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The Answer to Inflation

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CONSUMER PRICE DISCOUNTS:
THE ANSWER TO INFLATION

Inflation in Australia has produced a welter of confused argument about possible remedies, generally resulting in a vague suggestion that we must "tighten our belts"; "produce and export more"; and accept "heavy financial restrictions" to solve the problem. The latter generally embraces increased taxation, restrictions on bank lending, higher interest rates and a multitude of controls.

The superficial philosophy behind these so-called remedies aims at allowing "supply to catch up with demand". While academic argument distinguishes between what is called "cost inflation" and "demand inflation", when it comes to remedies the restriction of demand is the only factor taken into account.

Thus we have a paradox, in which the constant policy of tackling inflation by increasing charges, taxation and costs never varies. All evidence points to consistent failure wherever such policies have been adopted. Undeterred by the evidence, however, the same policies are continuously applied.

Nemesis now awaits not only the economist, but also his victim — the man in the street.

The effect of this unvarying repetition is to produce economic class warfare. The housewife opposes the grocer and the butcher. The worker wages war on industry. Country resents the city, and everyone bites the hand which feeds him. Such a situation is the seed-bed of revolution.

One control increasingly advocated is control of wages and prices — even though advocates of this policy concede that it provides no solution.

The truth is that every restriction on production is a further sabotage of the productive system. Each producer is himself a consumer. His output is largely governed by what he has to buy — the materials and services that he requires. Every squeeze in the economy — every increase in taxation, rates, charges and subsequently wages — limits his real potential.

Unfettered from the restrictions which industry now suffers the potential to increase the range, quantity and quality of production is almost limitless. Those who talk about "tightening our belts" must face the fact that they are advocating further restrictions on productive capacity — restrictions which have now produced real dislocation in the economy.

The concept of reversing progressive inflation through a policy which **reduces** the prices of basic items in the economy by subsidisation is often brushed aside as unworthy of serious consideration. It is argued that this concept is a new and revolutionary one, running contrary to the axioms of sound finance; that subsidisation would mean increased government controls, and some form of government price control; unnecessary surpluses would be subsidised; that a programme of subsidies would mean a substantial increase in taxation to pay the subsidies.

These arguments are all false. The concept of a comprehensive price-subsidisation programme is **neither new nor revolutionary.** It was introduced during the second World War in the United Kingdom, Canada, New Zealand, Australia and, later, the U.S.A. A new type of financial policy was made necessary by the war situation which smashed the widespread myth that the depression conditions in the 'thirties were "the result of an inevitable shortage of funds. Any suggestion, however moderate, of alleviating the depression conditions, — of permitting unemployed men to work on unused equipment and resources — was met with the hostile criticism that this would be "inflationary" and certain to cause greater havoc.

Surely, where all available evidence flies in the face of dogma, it is time to take another look?

Few would deny that one of the legitimate functions of Government is to ensure that the community has a monetary system which is just, honest, and which serves the people's requirements. Severe penalties are imposed upon those who seek to increase the volume of currency (dollar bills) illegally by counterfeiting. The provision of a just and honest money system is comparable with the Government's insistence on proper weights and measures. This all comes under the general heading of the Rule of Law. Satisfactory buildings could not be erected if the measurement system were constantly being changed. How can a satisfactory economic system be operated if the value of the monetary unit is progressively getting less?

Both Communists and Socialists understand this. John Strachey, former communist theoritician and socialist planner in the Attlee government, re-echoed the views of Karl Marx, who, in the **Communist Manifesto,** said that the ten steps he proposed for communising a State were merely means to an end, not ends in themselves, and that they would in due course "necessitate further inroads upon the old social order". Strachey wrote in his book **"Programme For Progress"** that inflationary credit policies were "an indispensible step in the right direction". Strachey said that . . . "the fact that the loss of objectivity and the intrinsic value of the currency which is involved (i.e. inflation) will sooner or later make necessary, on pain of ever-increasing dislocation a growing degree of social control . . . for the partial character of the policy will itself lead on to further measures. The very fact that no stability, no permanently workable solution can be found within the limits of this policy will ensure that, once a community has been driven by events to tackle its problem in this way, it cannot halt at the first stage, but must of necessity push on to more thorough-going measures of re-organisation".

