, 2002).

Single Parents and Welfare Dependency

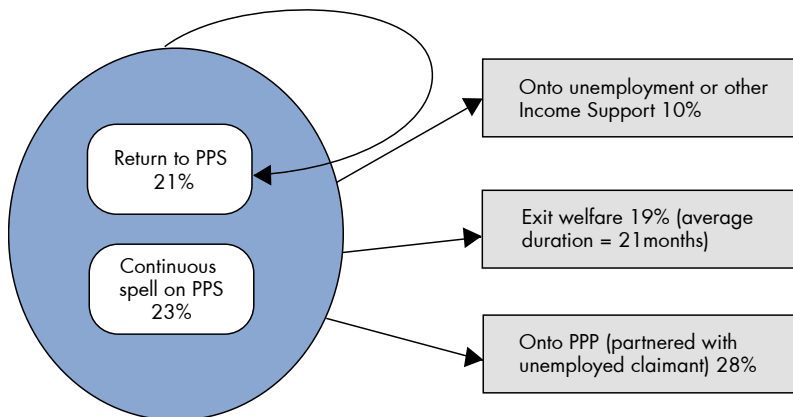
The proportion of working age women receiving the single person's Parenting Payment (PPS) has risen from 1% to 6% since 1969. One in ten of Australia's single parents claim no government benefits at all, but one in three have no income other than their welfare payment, and another 20% rely on welfare as their principal source of income.

Australia is one of only a handful of Western countries that allow single parents to stay on welfare until their youngest child reaches school leaving age. Because the average duration of each PPS claim is only two years, it used to be thought that claimants were moving swiftly through the welfare system. But this is not the case. Professor Bob Gregory has estimated that PPS claimants remain on benefits of some kind for an average of 12 years. Many of those who leave PPS simply exchange one kind of benefit for another (for example, they meet an unemployed partner and switch to partnered Parenting Payment, PPP). Three-quarters return to welfare within six months of leaving PPS (43% are back within one month).

Allowing sole parents to stay on benefits for an average of 12 years is expensive for taxpayers, unfair on working parents (who often have to work to make ends meet), and counterproductive for claimants and their children. Welfare dependent parents lose their vocational skills and their work habits and become habituated to a life on benefits, and their children may suffer by never seeing a working adult role model.

7.5 Parenting Payment, January 1995

What happened over the next 66 months to sole mothers on Parenting Payment



Source: Bob Gregory, 'The Impact of Continued Labour Market Change on Families', Keynote Address to Australian Institute of Family Studies Conference (Melbourne, 2003).

Expenditure on Welfare

Social security and welfare expenditure represents the biggest item in the public sector budget. Government welfare spending (most of it Federal) absorbs more than 10% of the nation's GDP.

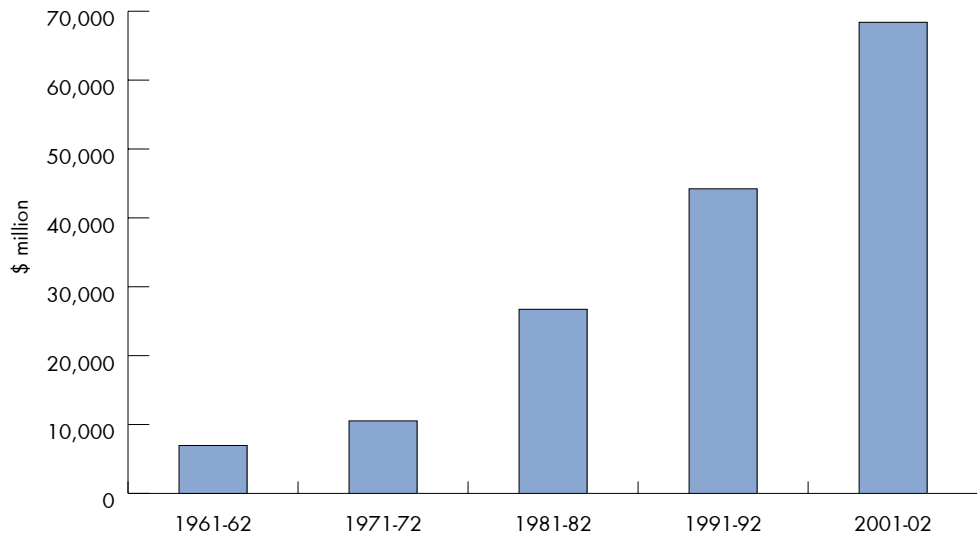
Figure 7.6 shows that welfare spending was almost ten times higher in real terms in 2002 than it was in 1962. The population did not even double over the same period. This means that real per capita expenditure on welfare increased fivefold.

The ageing population helps to explain why social security and welfare spending is going up—more people are living longer on the Age Pension. But this is not the main factor. As we have seen, payments to working age people have risen much faster.

Assistance to the aged is expected to absorb \$26 billion in 2003-2004. Payments to support low income parents and to aid with the costs of raising children will cost another \$20 billion. Disability support takes up \$9 billion, and unemployment assistance accounts for a further \$6 billion. The Federal government's social security and welfare budget in 2003-2004 is estimated at more than \$60 billion.

7.6 Welfare/Social Expenditure, 1961-2002

Real annual government expenditure, 2000, A\$ millions



Source: ABS, *Yearbook Australia*, Cat. 1301.0 (Canberra: ABS, 2003).

Public Support for Reform

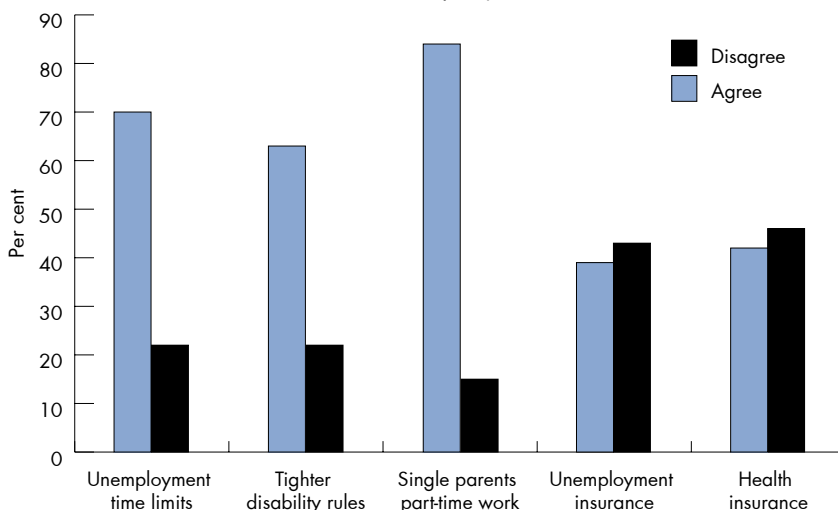
Public opinion surveys carried out during 2003 solicited people’s views on a series of reform proposals affecting health and welfare:

- *Time limits on unemployment benefits:* People were asked their views on a proposal to limit unemployment benefits to a period of six months, after which claimants would be expected to participate full-time in a ‘Work for the Dole’ scheme until they find a job.
- *Tighter eligibility rules for disability payments:* People were asked if they agree or disagree that we should tighten up the rules for deciding whether somebody can claim a Disability Pension.
- *Work requirements for sole parents:* People were asked when they think it is reasonable to expect a sole parent to go out to work part-time once their youngest child starts primary school (current PPS rules allow a parent to stay on benefits until the youngest child leaves school).
- *Privatisation of unemployment and sickness insurance:* People were asked to respond to a proposal that current unemployment and sickness benefits should be replaced by private unemployment and sickness insurance. Taxes would be reduced accordingly, and the government would help pay the premiums for people on low incomes.
- *Privatisation of medical insurance:* People were asked for their views on replacing Medicare with private health insurance. Again, taxes and levies would be reduced and the government would help pay the premiums for families on low incomes.

The results of these surveys indicate strong public support for reforming welfare benefits but less support for replacing government health and unemployment schemes with private insurance.

7.7 Public Opinion on Welfare Reform Proposals

Per cent of survey respondents



Source: ACNielsen survey data conducted on behalf of CIS.⁴

Summary

The Australian welfare state (including the socialised system of health care funding) evolved late by international standards. The irony is that the Federal government took on responsibility for providing these things at precisely the time when ordinary people were reaching a point where they could have supported themselves.

If the government did not tax so heavily to pay for services and to cover our incomes after retirement or during unemployment, most of us could afford to meet these costs ourselves. If the government topped up the purchasing power of those on the lowest incomes, we could be left to save for old age and to insure against loss of earnings through sickness and unemployment.

Because we have grown used to the government providing these things for us, many are sceptical about proposals aimed at enabling us to make our own arrangements. But a crisis is building in the funding of welfare benefits, and radical changes are needed to avoid a huge blowout in costs.

In the short term, considerable sums could be saved by tightening up eligibility for payments. One billion could be saved every year if sole parents went back to work part-time once their children start school. Two billion could be saved annually by time limiting unemployment assistance, and the same again by ensuring that access to disability payments is limited to those who really cannot work.

In the longer term, however, as with health, the funding of welfare benefits needs to change so that individuals and families take more responsibility and assume greater control of their incomes. The Australian welfare state is a mass solution to problems of need and deprivation that no longer occur on a mass scale.

8. POVERTY, TAX & INCOME DISTRIBUTION

PETER SAUNDERS

Introduction

We should not confuse poverty with income inequality. Poverty is about having insufficient money to maintain an adequate standard of living. Inequality is about having less money than somebody else.

Poverty is inherently a bad thing. Nobody in an affluent country like Australia should be living in poverty, least of all children. How many Australians (if any) are living in poverty is contested—estimates vary according to how we define an ‘adequate’ living standard.

Welfare groups often overstate their poverty estimates to put pressure on the government to increase taxes on higher earners and redistribute more money to people on welfare. But this agenda has more to do with reducing inequality than with reducing poverty.

Many academics and activists think income inequality should be reduced because it is threatening Australia’s traditional belief in a ‘fair go’. But this naively assumes that inequality is inherently unfair. A ‘fair go’ is about rewarding effort. If one person works harder than another, for example, few of us would think it unfair that they end up with a higher income. Unlike poverty, therefore, inequality is not necessarily a bad thing, and we should be wary of those who conflate the two.

Those who demand higher taxation to narrow the gap between higher and lower income groups claim that Australian taxes are low compared with other countries, but this is not the case. Tax rates have fallen, but ‘bracket creep’ means that most of us are paying higher taxes today than ever before.

The paradox in all this is that, far from relieving poverty, high taxation drives low-wage workers below the poverty line, and the government then has to bale them out with extra welfare payments. The government ends up taking money from people with one hand, and giving it back to the same people with the other.

Poverty in Australia

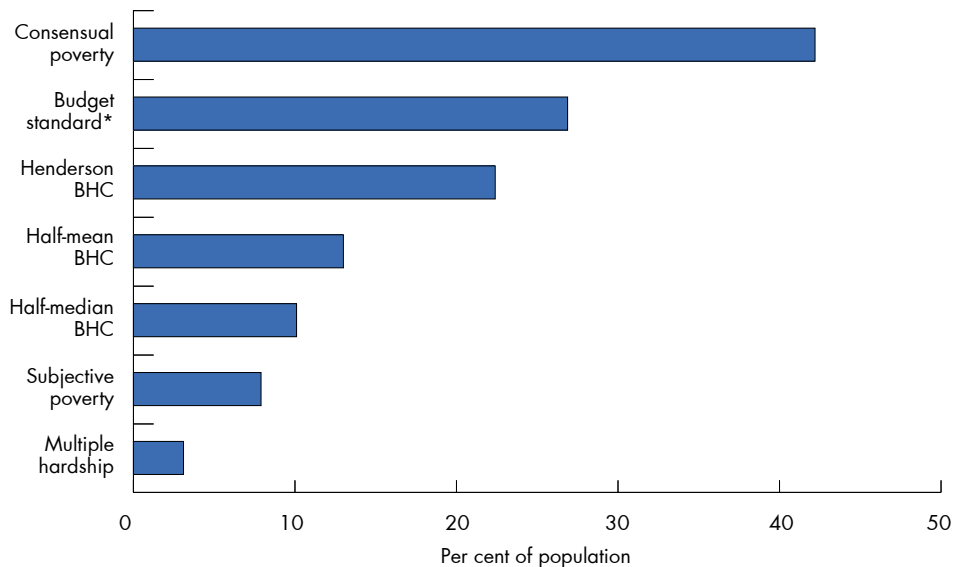
Compared with many people in developing countries, nobody in Australia is ‘poor’. However, poverty researchers argue that many Australians can still be seen as poor if they live below a standard that others think of as normal. But how do we define ‘normal’? Depending on the measure they adopt, researchers estimate the poverty rate at somewhere between 3% and 42% of the population.

The tightest definition (‘multiple hardship’) looks at people who have gone without food or heating, have pawned or sold something, or have sought help from charity organisations. The most generous definition (‘consensual poverty’) works out how many people have an income below what a sample of the public thinks is required to make ends meet.

Figure 8.1 includes these and five other poverty indicators. ‘Subjective poverty’ measures the number of people who say they do not have enough to get by on. The ‘half-mean’ and ‘half-median’ measures draw a poverty line at half of what the average or middle-ranking Australian receives (before housing costs). The ‘Henderson poverty line’ is supposed to define a basic minimum living standard, but it has become hopelessly inflated. Researchers at the University of New South Wales have tried replacing it with a new ‘budget standard’, but this is even more generous than the Henderson line.

The basic conclusion is that poverty is a highly politicised and essentially contestable concept. All poverty measures should be treated with extreme caution.

8.1 Seven Different Measures of Poverty Rates



* estimated at an average of 1.2 times Henderson, BHC= before housing costs

Sources: Ann Harding, Rachel Lloyd and Harry Greenwell, *Financial Disadvantage in Australia 1990 to 2000* (Sydney: The Smith Family, 2001); Peter Saunders, *The Ends and Means of Welfare* (Sydney: Cambridge University Press, 2002); Peter Saunders, ‘A New Poverty Line’, *SPRC Newsletter* No.69 (Sydney: UNSW, May 1998); Rob Bray, *Hardship in Australia*, Occasional Paper No.4 (Canberra: FaCS, 2001).

The Adequacy of Welfare Benefits

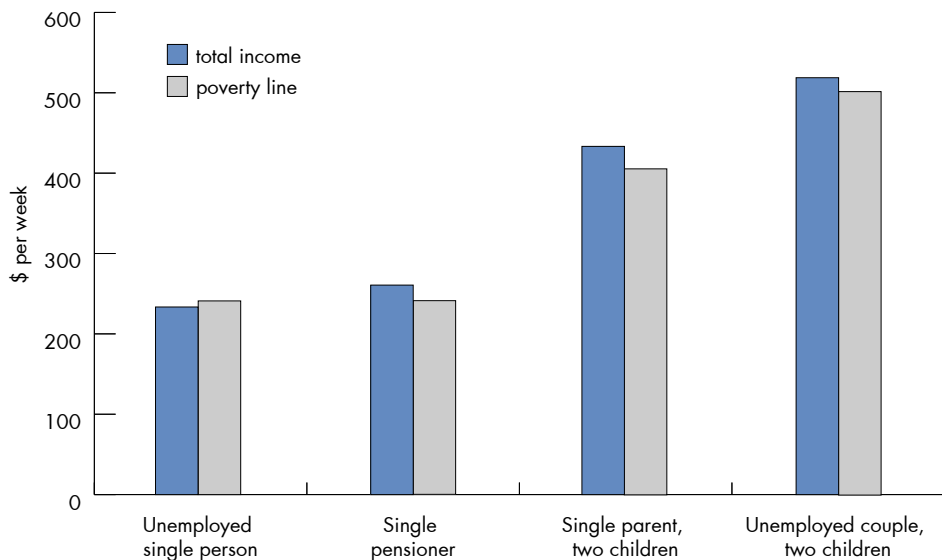
The Henderson poverty line was developed in the 1970s to measure the minimum income required by various household types to maintain an acceptable standard of living. Over the years it has become increasingly generous because of the way it has been adjusted with inflation. Today it would buy 37% more than it would have done in 1973.

If the value of welfare payments are compared with the inflated Henderson poverty line, in nearly every case, the total value of the benefits to which claimants are entitled (their allowance or pension, plus partner's allowance, Family Tax Benefit and rent assistance) is above the Henderson line.

This does not mean that people on welfare are well off—they are not—but it does indicate that the welfare system pays them enough to stay out of poverty (even when 'poverty' is generously defined).

Given that welfare levels are above the poverty line, and that minimum wages are well above welfare benefit levels, why do surveys still report that millions of Australians are in poverty? Part of the explanation is that people under-report their incomes in surveys or spend their money unwisely. Poverty sometimes has more to do with lifestyle than income.

8.2 Welfare Payments Compared With the Henderson Poverty Line, 2003



Source: Melbourne Institute of Applied Economic and Social Research, *Poverty Lines: Australia* (Melbourne: University of Melbourne, March 2003).

Poverty and Joblessness

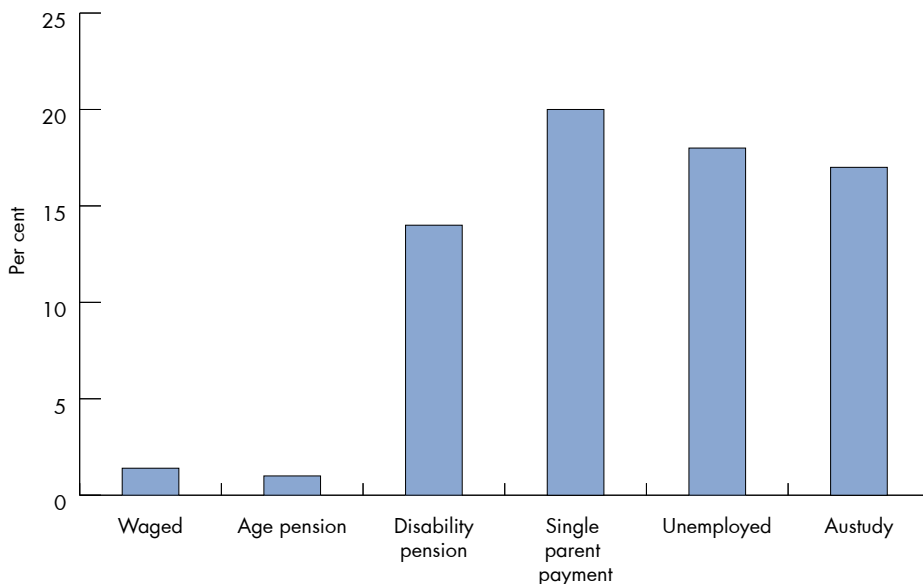
No matter how poverty is defined, its principal cause is always joblessness. Defined tightly (as ‘multiple hardship’), only 1% of households whose main source of income is a wage or salary are ‘poor’. This compares with between 14% and 20% of households living on welfare benefits. Even when poverty is defined more expansively (as below half the average income), a recent Smith Family report found that only 3% of households whose main source of income is a wage or salary are ‘poor’, as compared with 31% of those living on benefits.

The trade unions like to claim we have a serious problem of ‘working poverty’ in Australia, but people in full-time employment are rarely poor (not surprising considering Australia’s minimum wage is one of the most generous in the OECD, see Figure 9.5, p.112). Low income or ‘poor’ households are overwhelmingly those where no adults of working age are employed.