"CONTROLLED INFLATION"

Price is an essential feature of money. The expansion of the nation's money supply — the bulk of it in the form of financial credit (cheque money) — without reference to prices is highly irresponsible and immoral. It robs those on fixed incomes and those who have saved or invested. A government which openly says that it is following a policy of "controlled inflation" is admitting that it is pursuing a policy which robs people of their savings. It comes within the scope of a Government's provision of a Rule of Law for a monetary system to ensure that instead of inflation. which reduces the value of the monetary unit, there should be a reduction in the price level reflecting the real costs of production.

Immediately upon the outbreak of the second World War, the problem of a "shortage of finance" disappeared. Thousands of millions of pounds of new credit money was brought into existence through the well-established mechanism of modern banking. The well-known Australian Government adviser during the war years Professor L. G. Giblin, states in his authoritative work The Growth of a Central Bank, that "The (Commonwealth Bank) Board in 1942 recognised that a great expansion of central bank credit was necessary to finance the war . . ." In accordance with established practices of banking, the expansion of central bank credit enabled the Trading Banks to expand their supplies of new credits also. All this new credit money was issued against the nation's vast unused productive capacity, much of it, of course, devoted to a massive military programme. But it was demonstrated that it is nonsense to talk of an inability to use men and resources because of a shortage of money.

However, in the nature of the present finance-economic system, a great expansion of new financial credits, particularly with much of it being devoted to capital production (war industries, etc.) has the effect of increasing the price level. An increasing price level erodes the value of wages and salaries. The result is a demand for increases in wages and salaries to offset the erosion of the money value. But increased wages and salaries. which can only be financed out of further expansions of new financial credits by the banking system, must in turn be costed into prices, by employers, thus stimulating further what is often called the "price spiral".

Prior to, and for a short period after the second World War, the Basic Wage in Australia was governed automatically by what were known as the "C Index Series". This series of figures concerned the prices of certain foods, clothing, rents, etc. Inflation during the war was readily seen to be a serious threat to stability. It was rightly regarded as essential to offset it. Price control was introduced, but what today's advocates of price control fail to realise was quickly grasped at that time — namely, that price control could never halt inflation. Price subsidies were the main method adopted, the underlying concept being that if, in Australia, the items in the C Index Series were subsidised — i.e. reduced in price to the consumer without penalising the producer — this would in fact be a **real increase in** purchasing power without the necessity for wage increases.

Explaining the need for the subsidisation programme, the Minister for Customs, Senator Keane, was reported in **The Sydney Morning Herald, April 14th, 1943** as saying: "We must not look upon subsidies under the new plan as payments to which an industry is not entitled. They are not payments because the industry is inefficient in comparison with other industries, and they do not resemble doles. They are payments because the Government considers it **more economical to meet increased costs through subsidies rather than through rising prices".**

What was the attitude of the Opposition — a Liberal-Country Party Opposition as at present?

A study of the Hansards reporting the debates in the Federal Parliament on the introduction of price subsidies reveals that there was no dissent from the Leader of the Opposition, the then Mr. R. G. Menzies, or his colleagues Mr. John McEwen and the late "Artie" Fadden, and the Bill was not opposed.

Commonwealth Year Book No. 37, (1946-47) gave extensive details of the war-time measures:

> "Immediately after the outbreak of war the Commonwealth Government undertook control of prices and issued proclamations fixing as maximum prices of certain goods those prevailing on 31st August, 1939". However, it was soon discovered that price controls did not contain cost rises: "In order to avoid delays in the distribution of goods, general principles were adopted late in September, 1939, providing for the automatic adjustment of prices to increases in costs . . . An important change in the methods of price control was introduced in April, 1942 by the issue of Prices Regulation Order No. 666 which limited the trader's profit margin to the actual money margin obtaining on 15th April, 1942. From that date onwards the trader was allowed to increase his prices only by the actual amount of the increased cost. Increases in money margins were permitted only with special approval. This new principle was adopted because of the inflationary effects of increasing costs, increasing turnover and percentage profit margins on pre-war basis . . . Following the entry of Japan into the war in December, 1941, costs of many goods imported into Australia rose substantially as did costs of certain locally produced goods because of the transfer of a very large proportion of efficient labour from productive industry to war services. The retail price index number rose by 9.5% in the first 12 months of the Pacific war . . .

The next phase of price control was designed to secure price stability . . . On 12th April, 1943 Prices Regulation Order No. 1,015 fixed, as ceiling prices, the prices actually being charged by individual traders on that date . . . The ceiling applied not only to prices but to all prices, at every stage of production, manufacture and distribution . . . **The price ceiling could not, however, eliminate all rising costs**

. . . Government policy provided that, in future, **necessary relief from increased costs could be met either by price adjustment or payment of price stabilisation subsidy".**

On page 461 of the same Year Book a special description under the heading **Treatment of Costs and Subsidies**, the following comments were made:

"Although the Price Stabilisation plan provided for certain increases in prices, price rises up to the end of 1946 were the exception rather than the rule. When increasd costs could not be absorbed within the process of production or distribution, they were met generally at the source of payment of subsidies and thus were prevented from disturbing the whole price structure".

Section 11, under the heading **Action Taken On Price Increases:** "The Government was aware at the time it introduced the Price Stabilisation Policy that this situation (i.e. a rise in prices) would probably arise, and as soon as it was advised of the nature and extent of the rise it took necessary steps to absorb the rise in costs, **firstly by undertaking to refund to employers amounts paid as basic wage increases, and secondly** by reducing prices in such a way as to offset the price increases that had occurred. These measures were announced on 21st July 1943. The price of tea was reduced by 1s/2d per lb. to its pre-war level, and the standard retail maximum price for potatoes was fixed at 5 lb. for 6d. In the former case importers, and in the latter case growers, received a subsidy. At the same time, also, sales tax on clothing and textiles was reduced from 12½% to 7½% to take effect as existing stocks were cleared.

The range of commodities chosen for price reduction was small but all were universally consumed so that it was certain that the benefit of the reduction would be spread throughout the community".

EXPENDITURE ON PRICE STABILISATION SUBSIDIES — 1943-44 to 1946-47

Item	1943-44	1944-45	1945-46	1946-47
Potatoes	£1,725,446	2,433,492	2,829 648	3,012,170
Tea	2,460,612	2 188,292	2,356,176	4,413,702
Milk	318,976	1,785,946	2,517,247	2 252,649
Recoupment of Basic Wage	1,101,603	801,891	555,372	2 307,435
Imports (other than tea)	967,041	2,436 683	3,006,464	3,690,859
Coal	101,268	182,767	456,657	958,949
Firewood	199,679	305 221	201,204	314,852
Rubber	—	98,783	141,200	333,575
Raw Wool	—	—	—	3,416,876
Tobacco	—	—	250.000	617,704
Other Expenditure	131,035	576,349	669,766	1,322,137
TOTAL	7,005,660	10,809,424	12,983,734	22 640.908

The effect that price subsidies had on prices can be seen from the next figures. Price control on its own from 1939 did nothing to halt inflation. But from 1943 to 1947, consumer subsidies, at a time of drastic war effort, resulting in chronic domestic shortages, held the price structure at a stable level:

RETAIL PRICE INDEX-NUMBERS 1939-47
(Base of each group: September Quarter, 1939 equals 1,000)

Period	Food	Rent	Clothing	Miscellaneous	"C" Series All Items
Sept. 1939	1000	1000	1000	1000	1000
Sept. 1940	1019	1006	1146	1049	1046
Sept. 1941	1017	1009	1349	1117	1102
Sept. 1942	1147	1009	1605	1155	1207
Sept. 1943	1126	1008	1734	1212	1237
Sept. 1944	1126	1008	1714	1211	1233
Sept. 1945	1130	1008	1693	1208	1229
Sept. 1946	1118	1009	1819	1214	1251
Sept. 1947	1200	1010	1873	1262	1301

REFERENDUM TO CONTROL PRICES

In 1948 the Chifley Government sought powers, by referendum, to control prices in peacetime. This was rejected. In a Press statement on November 12th, 1949, the then Mr. Menzies said: "When, at the referendum of 1948, the people refused to give permanent price-fixing powers to the Commonwealth, the present government did two unpardonable things. First, it threw price control to the States, hoping they would make a mess of it. **Secondly, it withdrew most subsidies which had been created to keep down the cost of living.** While encouraging production to the full, we shall hold ourselves ready to **pay price subsidies in appropriate cases — as for example on those items affecting the basic wage-earner's cost of living".** He was referring to the dismantling of the price subsidy mechanism which had proved so successful during the war.