Given that the poorest sections of the community are those reliant on welfare benefits, it might be concluded that the best anti-poverty strategy would be to raise the value of benefits. But the more generous the benefits, the weaker the incentive of those on welfare to get a job, and the heavier the tax burden on workers who are trying to get by without government handouts. A far better solution is to get more people off welfare and into employment. That requires labour market reform (to generate more jobs) and tax and welfare reform (to improve work incentives).

8.3 Poverty and Principal Source of Household Income, 1998

Percentage of households suffering ‘multiple hardship’



Source: Rob Bray, *Hardship in Australia*, Occasional Paper No.4 (Canberra: FaCS, 2001), Table 15.

Income Tax Burden: International Comparisons

People demanding higher government spending often claim that taxation in Australia is low compared with other advanced OECD countries.

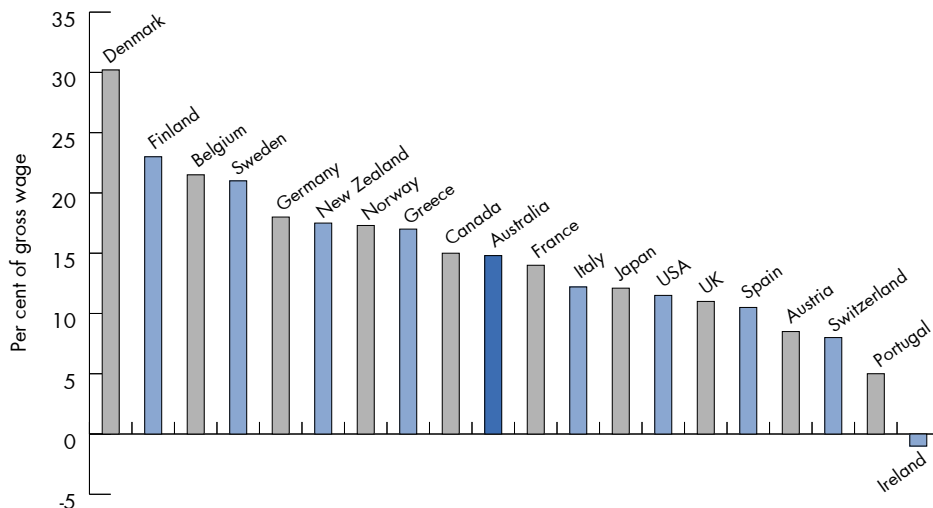
It is true that total taxation as a proportion of GDP is relatively low in Australia (31.5% as compared with an OECD average of over 37%), but this is mainly because indirect taxes are lower. Taxes on company profits are actually higher in Australia than in any other OECD country.

To compare the taxes that people in different countries pay on their wages, the social insurance contributions levied in other countries has to be taken into account as well as the cash transfers that people receive from their governments. The end result shows Australia at around the middle of the international rankings.

An American, British, French or Japanese couple with two children living on one average wage retains a higher proportion of their earnings than an equivalent Australian family who lose about 15% after deductions and benefits. However it could be worse—they could be living in Denmark!

8.4 Total Taxation of Family of Two Adults and Two Children on Average Wage, 2002

Net income tax and social security deductions
(after receipt of cash benefits) as a percentage of gross wage



Source: OECD, *Taxing Wages 2002* (Paris: OECD, 2003)

Bracket Creep

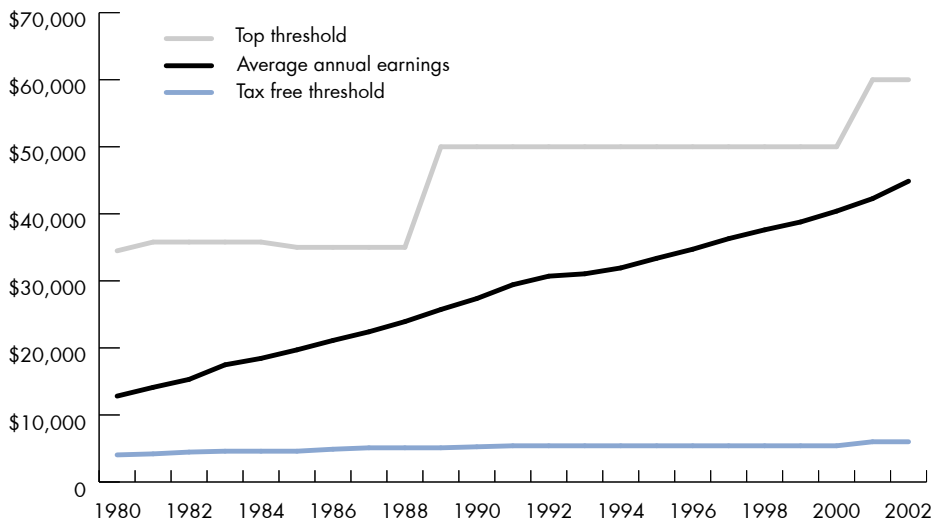
The amount of tax that people pay on any given income depends on two things—tax rates and tax thresholds.

Tax rates have declined in Australia over the last 20 years yet most people are losing a bigger slice of their incomes to the government than they were before. This is because tax thresholds have not kept up with inflation. Figure 8.5 shows that people in 1980 did not start paying the top rate of tax (which was then 60%) until they earned around \$35,000—nearly three times the average income. Today, however, the top rate (47%) is paid on earnings just one-third higher than the average.

This ‘bracket creep’ has also affected the basic rate of tax. In 1980, there was no tax at all until earnings reached \$4,041 per year (one-third of average earnings). Wages have gone up by 350% since then, but this tax-free earnings threshold has only risen by around 50%, to less than one-seventh of today’s average earnings. Every worker now therefore pays tax on a much bigger proportion of their earnings than they used to.

Because it takes so much tax from low earners, the government has to top up their incomes with increased welfare payments. The tax system today drives people into poverty and then the welfare system has to bale them out.

8.5 Tax Thresholds and Average Earnings, 1980-2002



Source: Bendzulla Actuarial Pty Ltd website (www.bendzulla.com.au)

Tax Freedom Day (TFD)

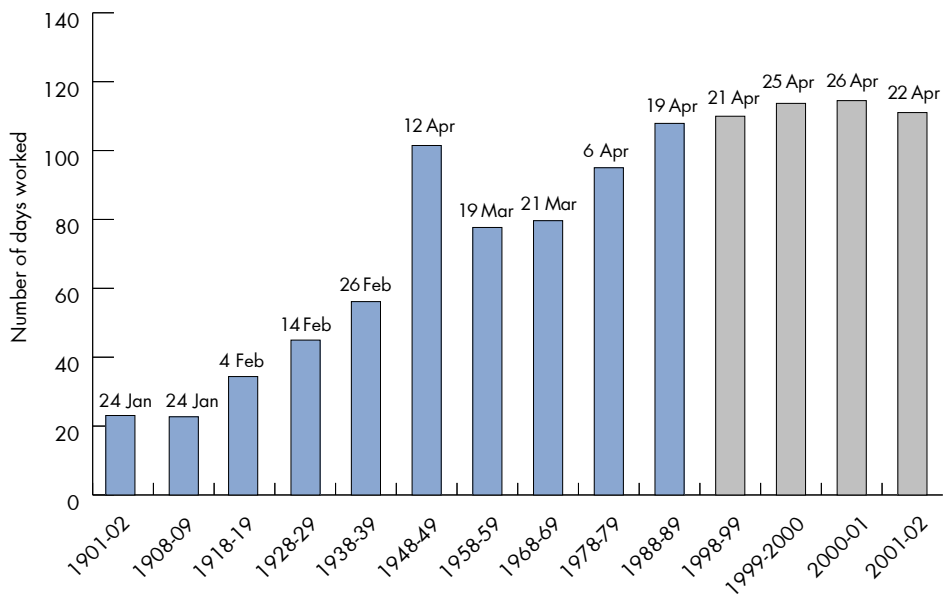
In feudal Europe, serfs had to work for their lord for a certain number of days each year, looking after his land or fighting his wars. For the rest of the year, they could work to meet their own needs.

In modern societies, workers still have to put in a number of days each year without payment, the difference being that now it is not the landed aristocracy that absorbs the product of our labours, but the government. One hundred years ago, this was a small price to pay, for governments stuck to the essential tasks, and the nation's tax bill was kept small. But as governments have extended their powers and responsibilities, so their impost has escalated. Most years, regardless of the political party in government, the tax take as a proportion of the nation's GDP gets bigger. Australians today work for almost four months every year to pay for the government's spending before they start earning money for themselves.

Data in Figure 8.6 cannot be compared with measures of TFD used by other countries (as they are not always calculated the same way). In its calculations, the OECD includes all government revenues which makes TFD 16 May in 2002 and a day earlier in 2003.¹

8.6 Tax Freedom Day, 1901-2001

Symbolic day of the year when the total national tax bill has been paid



Note: Grey bars indicate data that has been recalculated since *State of the Nation 2001*.

Source: ABS, *Yearbook* Cat. 1301.0 (Canberra: ABS, 2003).

Taxes or Services: What Do People Want?

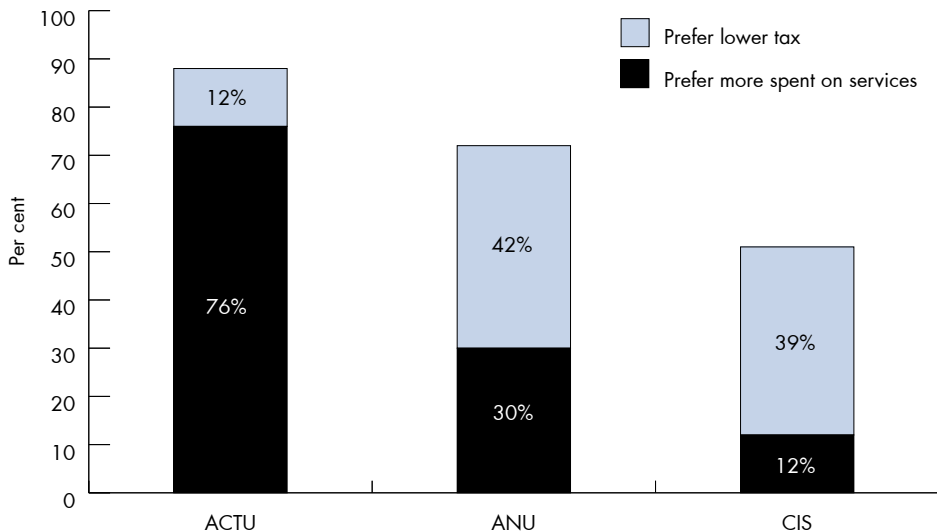
The Australian Council of Trade Unions (ACTU) ran a survey in 2003 asking people whether they would prefer to have a tax cut or see the money spent on schools and hospitals instead. Three-quarters of the people surveyed said they would prefer the government to spend the money rather than receive a tax cut.

Note that the ACTU survey asked if people wanted current levels of government spending reduced to pay for tax cuts. In a different survey at around the same time, political scientists at the Australian National University (ANU) asked people to choose between lower taxes and higher spending on social services, and a majority opted for tax cuts. Although ACTU leaders claimed that their survey had shown that people support higher government spending, the ANU survey demonstrates this is not the case.

Nor do people want to pay higher taxes to fund more spending. A third survey conducted in 2003 by The Centre for Independent Studies (CIS) gave people the choice between higher spending and higher taxes on the one hand, or lower spending and lower taxes on the other. Just one in eight chose more government spending when it was explicitly linked to higher taxes.

8.7 Public Opinion on Taxes and Social Expenditure, 2003

Per cent of respondents in three different surveys



Sources: ACTU website, see www.actu.asn.au; Shaun Wilson and Trevor Breusch, 'Taxes and Social Spending', *Australian Journal of Social Issues* 38 (2003); CIS ACNielsen survey data (see Chapter 7, endnote 1, p.158).

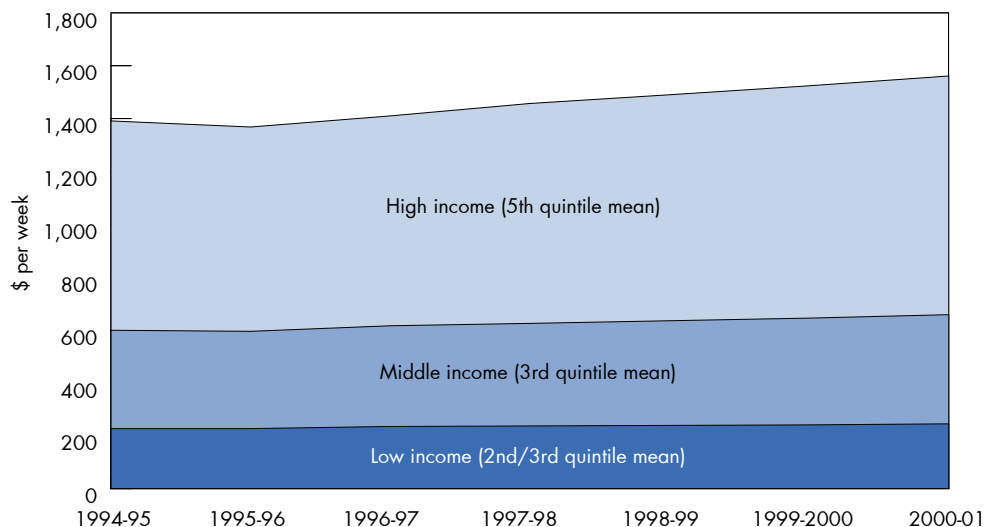
Income Distribution

The Australian Bureau of Statistics (ABS) carries out surveys to estimate the weekly incomes enjoyed by households after taxes have been paid and government cash benefits have been received. These surveys are plagued by problems, particularly households claiming to have the lowest incomes (those in the bottom 10%). Many of them claim to have zero or even negative incomes, and on average they spend three times more than they say they receive. The ABS therefore disregards this bottom group and defines 'low income' households as those in the second and third deciles (where expenditure is actually lower than in the first decile).

Obviously a single person household receiving \$1,000 per week is better off than a family of two adults and two children who receive the same amount. To account for this, the ABS adds together all the income received by the members of a household and then deflates this total to account for the number of adults and children who have to live off this income. The result is the household's 'equivalised' income.

Over the last ten years, 'real' incomes have gone up across the board (that is, everybody is now better off), but higher earners have fared best. Between 1994-2000, top incomes rose by 14% in real terms compared with a 12% rise in middle incomes and 8% growth in low incomes. The Gini Coefficient, used to measure inequality, increased very slightly over this period from 0.30 to 0.31. The main reason for this slight rise in inequality is that wages and salaries went up faster than welfare benefits. Given the need to strengthen work incentives, this is not a bad outcome—everyone is better off but those in work have done best.

8.8 Real Equivalised Disposable Household Incomes, 1994-2001



Source: ABS, *Household Income and Income Distribution*, Cat. 6523.0 (Canberra: ABS, 2003).

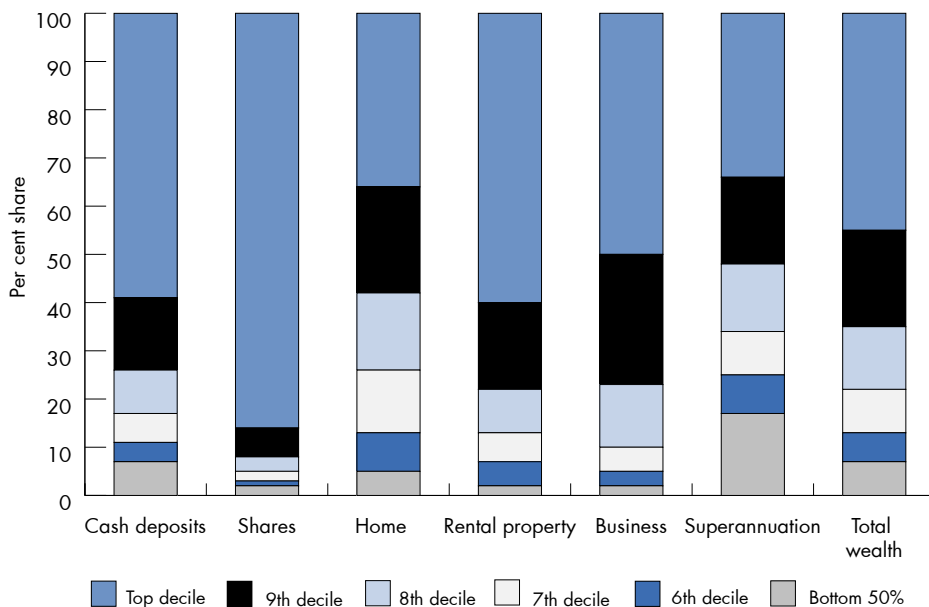
Distribution of Wealth

It is much more difficult to estimate people’s wealth (their asset holdings) than their income. The statistics from which this chart has been compiled are based on the sources of income that people report in surveys. For example, if somebody says they receive \$X per week in rent, or \$Y per year in dividends, then it is possible to make an approximate assessment of how much rental property they own, or how many shares they have. But these estimates are very rough.

Clearly wealth is much more unequally distributed through the population than income. The bottom quintile of wealth distribution owns virtually no income generating assets, and the poorest half of the population owns only 4% of the nation’s assets. The richest 10% of people own 45% of all the wealth.

The two biggest asset categories are, however, those in which ordinary people are most likely to have a stake. Around 40% of personal wealth is made up of owner occupied housing and since compulsory superannuation was introduced in the late 1980s, super funds have grown to account for another 20%. As superannuation builds up, so wealth may become a little more equally distributed in the future, and some politicians are now looking for other ways in which ordinary people can be helped to accumulate wealth in their own personal lifetime accounts.

8.9 Ownership of Key Assets, June 1998



Source: Ann Harding, ‘Trends in Income and Wealth Inequality in Australia’, Paper to the Economic and Social Outlook Conference (Melbourne, 2002).

Fair Shares

We often hear about the Australian belief in ‘a fair go’, but what exactly does this mean?

Socialists and egalitarians in the universities, the media and the policy community who spend their time writing and campaigning about income distribution assume it means equal outcomes. But a moment’s thought should alert us to the fact that equal shares can often be very unfair.

Is it ‘fair’, for example, if you work much harder than I do, but the tax system is used to reduce your final income to the same level as mine? Is it ‘fair’ if you and I freely agree to trade some good or service, but any profit we make is then taken away to ensure that we are no better off than other people who did not make this trade?

Clearly, there are different notions of ‘fairness’. A 2003 survey of the Australian public found the strongest support (85%) for the idea of fairness as the rewarding of talent and effort (that is, meritocracy is fair). Fairness as the result of market transactions was endorsed by 60%, and only one-third of respondents thought fairness requires that nobody gets a lot more or a lot less than anybody else (fairness as equality). Interestingly, most people gave mixed answers, yet these three conceptions of fairness are to a large degree incommensurable.

Australians do believe in fairness, but they do not assume this translates as equality.

What People Think Is ‘Fair’

Percentage of survey respondents who agreed with the following statements

In a ‘fair’ society...	Agree	Disagree
<p>Meritocracy is fair <i>People’s incomes should depend on how hard they work and how talented they are</i> (Meritocracy is the only fair principle = 24%)</p>	83%	6%
<p>Market is fair <i>People’s incomes should depend on how much other people value the services they provide</i> (Market is the only fair principle = 2%)</p>	60%	26%
<p>Equality is fair <i>Nobody should get an income a lot bigger or a lot smaller than anyone else.</i> (Equality is the only fair principle = 5%)</p>	34%	55%
<p>None of the three principles is fair</p>	5%	

Source: Public opinion research conducted for the Centre for Independent Studies by ACNielsen, July/August 2003.

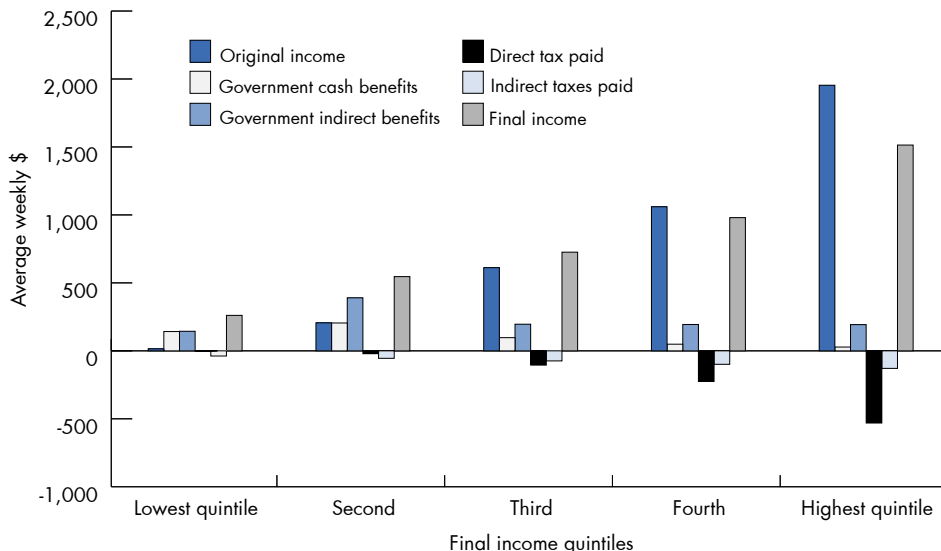
Redistributive Effects of Tax and Welfare (One Point in Time)

Our standard of living is determined by our 'final income'. This is made up of original income (what people receive before the government intervenes), plus cash benefits received from the government, plus the value of services like health and education provided by the government, less the direct and indirect taxes paid to the government.

Original incomes are very unequally distributed but government pensions and allowances narrow the gap. So does direct taxation, most of which is paid by the top quarter of income earners. Everybody pays indirect taxes (although higher income groups tend to pay more because they buy more), and everybody receives indirect benefits (but these make a bigger proportional contribution to the living standards of those on lower incomes).

Although the means tested, non-contributory system of welfare benefits targets people in need of income support more effectively than many overseas systems do, it is still the case that every year, substantial numbers of Australians pay taxes out of one pocket while receiving benefits in the other. Figure 8.11 shows that across the second, third and fourth quintiles of final income, people are receiving government payments at the same time as they are paying income tax. This can create serious disincentive effects, for as original income rises, taxes go up and welfare benefits go down, a double whammy that can lead to 80 cents or more in every new dollar disappearing before it is received.

8.11 Composition of Final Income, 1998-1999



Source: ABS, *Government Benefits, Taxes and Household Income*, Cat. 6537.0 (Canberra: ABS, 2001).

The Redistributive Effects of Tax and Welfare (Lifetime Analysis)

Most people are relatively affluent at some periods in their lives (for example, after children have grown up and both partners are working) but are relatively poor at others (while studying or when one partner gives up work to look after a new baby). Money flows over time show that net recipients at one time often become net payers at another.

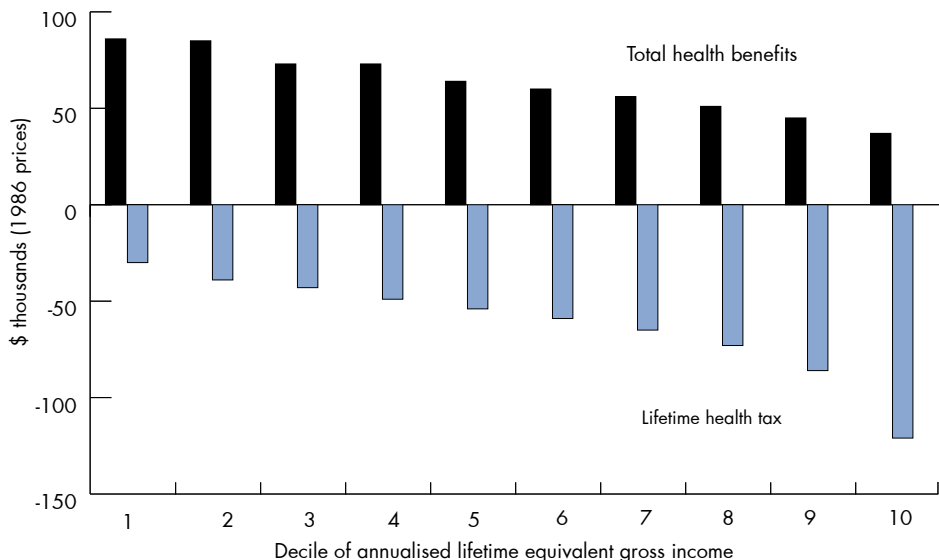
Much of the money we pay out during the affluent periods we receive back in the poorer periods. Seen in this light, the tax and welfare system functions more like a gigantic government piggy bank than a benevolent Robin Hood. Ann Harding of NATSEM concludes: ‘A significant proportion of income taxes paid during the lifetime are returned to the same individuals in the form of cash transfers during some other period of their lifecycle’.

It might make more sense if the government reduced taxation so people can buy the services they need through personal savings and insurance, and topped up the purchasing power of the poorest groups. This would be more efficient and it would allow individuals to choose their own service providers.

Figure 8.12 illustrates income churning over a lifetime using the example of health taxes and benefits. On average, people pay for three-quarters of what they receive.

8.12 Health: What People Pay and Receive Over a Lifetime

Dollars paid out (lifetime health tax) and value of benefits received (total health benefits)



Source: Ann Harding, Richard Percival, Deborah Schofield, Agnes Walker, ‘The Lifetime Distributional Impact of Government Health Outlays’, *Discussion Paper No.47* (Canberra: NATSEM, February 2000).

Summary

To the extent that there is a problem of poverty in Australia, its principal cause is joblessness. When lobbyists demand that government tackle poverty by increasing taxes on those who are better off and increasing welfare benefits for those who are worst off, they are focusing on outcomes rather than causes. Their proposals would make things worse rather than better.

The best way to reduce poverty is to get more people into employment, and one part of a strategy to achieve this is to increase the rewards for working. The argument that taxes on wages should be increased and welfare benefits expanded for those who do not work has everything upside down—it would lead to fewer people in work and higher poverty rates.

Between 2000-2002, 19 OECD countries reduced the total taxes levied on people's incomes. Even under a right-of-centre Federal government, however, Australia continued to increase them. An average worker with spouse and two children now loses a bigger slice of gross earnings than his or her counterpart in France, Italy, Japan, the United Kingdom or the United States. Higher up the income scale, the top rate of tax starts at A\$83,000 in France, A\$84,000 in the UK, A\$98,000 in Germany, A\$115,000 in Canada and A\$549,000 in the US. In Australia, it cuts in at just A\$60,000. Yet academics and activists still say this is too generous.

If poverty is going to be reduced, unemployment lowered and living standards raised, there needs to be radical reform to reduce taxes on wages and salaries. For a start, the tax free earnings threshold should be restored to its 1980 level (about \$14,000 in today's money) and the top rate of tax should be cut. As seen in Chapter 7, this can partly be funded by rolling back the welfare juggernaut which has careered out of control.

9. LABOUR MARKET

KAYOKO TSUMORI

Introduction

In October 2003, Australia's unemployment hit 5.6%, a 22 year low. It rose slightly to 5.7% in January 2004, yet the proportion of the unemployed who have been out of work for over a year remains alarmingly high, and there remains every reason to be cautious.

Unemployment arises when the number of jobseekers (labour supply) exceeds the number of job vacancies (labour demand). Experience across industrial countries suggests that an important determinant is labour market regulation, a set of laws governing employment, such as statutory minimum wages, firing restrictions, and bargaining rules. Heavy labour market regulation makes hiring costlier and more cumbersome and deters employers from recruiting. Job shortages may result. Jobseekers with few skills—school leavers, for instance—are the most adversely affected.

Many European industrial countries once enjoyed low unemployment under strict labour market regulation. However, few coped well with economic downturns. Their unemployment rates 'ratcheted up' after every global recession, resulting in chronic high employment. Amid a growing recognition of the urgent need for reform, many OECD countries in the 1990s embarked on creating a less regulated, more flexible labour market.

The move toward labour market deregulation in Australia dates back further, but the most important changes occurred in the 1990s. Previously, pay and conditions for the overwhelming majority of employees were prescribed in an industry or occupational 'award', a legally enforceable document made and varied by industrial tribunals. Individual enterprises were not afforded much discretion in, for example, adjusting wages to their respective financial circumstances. Toward the end of the 1980s, it was increasingly acknowledged that the award system was hindering productive operations of many enterprises. Thus, bargaining at enterprise levels was approved by the federal industrial tribunal in October 1991 and was then enshrined in the Industrial Relations Reform Act 1993. Enterprise bargaining was further facilitated by the Workplace Relations Act 1996.

Labour market performance has been improving, and there is little sign that employee welfare has deteriorated as a result of the move away from the award system. However, industrial relations reform to date remains unsatisfactory.

Labour Force Participation Rates

‘Labour force participants’ are those who are in work and those who are out of work but seeking a job. Those who fall under neither category are ‘not in the labour force’.

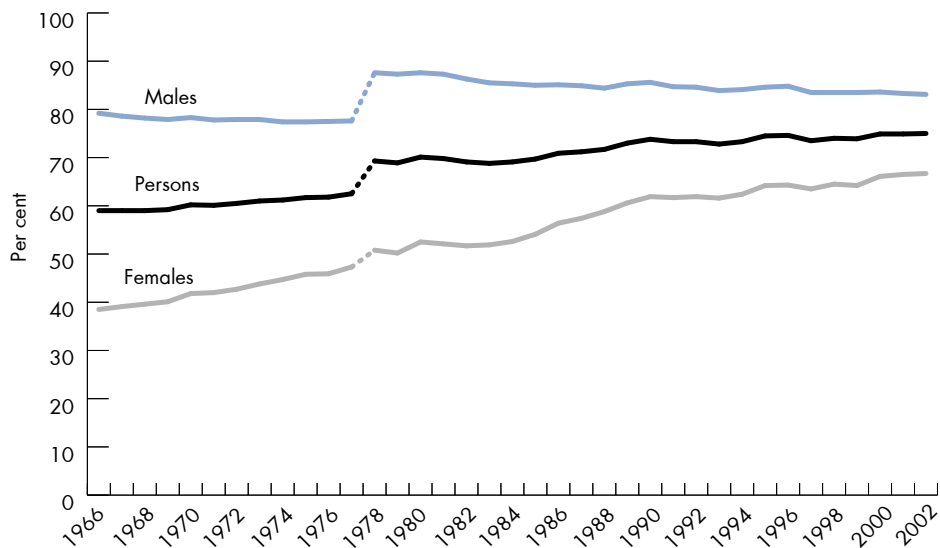
In a less regulated labour market, there are likely to be more jobs. The chance of successfully finding a job is greater, and notwithstanding disincentives created by welfare policies, people are more likely to be encouraged to enter the labour force, leading to an increase in the labour market participation rate. In a more regulated labour market the opposite is true. Additionally, generous income support programmes which reduce the cost of being jobless also discourage labour force participation.

Some common reasons why people stay out of the labour market include parenthood, education or early retirement.

There has been an upward trend in Australia’s female labour market participation over the past three decades, which stood at 66.7% in 2002. This is still unimpressive by international standards where, for example, in the United States labour market participation among women was 72.1%.

9.1 Labour Force Participation Rates, 1966-2002

Proportion of males, females and persons who are employed or seeking work



Note: The ABS labour force survey, on which the OECD figures are based, became monthly in February 1978.

Source: OECD, *Labour Market Statistics*, Indicators, www.oecd.org.

Employment-to-Population Ratios

Figure 9.2 delineates over time the ratio of employed persons to the population aged 15 and over. An economy that is producing more jobs will show a higher employment-to-population ratio.

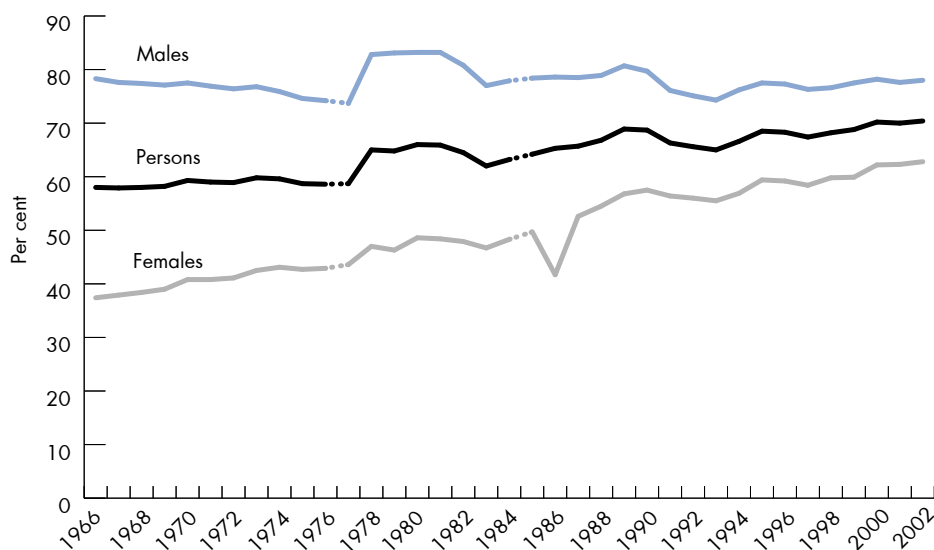
Over the past three decades, the proportion of employed Australians has steadily grown. The figure stood at 70.4% in 2002, representing an increase of over 10% from 1966.

This upward trend largely reflects the growth of female employment. Between 1966-2002, the chance of a woman being in work rose from less than two in five to more than three in five.

The flip side is the sluggish employment growth among men, although it appears to have recovered slightly in recent years. It is possible that employment opportunities that have been taken by men in the past are now being captured by women, who are increasingly better educated.

9.2 Employment-to-Population Ratios, 1966-2002

Proportion of 15-64 year old males, females and persons who are employed



Note: The ABS labour force survey, on which the OECD figures are based, became monthly in February 1978. In April 1986, the definition of employed persons was changed to include unpaid family workers who had worked less than 15 hours in a family business or on a farm. The breaks between 1977-1978 and between 1985-1986 reflect these changes.

Source: OECD, *Labour Market Statistics*, Indicators, www.oecd.org.

Unemployment

During the global recession of the early 1980s, Australia experienced a sharp rise in unemployment. It was only in 1990 that it recovered to pre-recession levels. Another global recession struck in the early 1990s and unemployment again spiralled upward, hitting an historic high of 10.7% in 1993. It then fell steadily, and now hovers around 6.0%.

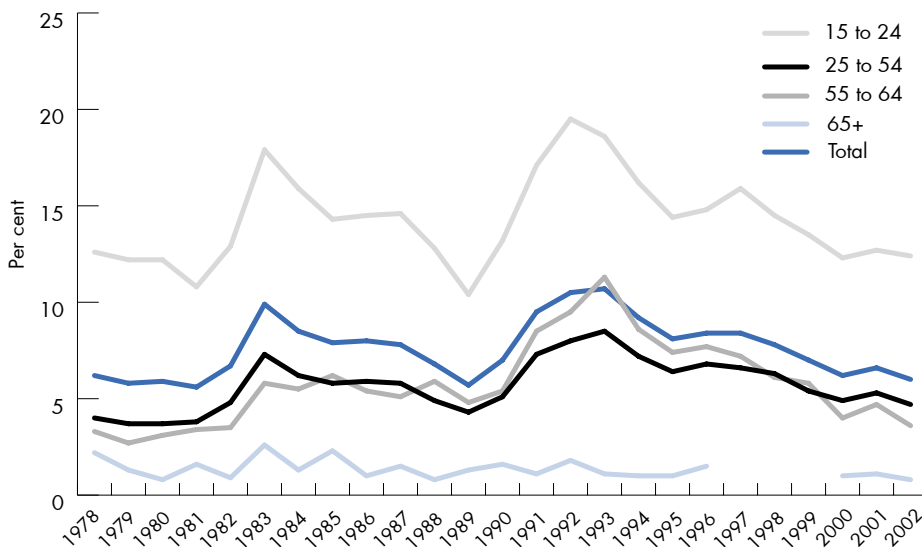
Younger labour market participants (aged 15 to 24) have fared worse generally, reflecting a shortage of low-skilled employment. Labour market regulations perpetuate the problem; for example, junior and trainee wages, which are set lower than standard wages, are nevertheless considered too high to create enough jobs for youths.

At first glance, older labour market participants (aged over 55) appear to be coping well. This is partly because these figures exclude the large number of unemployed people—particularly those over 50—who transfer from the unemployment allowance to the Disability Support Pension (see Figure 7.4, p.83).

Low unemployment in countries with strict labour market regulation, such as Sweden and the Netherlands, can also be explained by significant proportions of the unemployed claiming disability payments, and not being counted as part of the labour force.

9.3 Unemployment by Age, 1978-2002

Proportion of age group in labour force seeking full-time work



Source: OECD, *Labour Market Statistics*, Indicators, www.oecd.org.

Long-term Unemployment

An unemployment rate can conceal the true extent of the unemployment problem. For example, Portugal's unemployment rate was a mere 5.1% in 2002, but a staggering 35.5% were long-term unemployed—that is, out of work for over a year.

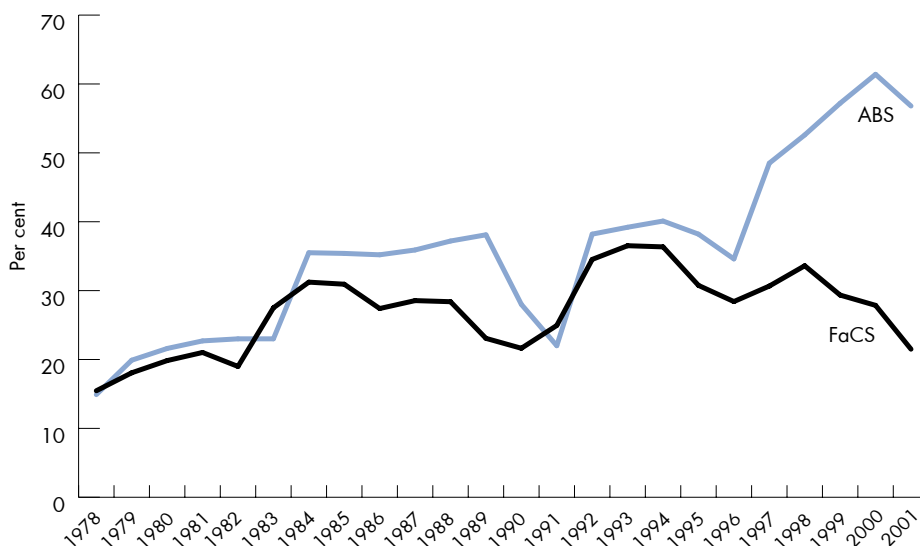
According to the Australian Bureau of Statistics (ABS), the proportion of long-term unemployed Australians has declined since the global recessions in the early 1980s and the early 1990s, standing at 22.1% in 2001.