Taking advantage of the immediate rise in costs which resulted, the Liberal-Country Party Opposition launched a simple and direct policy campaign for the 1949 Federal elections. They promised to reduce the burden of government. They promised to reduce taxation. And they promised to **put the shillings back into the pound** — clear acknowledgement of the mood of the electorate on inflation.

What techniques did they aim to use?

POLICY STATEMENTS OF PARTY LEADERS

It is illuminating to look back on the policy statements of Party leaders in the Opposition at that time:

On November 8th, 1949 the **Sydney Morning Herald,** under the headline "Subsidy Plan, McEwen on Inflation" said:

> "The Country Party, if returned at the elections, would restore subsidies on vital foods and clothes to increase the purchasing power of money, the Deputy Leader of the Country Party, Mr. J. McEwen said at Kyabram tonight. Mr. McEwen, who was opening his campaign said no greater service could be performed for the wage-earner than to arrange for his money to buy more. Under the Labor Government, wage-earners had seen the value of the pound shrinking and buying less. The Country Party had a clear-cut policy to make the weekly wage worth more by encouraging production, paying subsidies where possible, and making a vigorous attack on indirect taxation".

On November 11, 1949, the **Sydney Morning Herald** reported Mr. Menzies as advocating the restoration of "Parliamentary control over the Commonwealth note issue to check inflation of currency". He went on to say: "This is our great year of decision. Are we for the Socialist State, with its subordination of the individual to the universal officialdom of government, or are we for the ancient British faith that governments are the servants of the people, a faith which has given fire and quality and direction to the whole of our history for 600 years? Every extension of government power and control means less freedom of choice for the citizen. The best people in this community are not those who 'leave it to the other fellow' but those who by thrift and sacrifice establish homes and bring up families, and add to the national pool of savings and hope some day to sit under their own vine and fig-tree, owing nothing to anybody. Socialism is the politics of dependency and decay. And for a final count there is another charge, not to be made lightly. The Socialist doctrine has lost all spiritual content. It tells me all the time that my brother is my keeper. It forbears to tell me that I am his keeper; that his rights are my duties. Its attitude induces a deep cynicism about all spiritual values. It is, as Church leaders have pointed out, the lineal descendant of the gross materialism of Karl Marx **A resolute reduction in the burden of government and with it, in the rates of tax, will mean reduced costs of production"**

One day later, on November 12th. **The Sydney Morning Herald** again quoted Menzies: "On the true cost of household r quirements the pound was worth only 10/- compared with 1939. The greatest task, therefore, was to get value back into the pound by reducing prices. Increased production was needed. While encouraging production, a Liberal-Country Party Government **would pay price subsidies on items affecting the cost of living of basic wage earners".**

That this was no flash-in-the-pan pre-election gimmick is shown by the fact that the Country Party leader Mr. Fadden had announced the same policy 11 months earlier. On January 28th, 1949, **The Argus** (Melbourne) reported: "Restoration of subsidies would be advocated by the Federal Country Party as part of its platform for the Federal elections Mr. Fadden, leader of the party, said yesterday. **'Our policy of stabilised commodity prices is designed to improve the real purchasing power of wages, health and nutritional standards by increasing consumption'**, he said. 'The Country Party's proposal is to restore subsidies to commodities which are rising in price and are contributing to the already exorbitant living costs".

SOCIALIST PLANNERS CRITICISED

A number of Opposition members, the most prominent being Mr. Fadden and Country Party members, during the pre-1949 election period, strongly criticised Dr. H. C. Coombs and other Socialist planners who were advising the Chifley Government.