The other source of long-term unemployment statistics in Australia, however, paints a bleaker picture. Income support records compiled by the Department of Family and Community Services (FaCS) show that in 2001, 57% of those on unemployment allowances had been out of work for over a year.

The discrepancy reflects a difference in definitions. The ABS considers employment lasting for two weeks or more as breaking a spell of unemployment. FaCS, however, disregards any intervening period of employment lasting for fewer than 13 weeks for those who have been claiming benefits for more than a year.

9.4 Long-term Unemployment, 1978-2001

Proportion of unemployed seeking work for more than 12 months



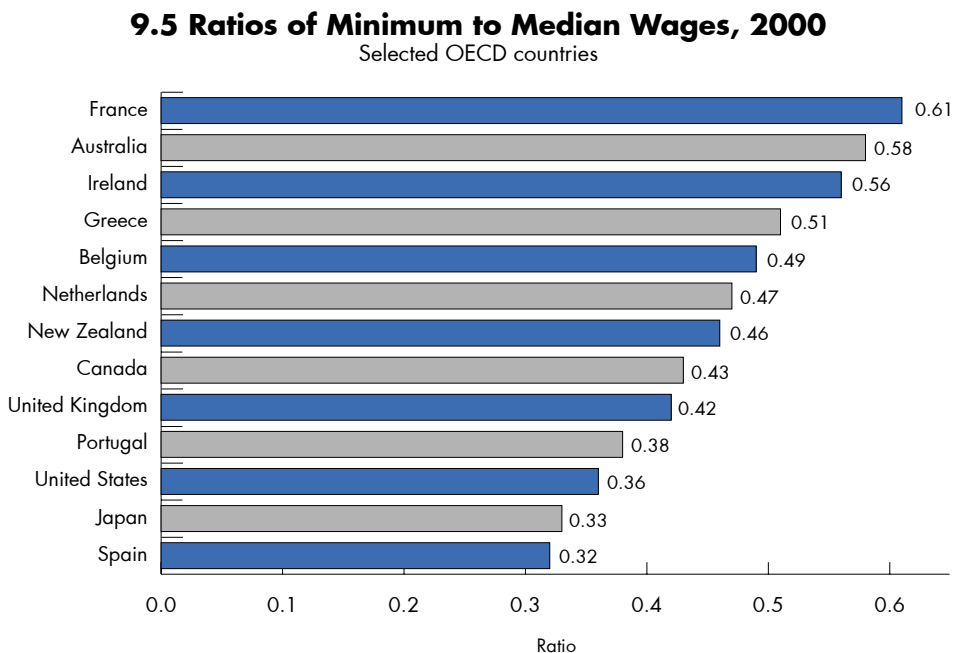
Sources: Peter Whiteford and Gregory Angenent, *The Australian System of Social Protection—An Overview*, 2nd edition, Occasional Paper No. 6 (Canberra: FaCS, 2001), Table 11; FaCS, *Income Support Customers: A Statistical Overview 2001*, Occasional Paper No. 7 (Canberra: FaCS, 2003); OECD, *Labour Market Statistics*, Indicators, www.oecd.org.

Minimum Wages

An excessively high mandated minimum wage raises the cost of employing less skilled, less experienced workers. The end result is a higher jobless rate among these workers.

An effective way of comparing the minimum rates of pay across countries is to obtain the ratios of the minimum to the median (middle) wages. A higher minimum-to-median wage ratio indicates a higher minimum wage in relative terms. As shown in the chart below, Australia has the second highest minimum wage among OECD countries.

Australia's 'award' minimum wage is adjusted annually by the Australian Industrial Relations Commission (AIRC) in a safety net review. It is carried out in response to a 'living wage' claim made by trade unions, referring to a wage which trade unions consider would meet the 'needs of the low paid'. The underlying assumption is that the low paid would become poorer were it not for a minimum wage increase. Over a half of poor Australians, however, are jobless, and any minimum wage increase would not benefit them. A higher minimum wage could actually aggravate poverty by increasing low-skilled unemployment.



Source: OECD, *Labour Market Statistics*, Indicators, www.oecd.org.

Award Coverage

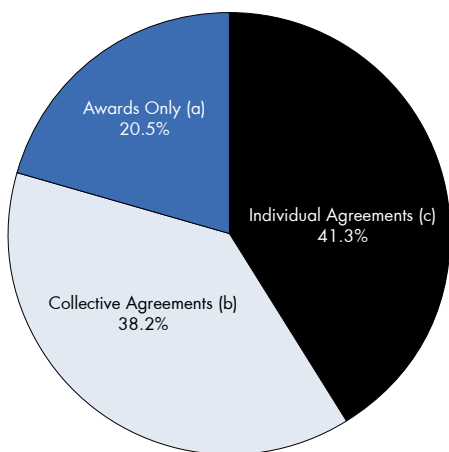
The principal instrument for labour market regulation in Australia is the award, the minimum rates of pay and conditions of employment set out by industrial tribunals.

The award ‘system’ can frustrate operations of enterprises or workplaces primarily for two reasons. First, award making and variation is essentially a process of centralised bargaining and cannot accommodate the particular needs of particular enterprises or workplaces. Second, the award system is adversarial by nature and can encourage hostile rather than cooperative employer-employee relations.

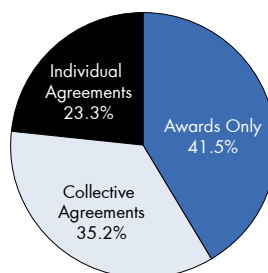
Since the introduction of enterprise bargaining in the early 1990s, the role of the award has declined. But as shown in the chart below, approximately one in five workers still have their pay set exclusively by awards. The incidence of award-only coverage is particularly high among low-skilled workers (see Insets).

The overwhelming majority of collective agreements are still underpinned by awards. The apparent spread of individual agreements is misleading because, for example, an award worker who receives an over-award rate of pay would be classified as being on an individual agreement.

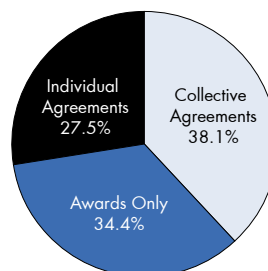
9.6 Methods of Setting Pay, 2002
Proportion of all employees



Elementary Clerical,
Sales and Service Workers



Labourers and
Related Workers



Notes: (a) Employees who had their wages or salaries set primarily by awards and were not paid more than the award rates of pay; (b) Employees who had their wages or salaries set primarily by registered or unregistered collective agreements or enterprise awards; (c) Employees who had their wages or salaries set primarily by registered or unregistered individual agreements.

Source: ABS, *Employee Earnings and Hours*, Cat. 6306.0 (Canberra: ABS, May 2002), Table 25.

Part-Time Employment

Full-time employment has ceased to be the norm in recent years. Other ‘non-traditional’ forms of employment, such as part-time and casual, are increasingly common.

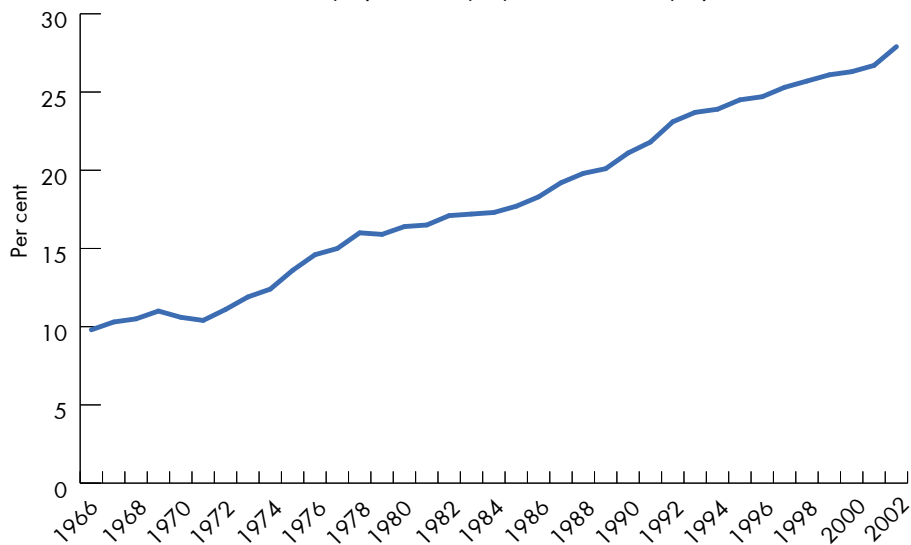
Part-time employment provides an opportunity for those who do not want to or are unable to work full-time. For example, mothers caring for young children might want to combine childrearing and employment outside the home.

Some labour market observers take a more negative view. For them, the growth of part-time employment is a sign that the economy is failing to create enough full-time employment, arguing that there are many part-time workers who want work more hours but cannot find any opportunities.

Though the number of ‘underemployed’ workers has increased since the 1980s, it has remained more or less stable over the past decade (see Inset). It is clear that workplace relations reform after the early 1990s did not cause widespread underemployment because a sharp increase had already occurred. A more likely culprit is labour market regulations, such as high minimum wages, which raise the cost of creating and maintaining full-time positions.

9.7 Part-time Employment, 1966-2002

Part-time employees as a proportion of all employees



Source: OECD, *Labour Market Statistics*, Indicators, www.oecd.org.

Casual Employment

Casual employment is another form of non-traditional employment that has become common in recent years. It has the same advantages for employees as part-time work, and enables employers to adjust the amount of labour employed for seasonal fluctuations, for instance.

A casual is generally defined as an employee who is not entitled either to paid holiday or to paid sick leave. Their hourly rates of pay are usually higher to compensate for this. In August 2002, 27.3% of all employees had no leave entitlements and were thus casuals. This definition can be misleading because casuals, under some awards, may be entitled to holiday or sick leave.

Casual employment is often considered inferior to permanent employment. Yet data from the Household Income and Labour Dynamics (HILDA) Survey show few casuals would agree.

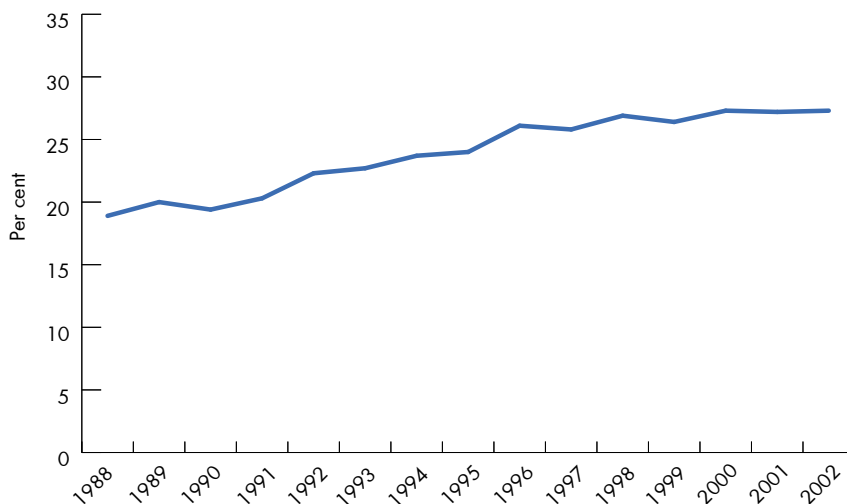
Further regulating casual employment will destroy casual employment opportunities, and will be unfair to those who prefer casual positions.

Job Satisfaction

	<i>Fixed-term</i>	<i>Casual</i>	<i>Ongoing/Permanent</i>
Pay	6.8	6.8	6.7
Job security	7.3	7.1	8.1
Work itself	8.0	7.2	7.6
Flexibility	7.4	7.7	7.3
Overall	7.8	7.5	7.6

9.8 Casual Employment, 1966-2002

Casual employees as a proportion of all employees

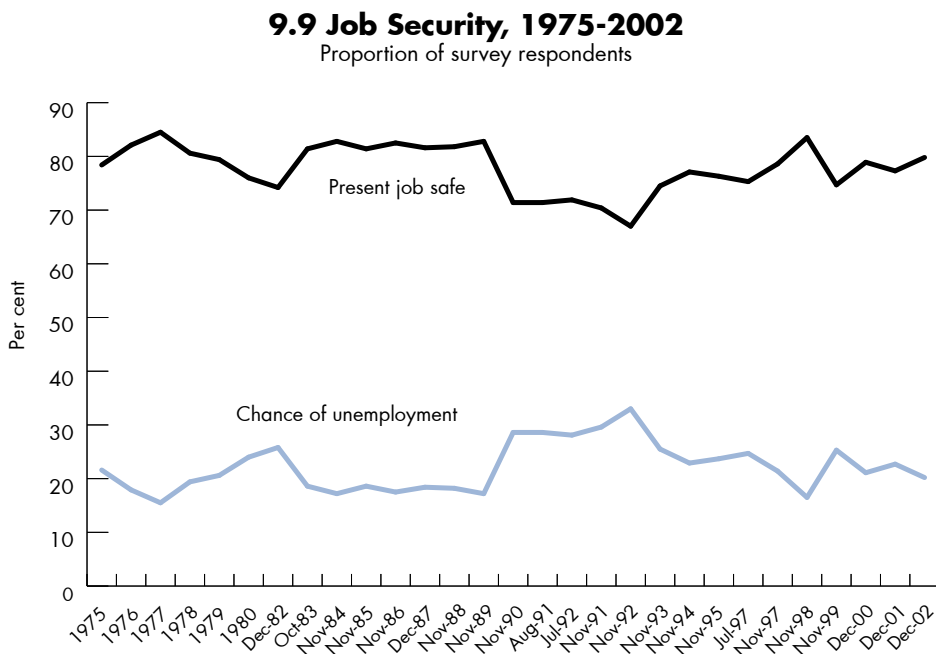


Source: Mark Wooden, 'Casual Employment in Australia: Evidence from HILDA—Data Tables', a handout that accompanied presentation at the Industrial Relations Society 2003 National Convention.

Job Security

There has been concern that the recent industrial relations reform (enterprise bargaining) will cause widespread distress among workers. Job security has been expected to decline, and working hours to extend. So far, neither has occurred.

Figure 9.9 shows the results of a Roy Morgan poll which periodically asks those who work full-time or part-time whether they think that their present job is safe, or whether they have a chance of becoming unemployed. Compared to the 1980s, job security appears to have fallen by only a few percentage points. The biggest decline occurred between 1989 and 1990. Since 1994, the perception of job security has improved and remained more or less stable. This indicates a weak association between the introduction of enterprise bargaining and a decline in job security.



Source: Roy Morgan Poll, www.roymorgan.com.au.

Working Hours

The claim that workers are working longer due to industrial relations reform is unfounded.

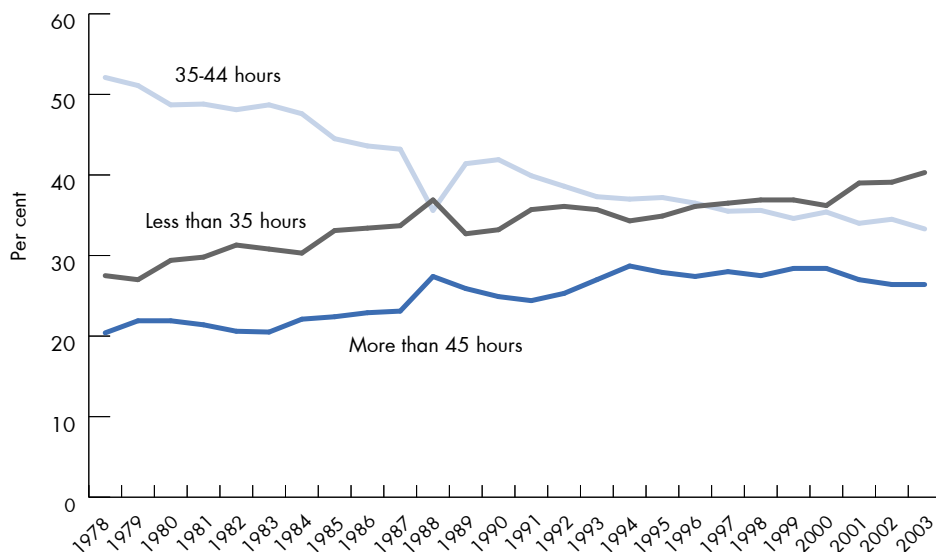
Figure 9.10 shows the distribution of working hours among all employed Australians. The gradual increase of those working less than 35 hours may reflect the growth of part-time employment. The proportion of those working 35 to 44 hours has declined, and there is a corresponding but more modest increase in those working more than 45 hours. Their incidence, however, has remained stable or even fallen in recent years. Clearly, the spread of enterprise bargaining has not caused longer working hours.

Some commentators and trade unions advocate reversing the alleged trend toward longer working hours by introducing a weekly cap, which is also intended to alleviate unemployment by redistributing work from those with too much work to those with too little work. This is an impractical solution because those working longer hours are often professionals who are highly skilled, and forcing them to cut working hours would not create jobs for the unemployed, many of whom are low-skilled. Exceedingly short working hours would also hurt the economy.

In 1998 France adopted a 35-hour cap on weekly working hours. In light of deteriorating economic conditions, it is now gradually being relaxed by, for instance, raising overtime quotas for small businesses.

9.10 Weekly Hours Worked, 1978-2003

Proportion of employees



Source: ABS, *Labour Force Australia*, Cat. 6203.0 (Canberra: ABS, various years).

Earnings Distribution

Critics of the recent industrial relations reform argue that enterprise bargaining has widened earnings inequality.

Figure 9.11 shows ratios between percentile wages. A percentile is obtained by dividing a group of people into 100 equal sized groups. For example, a worker ranked in the 90th percentile earns more than 90% of all workers. The larger the percentile ratio, the wider the wage disparity.

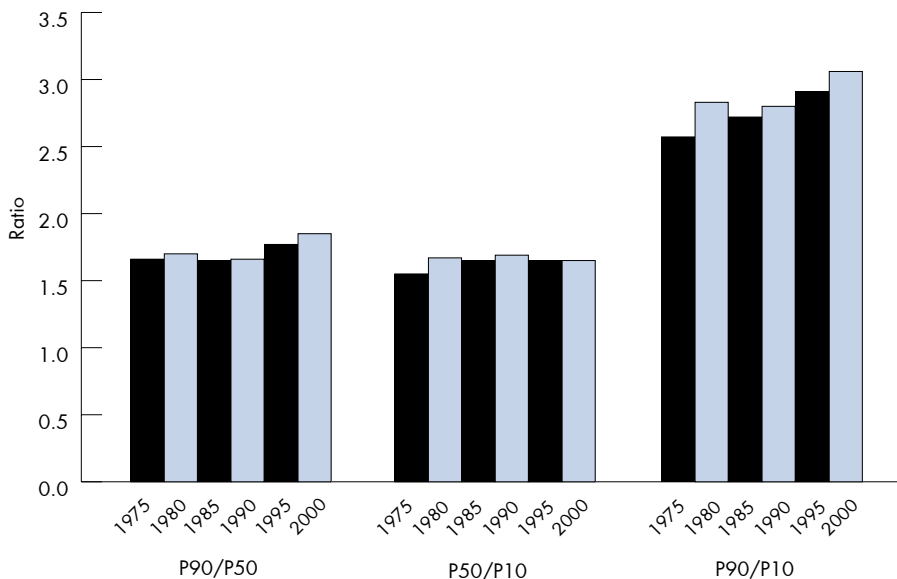
The gap between the 10th and 50th percentile earnings has remained more or less constant since 1980. The 90th percentile earnings, however, grew more significantly than the 10th and 50th percentile earnings.

The earnings distribution has widened, although whether or not such a trend has to do with labour market deregulation is another matter. If enterprise bargaining is responsible, it is neither surprising nor undesirable. Enterprise bargaining is intended to allow workers' wages to differ according to their employers' capacity to pay and each employee's skills, resulting in more diverse wage outcomes and distribution.

This does not mean that decentralised bargaining increases poverty, for earnings and household income distributions are not correlated. A considerable proportion—approximately 40% in the mid-1990s—of low-wage earners live with higher-wage earners, such as spouses, and are by no means poor. It might be possible to narrow the earnings distribution by considerably raising low wages, but it would not alleviate poverty.

9.11 Earnings Distribution, 1975-2000

Ratio of earnings in 90th, 50th and 10th percentiles



Note: P90, P50 and P10 refer respectively to the 90th, 50th and 10th-percentile earnings.

Source: OECD, *Labour Market Statistics*, Indicators, www.oecd.org.

Summary

After a decade of reform, Australia's labour market regulation remains excessive. The minimum wage is high by international standards, and prescriptive awards continue to underlie many non-award agreements. Hiring, particularly low-skilled labour, is unnecessarily costly and cumbersome. The creation of low-skilled jobs has been deterred and resulted in high unemployment among youths. Excessive labour market regulation has also perpetuated persistent long-term unemployment.

On a positive note, employment and the labour force participation among women has increased, underpinned by the growth of part-time and casual jobs, which are preferred by many women. These less traditional forms of employment are thought to have spread due to an increasing demand from workers. Another possible explanation is that regulations, such as minimum wages and unfair dismissal laws, have discouraged full-time and permanent employment.

Past reform neither eroded job security nor extended working hours and there is a strong case for further labour market deregulation. This may mean wider use of enterprise or even individual agreements where workers can negotiate with employers on equal terms, providing there are plenty of alternative employment opportunities in the market. The best protection for workers is to make it easier for employers to give people jobs, which entails less regulation.

10. ECONOMIC PERFORMANCE

WOLFGANG KASPER

Introduction

Economic welfare is a fundamental human aspiration. It ranks alongside such values as freedom, justice, (internal and external) security and peace, and the preservation of a liveable natural environment. Sometimes, ambitions for better economic welfare clash with these other objectives, but in the long run and in most instances, improved material welfare is compatible with, and supportive of, advances towards these non-material aspirations.

Material welfare is therefore one, but not the only, yardstick by which we judge the quality of government.

There is fairly widespread consensus that material welfare is determined by:

- Price-level stability (no inflation or deflation);
- High employment (those willing to work at the going wage rate finding employment);
- Steady expansion of overall demand in tune with growing supply capacities (no boom-bust cycles);
- External equilibrium (no unforeseen and disruptive changes in foreign debts);
- Equitable income distribution; and
- Economic growth commensurate to the resources and the aspirations of the nation.

The statistical indicators in this chapter show how the Australian economy has performed on these scores.

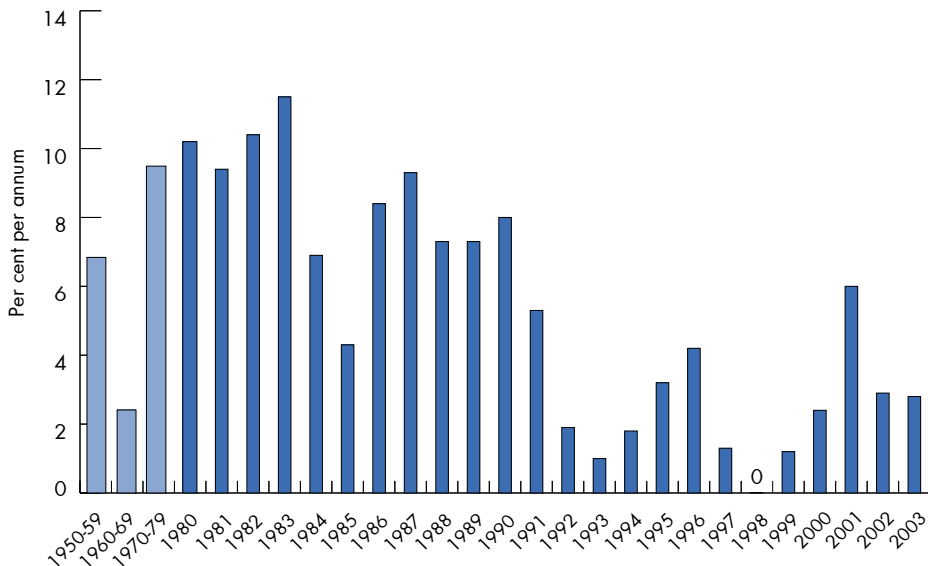
Price-Level Stability

Inflation relates to the price level—the average of all prices that, for example, typical consumer households face. Price-level stability does not mean that all individual prices stay the same over time. In a dynamic economy where demands, supplies, technologies, knowledge and many other factors change constantly, some prices go up and others go down. The average of these price changes ought to be close to zero.

Figure 10.1 shows the changes in the Consumer Price Index since the 1950s. After the high inflation during the shortages of the Korean War in the early 1950s, price-level inflation was comparatively low in the late 1950s and throughout the 1960s (some 2.5% per annum). This changed dramatically in the early 1970s, when worldwide inflation accelerated, oil prices were raised by the OPEC cartel, and the Whitlam Labor government embarked on a policy of monetary and fiscal expansion, as well as pushing up wage levels. From 1975-1976, annual inflation ran at over 16% per annum. Sustained high rates of inflation followed, which successive governments tried to peg back by restricting demand (in particular through restrictive monetary policies and high interest rates).

10.1 Inflation, 1950-2003

Annual per cent change in the consumer price index
(1950-1979 annual averages for decade)



Sources: Reserve Bank of Australia, *Australian Economic Statistics 1949-50 to 1996-97*, Occasional Paper 8 (Sydney: RBA, 2001), Table 5.7b, see www.rba.gov.au/Statistics/op8_index.html; ABS, *Australian Economic Indicators*, Cat. 1350.0 (Canberra: ABS, February 2003), Table 5.1.

The successful return to low rates of inflation was slow in coming, because the supply side of the economy was rather inflexible and monopolised (industry protection, heavy regulation, cartels and government-supported union monopolies). In the wake of domestic economic reforms and when fiscal deficits were cut back in the 1990s, Australians again enjoyed a high degree of price-level stability (and moderate nominal interest rates)—an experience paralleled by better inflation control in most developed countries. The ‘inflation spike’ in 2001 (see Figure 10.1) reflects a one-off adjustment of many consumer prices to the imposition of the Goods and Services Tax.

Over the past generation, relative prices have changed considerably, as the table below indicates. None of the prices cited has come down, but the cost of standard food items has risen only slowly. Bread and butter went up by an annual average of only about 2%. By contrast, the prices of newspapers and books have risen consistently and steeply, and the standard motor car has become about 5% per annum more expensive, reflecting a considerable degree of quality improvement. Not shown in the table are enormous price reductions in products and services that benefited from rapid technical change, for example computers.

Prices of Selected Household Items, 1970 & 2003

<i>Item</i>	<i>1970</i>	<i>2003</i>
Butter (500g)	\$0.88	\$1.57
Bread (loaf)	\$1.40	\$2.70
Milk (litre)	\$0.48	\$1.57
Eggs	\$1.14	\$3.27
Tea (500g)	\$1.52	\$10.00
Potatoes (kg)	\$0.38	\$1.60
Steak (kg)	\$6.00	\$16.00
Newspaper	\$0.10	\$1.20
Postage stamp	\$0.20	\$0.50
Holden Commodore (1978)	\$6,513	\$32,000
Paperback novel	\$1.25	\$22.95

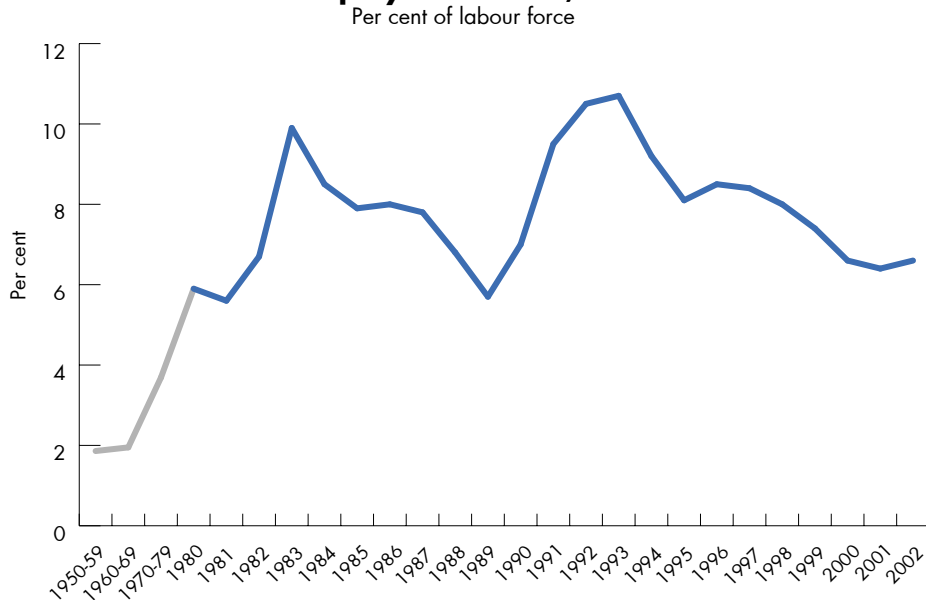
Sources: Glen Miller, *Australia's Twentieth Century* (Sydney: New Holland Publishers, 1999); ABS, *Average Retail Prices of Selected Items*, Cat. 6403.0 (Canberra: ABS, June 2003).

High Employment

Figure 10.2 shows that the 1950s and 1960s were periods in which almost all Australians willing to work at prevailing wages could find jobs. This changed with the onset of inflation and several wage explosions in the early 1970s, early 1980s and early 1990s when joblessness ratcheted up during recessions but dropped little during cyclical upswings. Inflationary wage costs, tax increases, cyclical instability and restrictive monetary policies made potential employers reluctant to offer jobs. The old, centralised and cumbersome industrial relations system, with its quasi-judicial, centralised wage fixing and posturing by organised labour and employer organisations, has become an obstacle to rapid job creation and hence a major source of economic misery.

Economic theory and international comparisons tell us that freeing up labour markets and wage rates would allow a return to high employment as well as improving productivity—the most important source of economic growth and job creation. There is no reason why unemployment should not drop to the low levels of the 1950s and 1960s.

10.2 Unemployment Rates, 1950-2002



Sources: Reserve Bank of Australia, *Australian Economic Statistics 1949-50 to 1996-97*, Occasional Paper No.8, see www.rba.gov.au/Statistics/op8_index.html; ABS, *Australian Economic Indicators*, Cat. 1350.0 (Canberra: ABS, February 2003), Table 6.1.

Steady Demand Expansion

The absence of unexpected, dramatic boom-bust cycles is an economic boon because it helps people avert unsettling and costly surprises. However, the business cycle can never be totally eliminated and some cyclical fluctuations should always be expected.

The upper panel of Figure 10.3 (overleaf) shows how production (Gross Domestic Product adjusted for price movements and seasonal fluctuations) expanded since the late 1960s. Most of the fluctuations in production are caused by fluctuations in aggregate demand: consumer spending goes through cycles; export demand moves from booms to busts; investment demand is subject to accelerations and decelerations; stocks are built up or run down; and elections often disrupt the steady flow of public sector demand. By contrast, the potential to supply goods and services tends to expand in more steady ways, as it is influenced by factors that evolve at a fairly steady pace: the population and workforce grow fairly steadily; fluctuation in investment in any one year makes little difference to long term growth of huge capital stock; and skills and technologies used in the national economy evolve gradually.

The growing supply potential can therefore be estimated by linking peaks in production in a linear way, with short-term output fluctuations attributed to variations in demand. Comparing the estimated supply potential (the peak-to-peak line in the upper panel of Figure 10.3) to actual demand and production (the GDP line) allows us to calculate the rate of national ‘capacity utilisation’.

In the lower panel of Figure 10.3, actual production (GDP) is expressed as a percentage of the corresponding supply potential. This depicts the rate of capacity utilisation of the national economy. It is the best reflection of the business cycle. Ideally, demand and production should expand in line with the growing supply potential, but that is rarely possible in a world of changing demand.

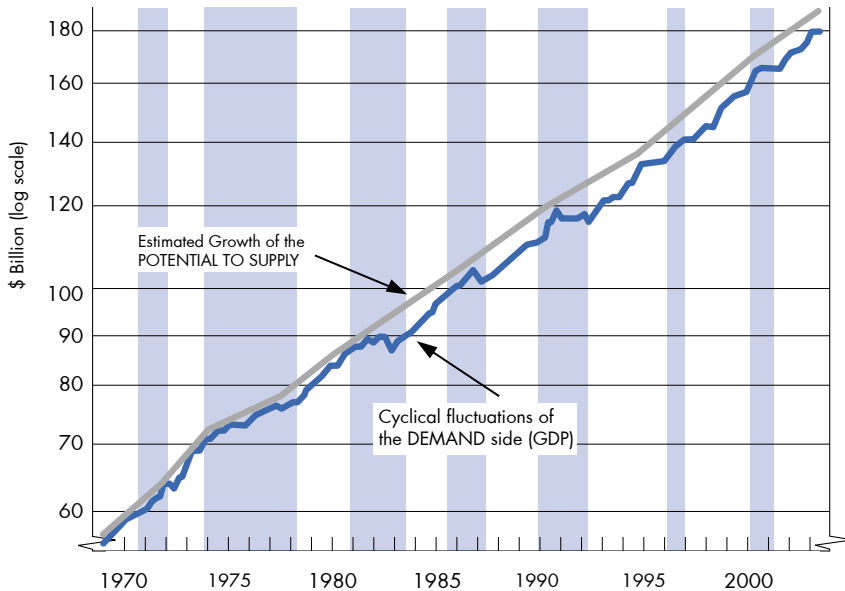
It can be seen that:

- The Australian economy, like all other economies, goes through cycles of about five years duration, which begin with a sharp decline (shaded area), followed by a longer period of expansion. Although these cycles are irregular, it is sensible to assume that what goes up inevitably comes down again, and to be prepared for unexpected recessions.
- Upswings are often interrupted by ‘mini-recessions’. These appear as ‘blips’ on the screen when rising demand begins to trigger new investments, because previously idle capacities are becoming fully utilised.
- Australian business conditions fluctuated much more widely when the economy was regulated and therefore rigid. Since the economic reforms of the 1980s and early 1990s, a more flexible economy has allowed Australians to enjoy a period of long expansion in line with supply growth (that is, unusually high capacity utilisation), which has made boom-bust cycles less likely.

10.3 The Business Cycle in National Economic Activity, 1969-2002

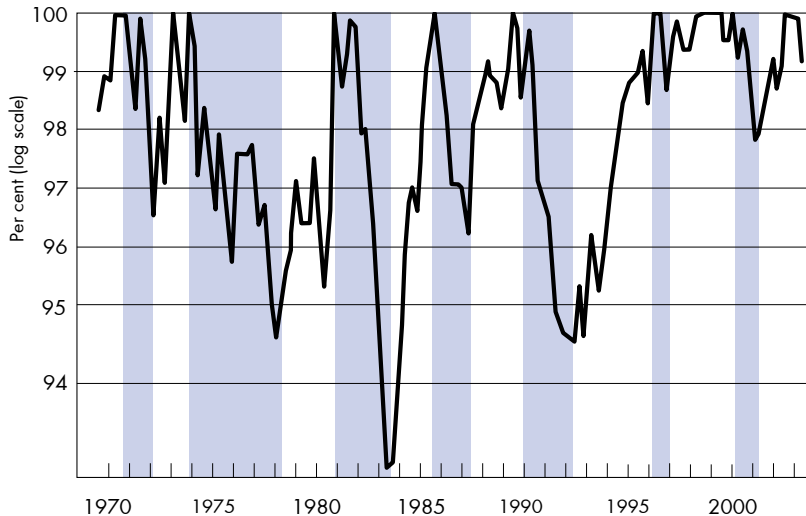
Based on seasonally adjusted, real Gross Domestic Product, chain volume index (reference year, 2001-02)

Aggregate Output and Supply Potential



Utilisation of the supply potential

Actual production (GDP) as a percentage of the supply potential in the corresponding quarter



■ period of recession

Source: ABS, *National Accounts* (Canberra: ABS, various years), analytical series.

External Equilibrium

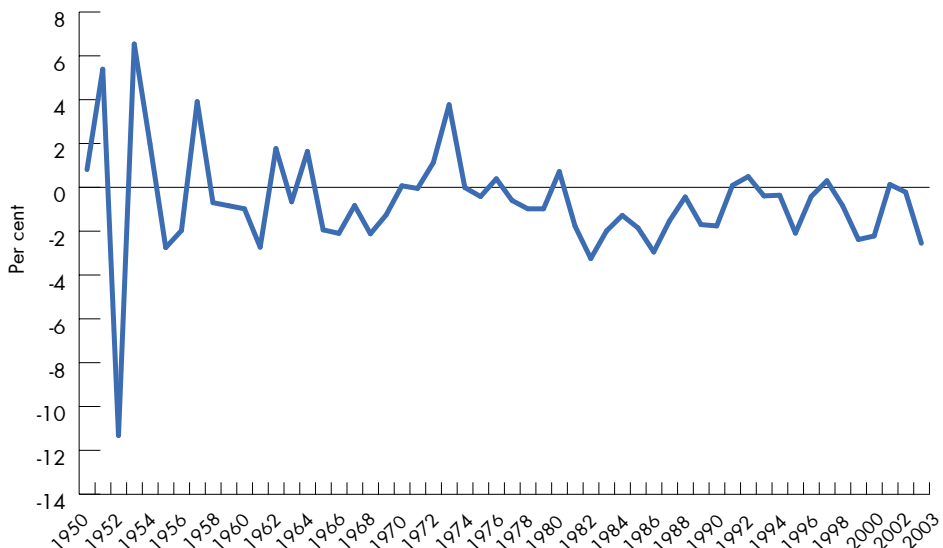
The difference between what Australian residents sell overseas (exports) and what they buy from abroad (imports), and taking into account income from investment abroad, is reflected in the so-called current account of the balance of payments. In Figure 10.4a, this balance is expressed as a percentage of the national product.

These data do not tell us anything about whether external deficits or surpluses were intended and welcome, or unintended. A deficit may mean that foreigners are keen to invest in Australia because it is an investment location that promises security and good profits. Or a deficit may be a matter for concern because foreigners may soon recall their credit to Australian borrowers and then destabilise our plans and activities.

Up to the 1980s, there were repeated, strong fluctuations in Australia's external current account, and some periods of deficit led to unwelcome foreign exchange and debt crises. Since the early 1980s, fluctuations have been smaller. This is due to the freeing-up of a most important price, the exchange rate of the Australian dollar. This has had a stabilising influence on our external balance. However, Australia's external current account has been fairly consistently in deficit since the early 1980s. As a result, foreign debt has accumulated (Figure 10.4b).