Probably, never before has an Opposition stated more clearly the policy it proposed to implement immediately it was elected. The Australian electors supported that policy by providing the Menzies-Fadden Government with a substantial majority at Canberra. It is quite clear that leaders of the new government believed that price control was unnecessary for effective price subsidisation. The referendum had just been held. Mr. Menzies' statements made his beliefs quite clear.

It was clear too, that action was contemplated along the lines promised as soon as the new Government gained office. On January 26th, 1950, **The Sun** (Melbourne) reported: "As a first step in bringing value back into the pound, the Federal Government is likely soon to subsidise some commodities in the Cost-of-Living Index. Cabinet plans to begin its anti-inflation drive, in fulfilment of election pledges, on February 7th. Appointment of a Ministerial Economic Policy Committee was announced today by the Prime Minister (Mr. Menzies). The Committee, he said, would start work next week with a team of experts **so that Government could formulate a policy on price subsidies at once".**

GOVERNMENT BLUFFED

Two months after the 1949 elections, the new Coalition Government was still expressing strong determination to solve the problem of rising prices through the restoration of price subsidisation. But "the experts" — the very socialist planners who Mr. Fadden had so strongly criticised in Opposition, clearly bluffed the government, demonstrating the enormous power which they wield. Three days after the date set for the anti-inflation drive (February 7th) the Government announced the appointment of Dr. Coombs as Chairman of the newly-created Commonwealth Bank Board, which replaced the Advisory Council created by the Chifley Government. Dr. Coombs — a Fabian-Socialist planner — had supported the Chifley Government's proposals to nationalise the Australian banking system — i.e. to establish a complete State monopoly of credit power.

But the Menzies-Fadden Government's banking proposals were in substance **a continuation of the Chifley proposals. The Age** (Melbourne) commented editorially on March 17th: "The present Government has been well advised not to carry its electoral victory on banking to extreme or vindictive lengths. The re-constituted controlling authority effects little change in substance".

There was widespread unrest in the Liberal Party concerning the evidence of retreat from election policy. **The Daily Telegraph** (Sydney) on March 28th, 1950 reported: "State Council of the Liberal Party last night attacked the Menzies Government's Banking Bill. The Council rejected a motion declaring the Bill contrary to Liberal policy by over 50 votes to 40 on a show of hands".

RETREAT FROM ELECTION PROMISES

By April 5th, 1950, the Prime Minister had formally capitulated to the socialist planners. **The Sun** (Melbourne) of that date, reported as follows: "Mr. Menzies said that putting the value back into the pound was not the Government's responsibility. It was the peoples'." From then on there was no more talk of restoring price subsidies. There was a steady retreat from the brave words and promises of the pre-1949 Federal elections.

A report from Canberra about 6 months after the election quoted a top Fabian as saying, "We were worried for a period, but we now have the situation under control".

Questioned in the last period of their 23 years on the Treasury benches, Government leaders flatly contradicted the statements of their leaders prior to 1949. In fact the replies to the subject of consumer subsidies over a period to many correspondents were so uniform in expression that it is clear that Ministers were merely signing their names to answers devised by their advisers — the socialist planners. For example, a letter from Mr. Andrew Peacock dated August 12th, 1971, at a time when he was Minister assisting the Treasurer, said:

" . . . There are . . . several problems associated with a system of consumer subsidies. In order to be effective such a system would have to be accompanied by a comprehensive system of rationing and rigid controls over wages and prices. Without comprehensive controls over prices, for instance the Government would not be able to ensure that the prices of goods were decreased as subsidies were granted . . . If . . . the purchase of goods was made more attractive by artificially reducing prices to the consumer, demand would tend to outstrip supply . . ."

Exactly the same type of reply came from the Labor Party when they were returned to office in December, 1972. A letter from Mr. F. E. Stewart, Minister assisting the Treasurer, dated 4/7/73 said:

". . . It seems unlikely that any price subsidy scheme or partial tax abolition scheme would be successful unless accompanied by a rigid system of price controls and rationing such as that employed during and after the 2nd World War . . ."