10.4a External Equilibrium, 1950-2003

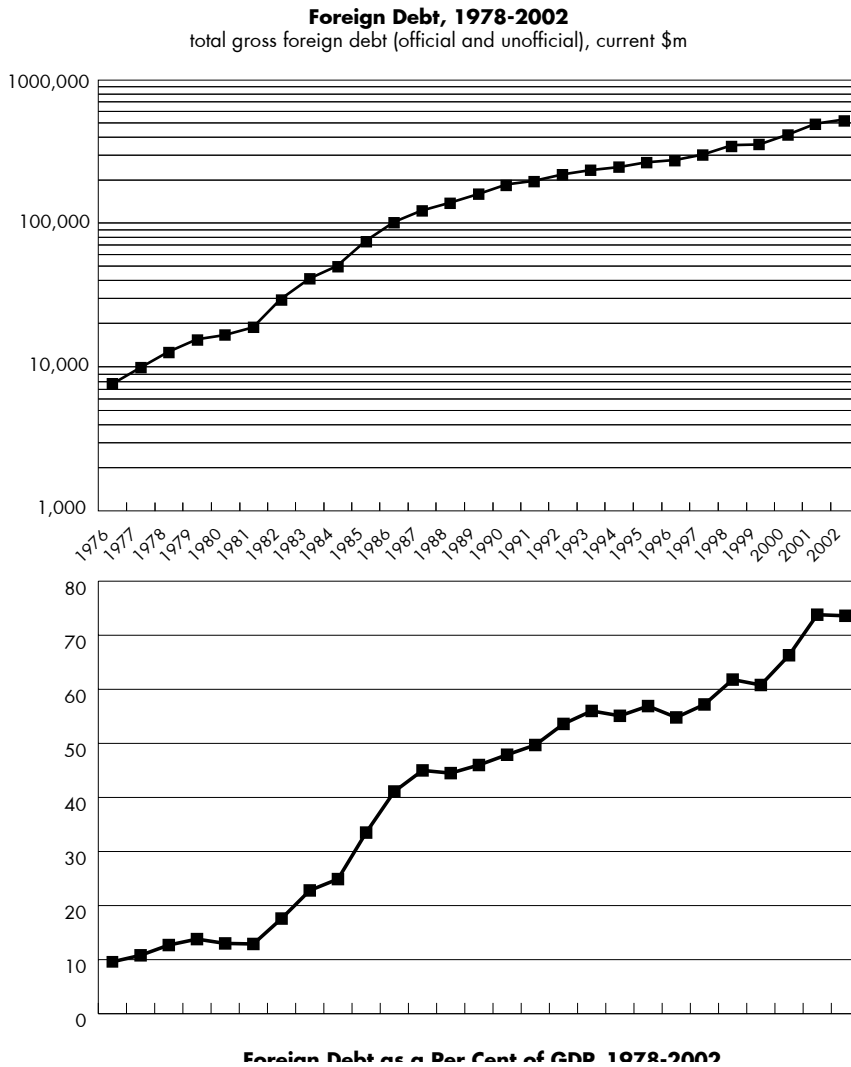
Exports minus imports as a proportion of GNE (annual, current prices)



Sources: 1950-96: Reserve Bank of Australia, *Australian Economic Statistics 1949-50 to 1996-97* (Sydney: RBA, 2001), Table 5.1a, see www.rba.gov.au/Statistics/op8_index.html; 1997-2003: ABS, *Australian System of National Accounts 2001-02*, Cat. 5204.0 (Canberra: ABS, 2002), Table 8; ABS, *National Income, Expenditure and Product*, Cat. 5206.0 (Canberra: ABS, June 2003), Table 46.

Figure 10.4b shows foreign debt has been rising consistently, both in absolute terms and as a percentage of the national product. Australians have obviously become increasingly used to buying more from overseas than they were able or willing to sell. Seen alternatively, they have saved far less than they invested, relying on the savings of foreigners to finance some of their massive capital investments.

The deregulation of international capital flows in the early 1980s facilitated this trend. It also means that policy now has to take account of the possibility of capital flight. Capital flight would turn unorthodox experiments in economic policy fairly quickly into destabilising external disequilibria or currency depreciations. This fast feedback mechanism is likely to prevent adventurism in economic policy.



Sources: RBA, *Bulletin Statistical Tables*, Table H8 see www.rba.gov.au/Statistics/Bulletin/index.html; ABS, *Australian System of National Accounts*, Cat. 5204.0 Supertables (Canberra: ABS, 2003), Table 8.

Distribution of Income

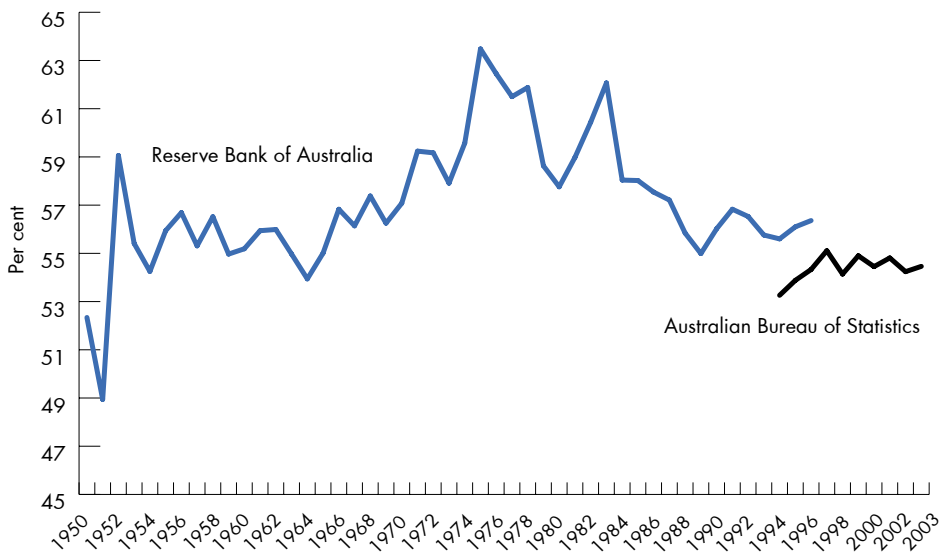
Income distribution has many dimensions (by person, social group, region and so on). Previous chapters have shown income, wealth and earnings distributions. Figure 10.5 shows another important aspect, namely the share of national income that accrues to wage and salary earners.

It can be seen that that share was driven up dramatically in the Whitlam era (after 1972) and again at the beginning of the Hawke era (in the early 1980s). Whether this is a welcome development for workers is a political question and demands a value judgement. Both periods of rising and high wage shares led to times of high unemployment and slow economic growth.

Workers are often worse off when they have a high share of the 'national economic cake' as the cake then grows slowly (as was the case in the latter part of the 1970s). They may well prefer a smaller share of a faster growing cake. What really matters is not income distribution at all, but the growth of real individual incomes and the level of absolute poverty (see Chapter 8).

10.5 The Wage and Salary Share, 1950-2003

Labour as a proportion of total factor income (current prices)



Sources: 1950-96: Reserve Bank of Australia, *Australian Economic Statistics 1949-50 to 1996-97* (Sydney: RBA, 2001), Table 5.3, see www.rba.gov.au/Statistics/op8_index.html; 1993-2002: ABS, *Australian System of National Accounts*, Cat.No. 5204.0, Table 8; ABS, *National Income, Expenditure and Product*, ABS Cat 5206.0 (Canberra: ABS, June 2003), Table 46.

Economic Growth

The underlying component of economic welfare is prosperity (the sustained rise of real living standards, as measured by real per capita production and income). This aspect of economic welfare is a long-term aspiration. It is reflected in the sustained growth of the supply potential (Figure 10.3) and the per capita gross domestic product in real terms (Figure 10.6). It is therefore appropriate to take a long-term perspective.

The long-term growth of the economy is a supply side phenomenon. It is greatly shaped by decisions and attitudes to working, learning skills, saving, forming capital and innovating. All this is driven by the prevalence or absence of competition and enterprise, which in turn depend greatly on economic freedom (see Chapter 11).

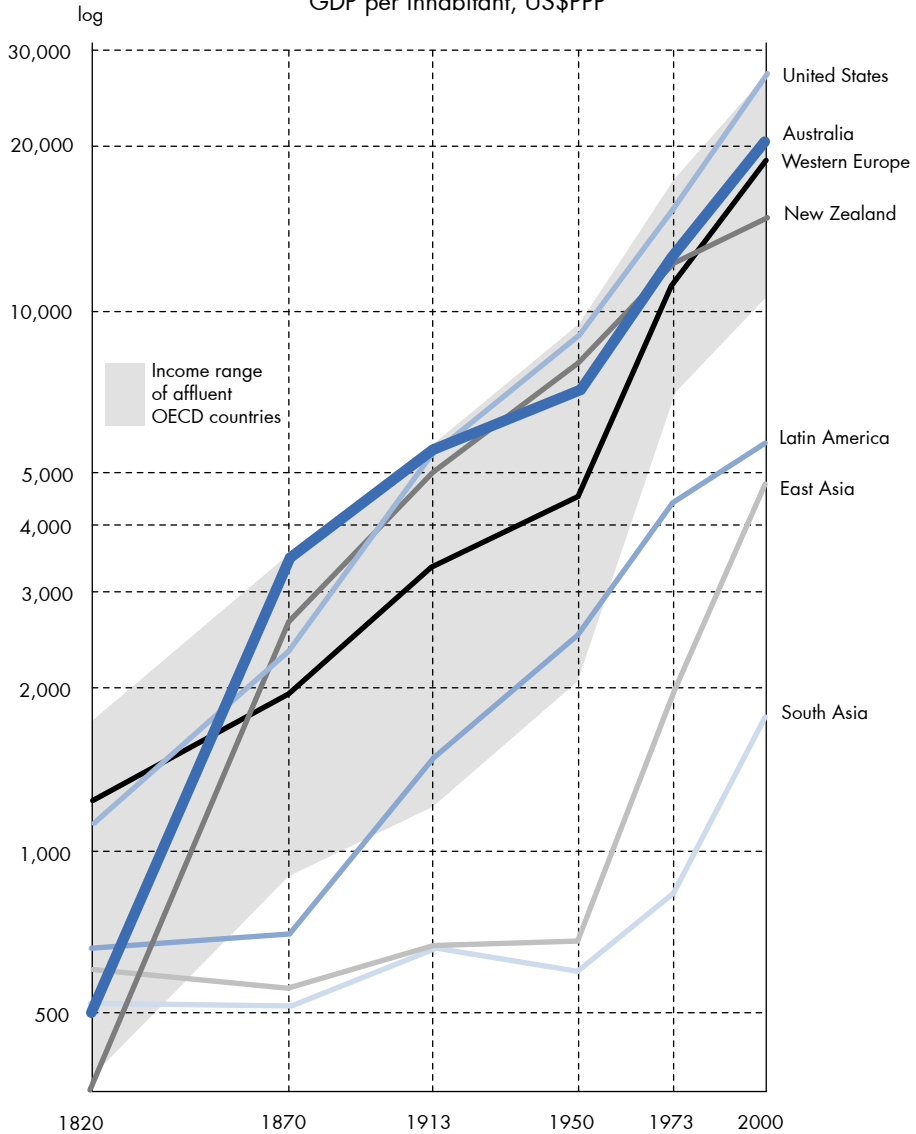
Economic growth cannot be assessed from one quarter or year to the next, but only over decades, if not generation-spans. By contrast, price-level stability, employment, demand stability and external equilibrium are monitored and assessed over the short term and may be influenced by short-term economic policies. They therefore tend to gain more media attention than issues and policies relating to economic growth.

In Figure 10.6, we compare Australia's long-term growth of real gross domestic product per person (per capita GDP), the most commonly used measure of economic growth and average living standards, with that of other regions from 1820 onward. It can be seen that the early settlers in Australia (and New Zealand) managed to attain very high levels of real income during the 19th century. Easy access to natural resources, the open inflow of skilled enterprising people, technical knowledge and capital, as well as simple, trust-inspiring institutions (British law on property and contract, and small, predictable government) permitted the settlers to move the Australian colonies into the most prosperous part of what later became the OECD, the 20th century club of affluent capitalist nations.

After Federation and for most of the 20th century, the Australian economy performed less well by international comparison. The interventionist protectionism of the 'White Australia policy' and rising tariffs, plus massive, politically motivated transfers to the urban and industrial areas, and regulated labour markets combined to erode growth incentives and entrepreneurial opportunities. Australia missed the trade-driven growth wave of the 1950s and 1960s to a large extent. In the 1960s, growth rates averaged less than 3% per annum. This was seen as satisfactory by historic standards, but was far short of what most other developed economies achieved at the time. In the 1970s (a period of a slowdown in worldwide growth), Australian production grew by only 1.8%, falling further behind America and Western Europe. The Australian lead in living standards over the new industrial countries of East Asia has narrowed. Some—such as the average inhabitants of city economies of Singapore and Hong Kong—now enjoy higher living standards than average Australians. Nonetheless, Australia's economic growth has picked up in the wake of economic reforms over the past two decades.

10.6 Economic Growth in Australia and the World

A long-term, global perspective
GDP per inhabitant, US\$PPP

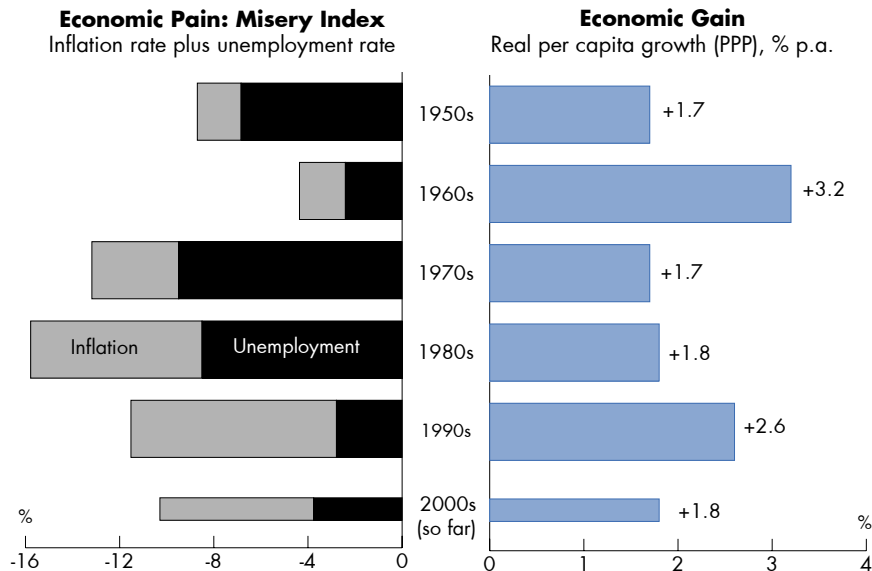


Source: A. Maddison, *The World Economy, A Millennial Perspective* (Paris: OECD, 2001), updated to 2000 from national statistics.

Summary

Commentators sometimes summarise and compare the economic performance of a nation (over time and internationally) by adding the unemployment rate and the inflation rate to compile an ‘economic misery index’ and to compare that with the growth of average real living standards (inflation-adjusted GDP per capita).

10.7 Broad Brush Evaluation: Economic Pain and Gain, 1950-2000



Source: A. Maddison, *The World Economy* (Paris: OECD, 2001), 279, Table C1-c.

Figure 10.7 makes a broad-brush attempt to evaluate Australia’s economic performance over the past half century in these simplistic, but nevertheless telling, terms. It emerges that:

- The 1960s were a period of less pain and more gain than the 1950s.
- The 1970s and 1980s, when two oil shocks and the unorthodox economic experiments of the Whitlam era, combined with a refusal during the Fraser era to embark on economic reform of the rigid economy, were periods of little economic gain and considerable economic pain for average Australians.
- The reforms preceding the 1990s and the first years of the 2000s have reduced the economic pain and produced good economic gains.

If Commonwealth and State parliamentarians and executive governments focussed more on medium-term economic perspectives, and business, the public and the media were less concerned with the short-termism of share price movements, interest rate changes and monthly unemployment data, much better economic welfare could be achieved. There is no reason why unemployment should not drop to 2%, inflation should not be kept below 2% per annum, and economic growth (per capita) at about 3% per annum.

11. ECONOMIC FREEDOM

WOLFGANG KASPER

Introduction

In a tradition that goes back to the founding fathers of modern economics, such as Adam Smith (1723-1790), economists have shown that secure property rights, free markets and the equality of all before the law—in short ‘economic freedom’—are central to the attainment of economic welfare. Economic freedom is also important to attaining civil and political freedom, social peace, security and conserving our environment.

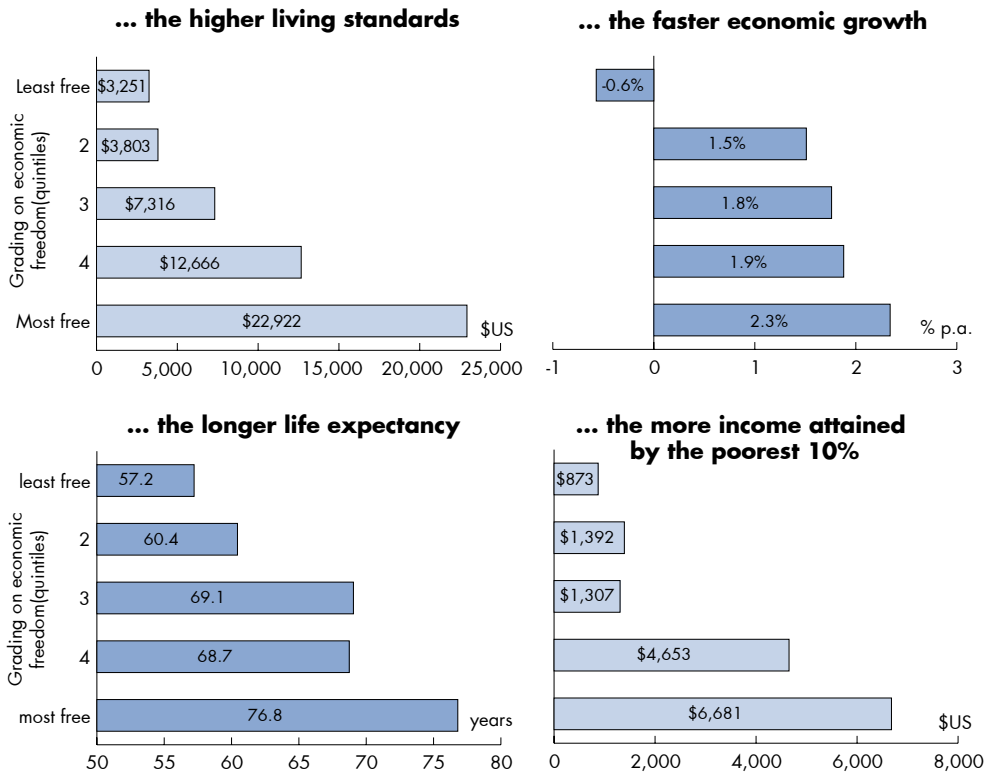
Conversely, high and improving economic welfare is hampered by such things as big government, intrusive, prescriptive regulation and legislation, inflation, political subsidies to specific, favoured industries or groups, discriminatory and high taxes, tariff protection and other political interferences with the free international flows of goods, services, capital and knowledge, and the arbitrary confiscation of property rights. Such interventions may serve the careers of parliamentarians, rulers, administrators and members of well-connected, organised interest groups, such as industry lobbies, trade unions or single-issue activists. However, they invariably undermine the long-term economic welfare of most citizens. Interference with economic freedom and individual responsibility tends to have unforeseen and deleterious side effects, which erode incentives and make it harder for competing producers and buyers to discover information about what is widely appreciated and useful to people.

Because these fundamental insights had been almost forgotten or were widely ignored in most nations during the 20th century, leading economists, such as Economics Nobel Prize winner Milton Friedman, instigated a major international effort to measure economic freedom in many different countries. The purpose was to show the benefits or otherwise of economic freedom. It has resulted in annual assessments of economic freedom in 123 countries around the world.¹ Such international comparisons date quickly and are somewhat abstract. Therefore, The Centre for Independent Studies published *Economic Freedom Watch*, with regular and up-to-date assessments of economic freedom in Australia. The project also highlighted decisions by parliamentarians, administrators, judges, businesses and other organisations, which promote or diminish the economic freedom of average Australians.²

Economic Freedom and the Consequences

To show the relevance of economic freedom, the assessments for 2001 of 123 countries were averaged across five groups, ranging from the least free quintile (among them, for example, Russia and Zimbabwe) to the most free quintile (among them Hong Kong, the United States and Australia). Then, the degree of economic freedom in these groups was compared with widely used measures of prosperity and other aspects of social wellbeing (Figure 11.1).

11.1 Economic Freedom and Welfare The higher economic freedom...



Source: J. Gwartney and R. Lawson, *Economic Freedom of the World* (Vancouver: Fraser Institute, 2003).

It can be seen that greater economic freedom makes a huge difference to both the level and growth rate of per capita incomes. For example, citizens in free economies produced and enjoyed average living standards of US\$22,922 per annum in 2001, as compared to a mere US\$3,251 per annum for the least free economies. Likewise, living standards in the least free countries declined in absolute terms during the 1990s, but in the freest economies they grew at a healthy average of 3.3% per annum.

The positive influence of freedom on economic welfare is also borne out by numerous country-to-country comparisons. Thus, many of the heavily regulated welfare states of Western Europe, where high taxes, regulations and the expropriation of property for the sake of environmental objectives are eroding traditional economic freedom, have been suffering from long-term stagnation (and social and political discontent), whereas jurisdictions which implemented economic reforms to enhance freedom (such as Australia) have enjoyed economic growth and a normal level of material confidence. The old Marxist adage that ‘the rich are getting richer and the poor are getting poorer’ has to be restated: ‘the free economies are rich and are getting richer, and the unfree are getting poorer’.

Figure 11.1 also shows that differences between the least free and most free economies have a major impact on life expectancy. Moving from heavy economic repression to a free economy tends to correspond with a remarkable 20 more years in life expectancy (at birth). Other important social indicators, such as literacy, standards of health, fundamental human rights (not shown here), tend to show similar beneficial associations with economic freedom.

It can also be seen that the poorest 10% of people in the freest (and hence most affluent) economies enjoy much higher incomes than in the most unfree (and hence miserable) economies of the world. The poorest 10% of citizens see their real per capita incomes (the best measure of ‘absolute’ poverty) go up by more than eightfold on average if a jurisdiction moves from economic repression to a high level of economic freedom. By contrast, ‘relative’ poverty, as measured by the income share of the poorest 10% of the population, is not affected much by variations in freedom (and hence prosperity). The poorest 10% of the population tend to get only 2-3% of national income, irrespective of freedom ranking and living standard. We therefore have to conclude that there will always be relatively poor people, but that it is preferable for those who are materially weakest, to live in less regulated, small government and affluent economies.

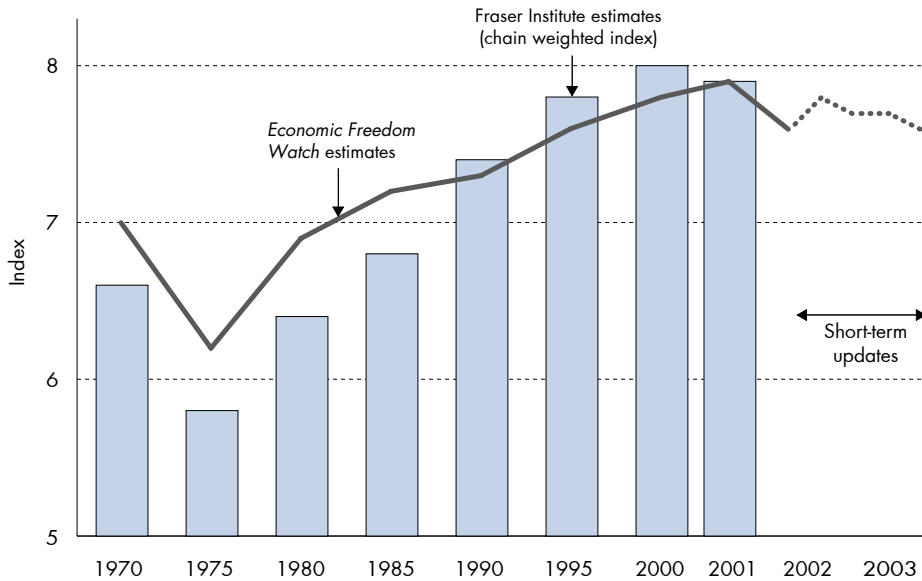
Economic Freedom in Australia

Figure 11.2 depicts the evolution of economic freedom in Australia since 1970, as assessed by the Fraser Institute team and *Economic Freedom Watch*.

It can be seen that the economic freedom Australians used to enjoy was severely diminished during the Whitlam era. Australia's economic freedom rating went from a passable 6.6 to an average of 5.8 out of 10. Since then, economic freedom in Australia has been gradually and slowly enhanced by economic reforms, most notably those by successive Labor administrations in the late 1980s and early 1990s. The subsequent benefits in terms of better economic performance (see Chapter 10) are entirely in line with long-term experience and international comparisons.

11.2 Measuring Economic Freedom in Australia, 1970-2003

Economic Freedom Index (out of a possible maximum of 10)



Sources: J. Gwartney and R. Lawson, *Economic Freedom of the World* (Vancouver: Fraser Institute, 2003) and W. Kasper, *Economic Freedom Watch Report No.6* (Sydney: The Centre for Independent Studies, 2003).

More recently, there has been a 'tea break' in economic reform, and Australia's economic freedom has been sliding back. The material consequences of this are not immediately visible, as the connections are normally long-term and slow to evolve. Short-sighted observers may seem justified in feeling glib about Australia's present economic freedom standards. However, the rest of the world is not standing still. Worldwide, economic

freedom standards are improving gradually while Australia's shortfall in reform as compared with the other major Anglo-Saxon countries has been widening in recent years. These are setting an international benchmark against which Australia is being measured by competitors and investors. With globalisation and a move to freer trade and capital flows between Australia and the United States, Australia's recent neglect of economic reforms is a matter for serious concern.

The Australian economy was still ranked in 2001 amongst the freest ten economies in the world (Hong Kong, Singapore, United States, New Zealand, United Kingdom, Canada, Australia, Ireland, Switzerland, Holland). However stagnation and economic misery may rise quickly when reform fatigue leads to a relapse into political meddling with property rights, equality before the law and big government.

For example, this was borne out in Japan and Germany in recent years. These once vigorous and enterprising economies were subjected to much political interference during the 1980s and 1990s. As of 2001, they rated poorly on economic freedom, placed 26th and 20th respectively. Consequently, these two economies have experienced economic stagnation, high unemployment and a decay of asset values, accompanied by a loss of confidence and social optimism.

Big Government and Unfree Labour Markets

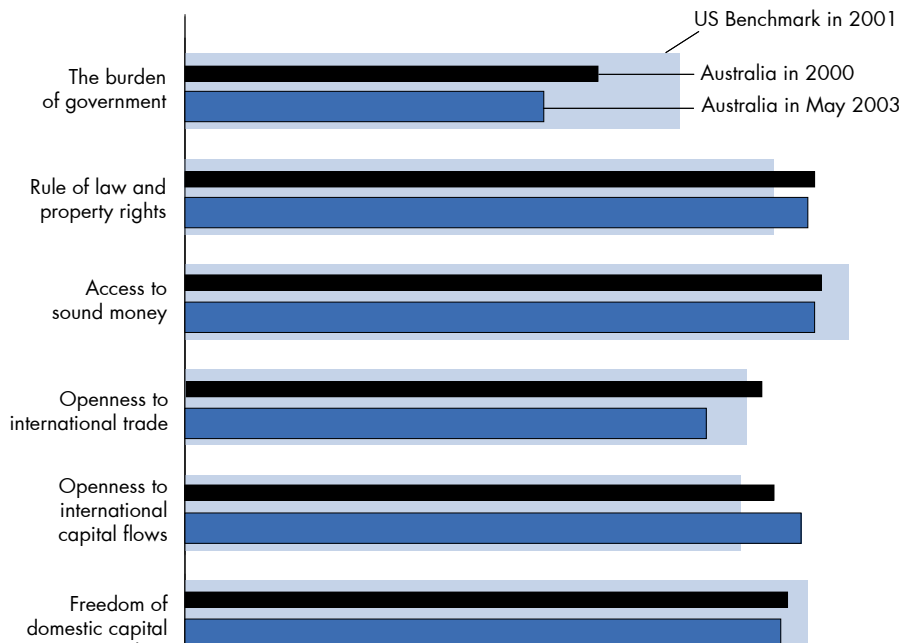
Figure 11.3 shows specific aspects of economic freedom, as measured by the Fraser Institute and *Economic Freedom Watch*. It reveals what detracts from a better freedom rating.

The lowest freedom rating of the Australian economy relates to the freedom to work, a fundamental human right. Many Australians are prevented from negotiating their own wage contracts with potential employers and thus securing their jobs. Minimum wage laws, detailed regulations, central wage fixing through a quasi-judiciary apparatus and union monopolies limit our freedom to work. The persistence of unemployment in times of respectable economic growth is explained by these restrictions of economic freedom.

Big government is the second major aspect that detracts considerably from the economic freedom of Australians (and foreign investors and enterprises who consider engaging here to create jobs and wealth). The burden of government in Australia has hardly improved since the 1970s. While the economic reforms of the 1980s and early 1990s did much to secure property rights, access to sound money and the freedom to trade and invest internationally, those in charge of government appear to have exempted themselves from the need to adjust to a more open, more competitive global economy. This places an increasing burden on individual citizens and companies, diminishing their chances of success in world and domestic markets.

The Main Components of Economic Freedom

Current ratings compared with the US benchmark and ratings in 2001



Sources: J. Gwartney and R. Lawson, *Economic Freedom of the World* (Vancouver: Fraser Institute, 2003); W. Kasper, *Economic Freedom Watch Report No.6* (Sydney: The Centre for Independent Studies, 2003), 3.

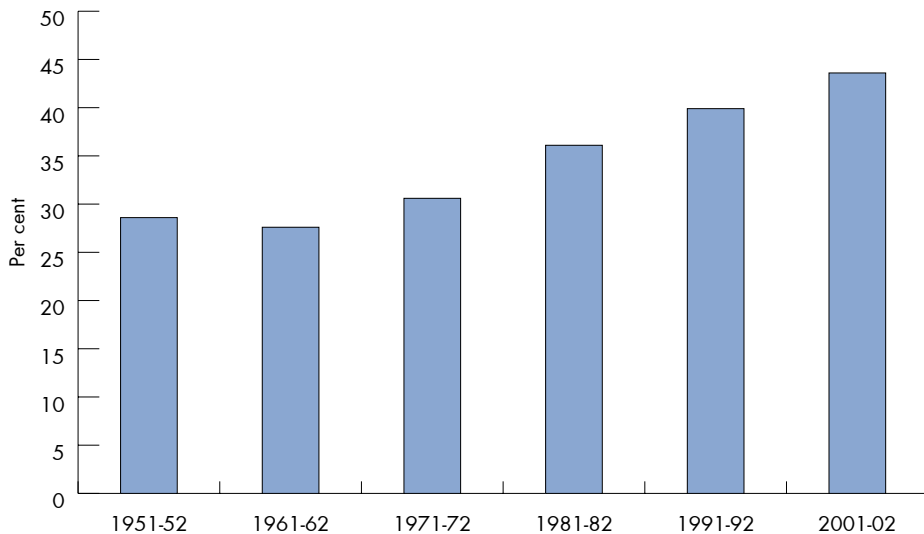
The Burden of Government

Figure 11.4a gives a long-term perspective of the size of the public sector in Australia (Commonwealth and State governments taken together). It can be seen that the claims of governments on the growing economic cake were reduced during the 1960s, from a war-bloated level at the beginning of the 1950s. Since then, the ‘government take’ has been pushed up steadily and relentlessly every decade, irrespective of which political party was in control, federally or at State level. By 2001-2002, the government share stood at 44%, higher than in most Anglo-Saxon market economies and markedly above the emerging free market economies of East Asia with whom we compete (there the government share averages 28%).

Government spending makes a positive contribution to economic welfare, in particular when governments protect private property rights and secure access for all to certain commonly shared amenities (such as roads and other public domain infrastructures). However, much of the relentless growth of Australian governments has been driven by political redistribution, that is the confiscation of private property by coercive means and the reallocation of these resources to better organised groups. A considerable part of the shift can also be attributed to churning of taxes and welfare handouts (see Chapters 7 and 8). Over the long term, this diminishes (economic) freedom and detracts from prosperity, opportunity and international competitiveness.

11.4a Size of Government, 1952-2002

Public sector outlay as a proportion of GDP



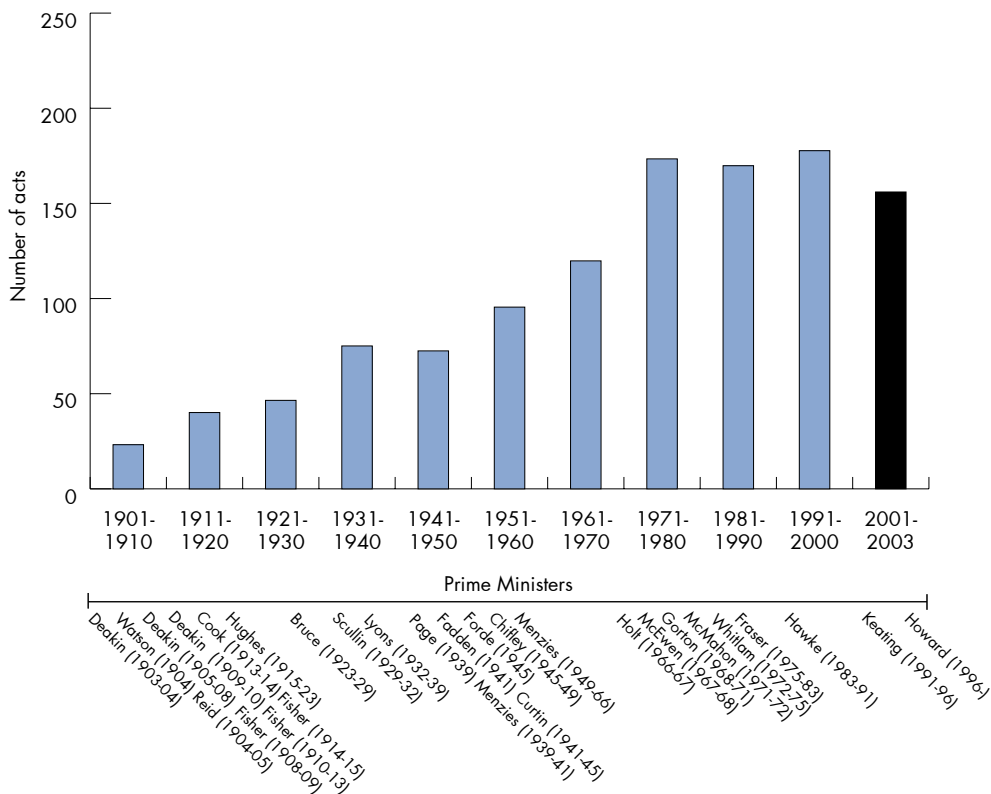
Sources: R.A. Foster, *Australian Economic Statistics, 1949-50 to 1996-97*, Occasional Paper 8 (Sydney: Reserve Bank of Australia, 1997); ABS, *Government Finance Statistics 2001-02*, Cat. 5512.0; ABS, *Australian Economic Indicators*, Cat. 1350.0 (Canberra: ABS, 2003).

Figure 11.4b illustrates another aspect of the burden of government, namely the trend of the Commonwealth Parliament since Federation to impose more, and more detailed, prescriptive legislation on Australian citizens. From an annual average of some 25 acts passed in the early years of the Commonwealth of Australia, the volume of new legislation (and ensuing administrative regulations) has risen relentlessly, irrespective of which party controlled the Parliament. There was a particular shift to legislative activism in the late 1960s and early 1970s, at a time of relative economic prosperity. Economic freedom was subsequently diminished, and the economic welfare of Australian citizens suffered. Parliamentary activism subsided somewhat during the 1980s, but reached new heights in the early 1990s.

Citizens cannot know or obey all these acts, even if they wanted to, and governments do not have the resources to enforce much of the legislation. The side effects of many of the 200 new acts, which the Commonwealth Parliament is now inflicting every year, cannot be known, but it is certain that they include high and rising compliance costs and frequently limit individual freedom and self-responsibility.

11.4b Commonwealth Legislation, 1901-1997

Number of new acts, decade annual average



Source: Attorney General's Department, <http://scaleplus.law.gov.au/legislation.htm>

Protecting Private Property Rights

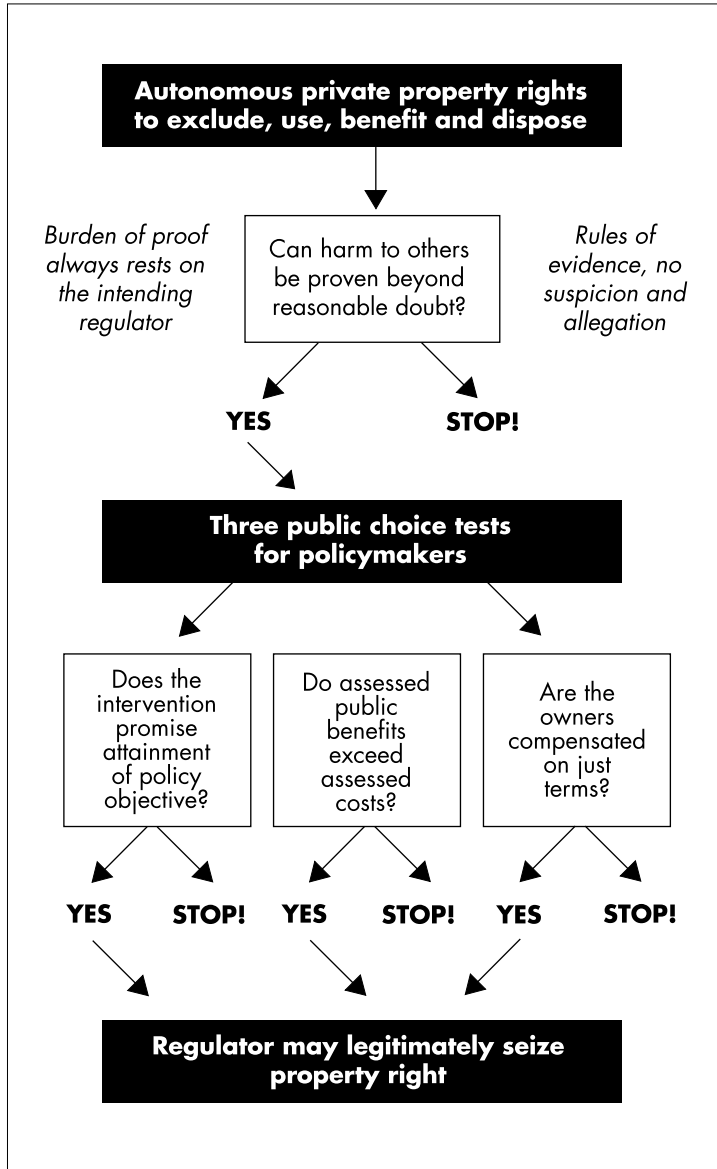
Secure private property rights have been the foundation, not only of economic freedom, but the freedom of citizens in general. Advances in economic freedom have normally preceded advances in civil and political liberties, both in European history and more recently in East Asia. In recent decades, a branch of law and economics called ‘public choice economics’ has alerted us to numerous reasons why private property rights tend to be endangered by powerful individuals, cartels, unions, law courts and elected parliaments.