This stock-in-trade answer from the planners, irrespective of which Party was acting as mouthpiece, had earlier prompted some inquiry as to how the few consumer subsidies in the form of bounties operated. The Country Party in particular championed the fact that certain bounties provided primary producers with cheaper products.

"POWERS REST WITH STATES"

On August 14th, 1970, Mr. Anthony wrote as follows:

" . . . As I mentioned in my previous letter to you, the effectiveness of any consumer subsidies would depend very much on the Government's ability to control prices. However, a proposal to give the Commonwealth Parliament power to make laws with respect to prices was rejected at a referendum held in May, 1948. Consequently, powers to make such laws now rest with the States. In regard to the bounties on fertilisers and tractors, there are only a small number of producers involved, and it is therefore possible to ensure that the respective bounties are reflected fully in the prices charged to consumers on these goods. Nevertheless, the Commonwealth does not have the constitutional power to actually control the prices finally charged for these goods".

Mr. Anthony elaborated on this in a further letter, dated September 18th of that year:

" . . . The legislation providing for the payment of subsidies on fertilisers. such as superphosphate, empowers the Minister for Customs and Excise to examine the records of the manufacturers to ensure that the full amount of the subsidy is reflected in ex-factory prices. This is a practical arrangement because there are only a few manufacturers of fertilisers in Australia.

In regard to the bounty on tractors, **competition from imported tractors** which account for a substantial proportion of the total sold in Australia ensures that excess prices are not charged by local manufacturers of tractors. Competition is, in fact, so keen that under recent drought conditions (which have affected sales of all agricultural implements) the financial results of manufacturing companies have been severely affected . . . "

Surely this is a contradiction of the statement that price subsidies can never work without price controls?

MEAT PRICES SPIRAL

In 1973, with a spiral in meat prices due to a world shortage of meat two New England economists proposed a system of consumer subsidies to provide the Australian housewife with meat at reasonable prices. Writing jointly, Professor John Dillon and Mr. Roy Powell, in a letter to the **Sydney Morning Herald** on May 1st, 1973, said:

"The Government's request to the Meat Board for proposals to stabilise meat prices causes concern. The reaction has obvious political overtones because of the timing of the announcement, just before the release of the latest consumer price index figures, and at the same time as various consumer lobbies are vocally protesting about meat prices.

On the other hand, items such as potatoes and onions, which also show a substantial rise do not evoke attention nor does the agricultural product which has shown the largest rise of all — wool.

The following points should be borne in mind, in relation to this issue.

Firstly, the implications of any form of action on meat prices are likely to have wide repercussions extending beyond the ambit of the Meat Board and its available expertise.

Secondly, a large proportionate rise in the price of a component is not sufficient justification for the action. The base period used for comparison may have been one of unusually low prices so that the increase is merely a return to more normal levels. International comparisons of meat prices tend to indicate that this may be so, at least in the case of sheep meats.

Thirdly, the agricultural sector has long been plagued by rigidly fixed prices which have failed to indicate and facilitate needed adjustments in resource use.

Meat prices are closely related to world market prices and indicate a relative shortage of meat. A dampening of incentives to increase meat production is likely to prolong this shortage and prevent the economy from taking full advantage of the present favourable situation.

Likewise, a more flexible and realistic pricing policy for dairy products and wheat may contribute more in the long run to increasing production and relieving market pressure than some artificially imposed pricing arrangements. However, the possible need for some short-term control may exist.

Fourthly, short-term benefits to consumers in the form of lower meat prices may best be provided by a consumer subsidy. This avoids the problems associated with trying to maintain domestic prices lower than world market price, such as dampening incentives to expand production and the need to enforce deliveries to the domestic market.

Finally, there are strong equity arguments against forcing one industry to bear the cost of stabilising consumer prices because its price has risen. This is inequitable as between particular agricultural industries, apart from the possible inequities of having the agricultural sector subsidise consumers. Action to stabilise and possibly subsidise prices to consumers is most equitably financed from taxation".