Figure 11.5 (overleaf) depicts the legal tests that should be conducted in a system of secure property rights and a system that takes the maxim of economic freedom seriously. The right of owners to exclude others from using their property, to use the many different rights that property conveys and to dispose of the property as they see fit (in short full property rights) can be legally interfered with when this harms others beyond doubt. Such tests are frequently conducted in courts. British/Australian law has developed rules of evidence and other procedural protections that should apply. If no provable harm is alleged, rightful property owners do not have to prove anything.

The taking of a private property right should not be considered if the intervention does not plausibly promise that this will advance the policy objective, that the benefits to the community do exceed the costs of confiscation and that rightful owners are justly compensated.

Numerous case studies show that, time and again, individual property and other human rights are taken away without such rigorous tests. Indeed, there is a rapidly growing political tendency in Australia and overseas to short-circuit the taking of private property rights by legislators, judges and administrators for various political purposes not only when the exercise of a private property right causes proven harm to third parties but also when someone alleges or fears future harm. For example, environmentalists demand the application of ‘precautionary principle’, using their fear of environmental damage to justify the confiscation of an individual property right.³ A similar precaution as to human welfare and economic prosperity is then frequently rejected.

11.5 The Rule of Law: Property Rights and Regulation



Source: W. Kasper, *In Defence of Secure Property Rights*, Occasional Paper No. 84 (Sydney: The Centre for Independent Studies, 2003).

12. AID & DEVELOPMENT

HELEN HUGHES

Introduction

China, other East Asian countries and India have grown strongly during the last 20 years, following the excellent performance of the East Asian ‘tigers’ (Hong Kong, the Republic of Korea, Singapore and Taiwan), and of other rapidly growing East Asian countries (Indonesia, Malaysia and Thailand) to 1997.

At the end of World War II, Latin America was far more advanced than Asia. The Middle East and North Africa are petroleum rich. But in spite of the rapid growth possibilities of ‘catching up’ for developing countries, these two regions’ growth rates have lagged over the past two decades so that their standards of living have fallen behind industrial countries.

Because of their large populations, rapid growth in China and India has more than halved absolute poverty in the world from a peak of 1.5 billion people in 1980, mainly in Asia, to 650 million people in 2000, mainly in Sub-Saharan Africa. In this region, repression and resulting civil insurgencies and cross border wars have increased poverty to a new peak of 360 million people in 2000.

The reasons for the failure of development have been thoroughly researched. Countries’ own domestic policies are the principal determinants of economic growth. Most developing countries, notably those with high natural resource endowments that create windfall incomes and hence ‘economic rents’ (profits in excess of the competitive level), have opted for policies that favour wealth creation for elites rather than agricultural productivity, employment and incomes for the majority of their peoples. Although the islands of the South Pacific have received the highest aid per capita, they are among the most slowly growing countries of the world.

Financial aid to developing and transitional (former European and Central Asian communist) economies totals over \$50 billion a year. But, like income from rich natural resources, aid has become a source of economic rents which distort economies in favour of government expenditures, creating a bias against farmers and other entrepreneurs and encouraging corruption. Aid has thus been a major contributor to keeping in power elites who pursue exploitative policies. Without the support of aid, many of these would have long fallen.

‘Boomerang’ aid is also funded by economic rents from aid. It accrues in the form of salaries and fringe benefits such as travel granted to large numbers of bilateral and multilateral aid workers and consultants.

Global Growth Trends

Figure 12.1 illustrates global growth trends during the past 20 years in terms of developing and transitional countries' incomes as percentages of industrial countries' incomes.

China and other leading East Asian countries and India have had the highest growth. Singapore has bypassed lagging industrial countries. Taiwan and the Republic of Korea are close behind. Indonesia, Malaysia and Thailand grew rapidly until the early 1990s, but the counterproductive policies they adopted led to 'crony capitalism' and the financial crisis of 1997. Together with the Philippines these ASEAN (Association of South East Asian Nations) members have failed to reform their policies, producing correspondingly fraught economic performances and the potential for political disturbances. The region also has very poor performers, notably, Burma, Cambodia, Laos and the South Pacific. After 40 years of very low growth, India's economic performance improved in the early 1990s. Other South Asian countries, however, continue to lag.

Latin American average per capita income has fallen from 36% to only 26% of average industrial country incomes since 1980. Chile is the only strong economic performer. Petroleum rich Middle East and North Africa's per capita income has fallen from 28% to 21% of the industrial country average in the same period.

Sub-Saharan Africa's percentage of industrial country per capita income has fallen from 9% to 5% during the past 20 years. Such decline is not inherent in these countries' histories or natural endowments. Mauritius and Botswana have grown strongly, improving their standards of living markedly.

12.1 Developing and Transitional Countries: population and per capita income as a percentage of the per capita income of industrial countries, by region, 1980 to 2001.

	Population	Per capita income 2001 (PPP in 1990 dollars)	Per capita income as a % of industrial countries average per capita income	
	Millions	US\$	1980	2001
China	1,275	3,583	7	16
Other East Asia and Pacific	553	5,380	16	24
Latin America and Caribbean	527	5,812	36	26
Middle East and North Africa	385	4,623	28	21
India	1,024	1,957	6	9
Other South Asia	349	1,456	6	6
Sub-Saharan Africa	671	1,146	9	5
Central Europe	95	6,999		31
Eastern Europe and Central Asia	317	4,451		20
Industrial countries	859	22,516		100

Source: Angus Maddison, *The World Economy: Historical Statistics* (Paris: OECD, 2003).

Aid Flows to Developing and Transitional Countries

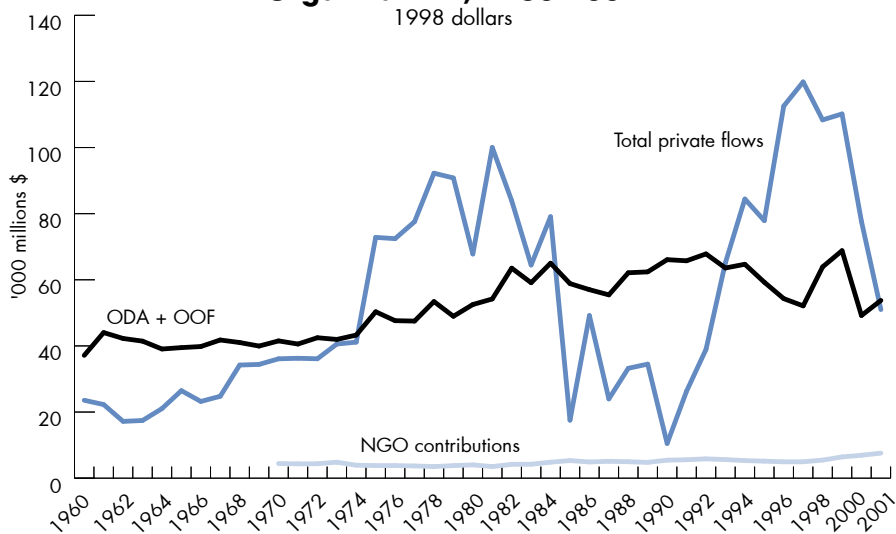
Figure 12.2 shows the flows of official bilateral and multilateral aid from the Western democracies to developing and transitional countries from 1960-2001. The concessional component of bilateral and multilateral loans is included.

Private commercial flows were much higher than aid flows. They fluctuated with economic conditions, being concentrated in rapidly growing countries. But private investment only succeeds in generating employment and income when it goes into countries with economic policies conducive to competitiveness and openness. In monopolistic economies it distorts income distribution and creates greater costs than benefits.

NGOs (Non Government Organisations) contribute about 7% of total aid. In addition, substantial taxpayers' funds add to NGO's incomes so that their influence is considerably higher than their contributions to developing countries.

Official aid funding is primarily from national, that is bilateral, sources, but multilateral financial organisations add commercial funding (to the costs of which they add administrative charges). These organisations, led by the International Monetary Fund and the World Bank, have become very powerful in the exercise of their lending functions, although they have created unsustainable debt for many countries. They have come to set aid policy agendas in collaboration with the multinational NGOs and the United Nations. Their focus, notably in their current Millennium Development Goals agenda, is on poverty alleviation through income redistribution rather than on increasing productivity and investment for growth.

12.2 Net Flow of Funds from Development Assistance Committee (DAC) Countries to Developing Countries and Multilateral Organisations, 1960-2001



ODA = Official Development Assistance; OOF = Other Official Flows

Source: OECD, *The DAC (Development Assistance Committee) Journal, Development Co-operation, 2002 Report 4:1* (Paris: OECD, 2003).

Aid and Growth

Figure 12.3 indicates that aid, far from promoting growth, is inversely related to it. The most rapidly growing countries and regions have had the lowest per capita aid not just in the recent past, but for the past 50 years. The slowest growing countries, notably in the Pacific, the Caribbean and Sub-Saharan Africa have had the highest per capita aid.

The inverse relationship between aid and growth is not accidental. Peter Bauer showed in the 1950s that aid flows, like high mineral incomes, had counterproductive economic, social and political effects that explain why high aid recipients, like most resource rich countries, have grown slowly. Their rates of exchange become overvalued, making the production of labour intensive goods for the domestic market and for export uneconomical, thus undermining employment creation. Because aid goes to governments, aid and resource rents encourage monopoly and swollen, uncompetitive public sectors.

Aid has been particularly ineffectual in alleviating poverty. Linking increased aid to poverty alleviation failed to reduce absolute poverty in the 1970s and early 1980s. The Millennium Development Goals agenda adopted in 2000 has also been ineffective. On the contrary, the diversion of resources from increasing productivity in agriculture and creating urban employment is delaying poverty alleviation. A decline in absolute poverty during the last 15 to 20 years mainly reflects improved domestic policies focused on investment and productivity in China and India, where aid has been negligible.

Aid maintains corrupt governments in power. The World Bank's research argued that if aid flowed to countries with 'good economic' policies it would be effective. Considerable doubt has now been thrown on these research results. The World Bank regards Ghana, Bolivia, Vietnam and Uganda as examples of successful policy reformers. This claim is also dubious. In Uganda, the most highly regarded of these reform cases, aid amounted to more than 55% of government expenditure in the 1990s, but per capita income grew at only 3% to 4% a year.

12.3 Developing Countries: Economic Growth and Aid Flows 1980-2001, by Region

	Average annual real % growth 1980-2001	Total aid flows 1980-2001 (1998 dollars)	Average aid per capita 1998-2001 (1998 dollars)
	Per cent	US\$ million	US\$
China	5.5	44,681	1
Other East Asia and Pacific	2.9	138,731	11
Latin America and Caribbean	0.5	121,932	10
Middle East and North Africa	0.5	203,050	13
India	3.7	51,800	2
Other South Asia	2.5	101,274	10
Sub-Saharan Africa	-0.4	352,534	20

Source: Angus Maddison *The World Economy: Historical Statistics* (Paris: OECD, 2003).

The Composition of Australian Aid

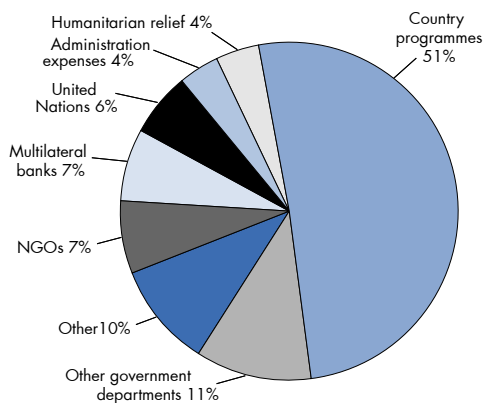
Australian taxpayers contribute more than \$1.5 billion annually to aid. This represented 0.22% of Australia's Gross National Income in 2001. The average for all industrial countries was 0.23%.

Figure 12.4a shows that about half of Australian aid went to global programmes, that is, for humanitarian relief, multilateral banks and UN agencies, to NGOs and for distribution by Australian government departments other than AusAID. Half went to country programmes.

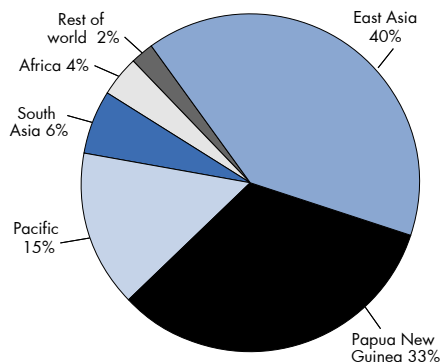
Figure 12.4b shows that the Pacific accounted for 48% of Australian country aid. Australia is the principal aid donor in the Pacific. France makes larger financial transfers to its Pacific colonies, but these maintain French nationals in the colonial civil service in Tahiti and New Caledonia. East Asia (including Indonesia, East Timor and China) receives 40% of Australian country aid. South Asia, notably India, receives much less aid than China. Low Australian aid flows to Sub-Saharan Africa recognise that it is not responsive to aid.

Australia committed considerable resources to restoring civil peace in the Solomon Islands in 2003 and has proposed to transfer more than \$2.4 billion to Papua New Guinea during the next five years. But there has been no change of economic policies in the Pacific. There is little evidence in roads, ports, power and water supplies, or education and health facilities, of the more than \$75 billion of aid (in 1998 dollars) that has flowed to the Pacific since 1970. Unless Pacific states respond with extensive policy reforms, aid will not be any more effective in the future than it has been in the past.

12.4a Composition of Australian Aid



12.4b Composition of Australian Country Aid



Source: Commonwealth of Australia, *Australia's Aid Program, 2002-03*, Statement by the Honorable Alexander Downer, MP, Minister for Foreign Affairs (Canberra, May 2002).

Aid Has Failed the Pacific

The islands of the South Pacific, the principal focus of Australia's aid effort, are a microcosm of Peter Bauer's theory of aid and development. Large aid flows since their independence, added to large incomes from minerals, timber and fish, have funded governments that have failed to adopt pro-growth policies. Nauru, which in 1968 had an accumulated income of half a million dollars per person, has since wasted phosphate export earnings of US\$3.3 billion (1998 dollars). It is now trying to use the Australian funds intended for rehabilitation of its mined land for recurrent expenditures and requests more aid.

As Figure 10.5 shows, population growth has exceeded income growth. Most of the benefits of growth have been appropriated by village elders, politicians and bureaucrats. The hard work of Pacific village women in gardens and orchards has fed the growing population and produced cash crops. Most men, however, are ageing into their 30s and 40s without income earning opportunities because communal ownership of land stultifies agricultural development and there are no urban jobs suitable to Pacific levels of labour productivity. A plague of crime and violence has followed, notably in Papua New Guinea and the Solomons, but also in other islands.

Standards of education and health remain among the lowest in the world. Only the islands of emigration—Samoa, Tonga, the Cook Islands and Niue—have primary and secondary schools that enable their young people to find jobs abroad. High infant and maternal mortality rates reflect the high number of births per woman and inadequate health facilities. Malaria control contributed to rising longevity, but has slipped in recent years in several islands. An AIDS epidemic threatens.

10.5 Pacific Economic Indicators

	Land area km ²	Population 000 s 2000	Density people/km ² 2000	Annual % growth 1970-2000 Population	Real GNP per capita
Papua New Guinea	463,000	5,200	11	3.7	0.3
Fiji	18,272	812	44	1.9	2.7
Solomon Islands	28,530	447	16	3.9	-0.4
New Caledonia	19,103	213	11	3.2	(NA)
Vanuatu	11,880	197	17	4.6	-0.3
Samoa	2,935	170	58	0.6	0.8 ⁽⁷⁾
Micronesia Fed. States	702	118	6	3.3	(NA)
Tonga	699	100	143	0.5	2.6
Kiribati	690	91	132	2.8	-1.2
North Marianas	477	70	68	(NA)	(NA)
Marshall Islands	181	50	36	2.9 ⁽²⁾	(NA)
Cook Islands	240	21	88	0.0 ⁽²⁾	(NA)
Palau	458	20	23	(NA)	(NA)
Nauru	21	12	571	(NA)	(NA)
Tuvalu	26	11	423	1.6	-1.4
Niue	259	2	8	(NA)	(NA)
Tokelau	10	1	100	(NA)	(NA)
Pacific average				3.4	0.6

Source: Compiled from World Bank, Asian Development Bank and *CIA Factbook* data.

Summary

Standards of living improved much more slowly in most developing countries in the second half of the 20th century than conditions warranted because of restrictive domestic economic policies. The reduction of the numbers living in absolute poverty during the last 20 years largely reflects economic policy reforms in China and India and even these have not met opportunities for development. The failure of most developing countries to take advantage of the growth possibilities inherent in 'catching up' has made a mockery of the hopes of post World War II independence movements. Millions of people remain so impoverished that they cannot even consider migration, but enough growth has taken place to create frustrated middle income groups that want to emigrate to the liberal West. If developing countries do not turn toward greater economic freedom, the migration pressures will increase.

Affluent leaders of developing countries crowd the forums of the United Nations and other international gatherings. Official and NGO multinational aid agencies have become world centres of privilege and power. But at best, the per capita incomes of developing country citizens average only a fifth of those of industrial countries. More than 350 million people in developing countries still live in absolute poverty.

The exploitation of minerals, timber, fish and high aid flows have thwarted development in the Pacific. After 25 years of independence, the Pacific should be well on the way to industrial country living standards. Instead, secondhand dresses and trousers dominate clothing purchases, most Pacific Islanders do not have sewerage, water and power, and education and health standards are minimal. It is not surprising that thousands emigrate every year.

After World War II, industrial countries liberalised their economies to achieve high living standards. But they allowed multilateral agencies—the UN, development banks and NGOs—to dominate aid policy and implementation. Industrial countries merely supplied the funding for aid. They ignored remaining protection of agricultural and labour intensive products that still cost developing countries more than US\$300 billion a year. This is six times the US\$50 billion of annual aid flows to developing and transitional countries. Reducing agricultural and labour intensive product protection would not automatically stimulate development as that largely depends on liberalisation in developing countries, but it would enable developing countries that do adopt liberal economic policies to grow much faster.

The industrial countries' concern with development can no longer remain merely humanitarian. The failure of development is the principal reason for the pressures of migrants that threaten to swamp the ability of industrial countries to absorb immigrants, so that the very liberal institutions that created the conditions that attract migrants are threatened. Industrial countries can no longer afford to leave development to the multilateral organisations (including NGOs) that have so conspicuously failed to achieve it. Hopefully, in the Pacific, Australia will be able to reverse the history of the failure of aid by binding aid to the principle of mutual obligation. Pacific states must adopt the reforms they need to provide the living standards their people deserve.

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