PRICE SUBSIDISATION

Another economist who has lent some weight to the general idea of price subsidisation is Mr. H. W. Herbert. of Queensland. Commenting on Mr. Snedden's 'mini-budget' in 1972, Mr. Herbert wrote in the **Sunday Mail** of July 16th:

"The tax concessions represent only a 2½% cut because of inflation. We should, therefore, cut sales tax in half, **and put a 5% Consumer Subsidy on,** providing it is passed on to the consumer. These two measures would help lower prices and reduce the crazy spiral of prices forcing up wages, which then force up prices . . . "

On July 22nd, in reply to questions on his article, Mr. Herbert wrote: "The subsidy on sales is of much less importance than cuts in sales tax, but the point you made, of being sure it is passed on to the consumer, is a sound one". Mr. Herbert went on to describe the application of consumer subsidies: "On some 10% of consumer purchases it would be easy to apply, as these are services sold by various authorities, namely fares, council rates, fuel and power. Another 8% of consumer purchases are goods usually sold at standardised prices, namely bread, milk, butter, eggs, sugar and tea. In most other items competition and price-cutting is keen especially in household appliances, hardware and furniture whose sales are particularly in need of stimulation because factory employment has fallen. Most of these lines are carrying 2½% Sales Tax, and some 27½%. The 2½% could come off, and the 27½% be reduced. Should a subsidy be paid as well, on items like radiators and tools? With keen competition it would be likely to be passed on, but some might object that 'tax revenue was going into maunfacturers' and retailers' profits'. If price surveys showed that the subsidy was not being passed on to the consumer, I think it would have to be withdrawn. It is too cumbersome for the consumer to present his receipts at some government office and collect the subsidy".

In answer to questions as to the source of finance for such consumer subsidies, Mr. Herbert replied on July 31st: This year when a large budget deficit is justified, **Consumer Subsidies could be paid for by new credits.** But some people would still say it was tax money going into retailers' profits. A receipt system for subsidies would be workable, but laborious compared with paying the subsidy to the retailer without any extra work".

In fact, a relatively small scheme already working gives a specific example, the principle of which could be varied to apply in a number of fields. That is the scheme which provides primary producers with cheap diesoleum fuel. Each producer is allocated a Diesel Fuel Certificate Number, once his bona fides has been established. Any Oil Company selling him fuel charges him 15 cents per gallon less than normal price. The Company sends in a return monthly of all such sales to the Department of Customs and Excise, and is reimbursed accordingly. There is no question that the discount goes to the consumer. The retailer is the agent for the transaction.

Ministers and other politicians replying to questions have stressed that any attempt to finance consumer subsidies from new credits would be grossly inflationary. Again, this begs the question, for just as important as the question of credit creation is the question of how any new credit is introduced into the economy. There are good grounds for arguing that the volume of money has been increased at far too great a rate in recent years but with an adverse effect on economic activity:

GROSS NATIONAL PRODUCT AND THE VOLUME OF MONEY — 1948-49 to 1973-74

Volume of Money ($ million)

Year	G.N.P.	Tot. Bank Deposits	Notes & Coin	Total	Ratio — Money to G.N.P.
1948-49	4,472	3,164	420	3,582	80%
1949-50	5,354	3,642	452	4 870	77%
1950-51	7,172	4 342	528	4 870	68%
1951-52	7 684	4,236	584	4,820	63%
1952-53	8,344	4,616	640	5,256	63%
1953-54	9.014	4,930	670	5,600	62%
1954-55	9,732	5 062	704	5,766	59%
1955-56	10,568	5,096	722	5.816	55%
1956-57	11,464	5.470	738	6,208	54%
1957-58	11,576	5 604	750	6.354	55%
1958-59	12,424	5,912	764	6,676	54%
1959-60	13,790	6,392	800	7,192	52%
1960-61	14 532	6,504	798	7,302	50%
1961-62	14,776	7,036	810	7,846	53%
1962-63	15.950	7,700	818	8,518	53%
1963-64	17,979	8 741	815	9,556	54%
1964-65	19,753	9,523	814	10,337	53%
1965-66	20,688	10,154	783	10,938	52%
1966-67	22 757	10,942	882	11,824	52%
1967-68	24,281	11,841	964	12,805	52%
1968-69	27,216	12,869	1,065	13,974	52%
1969-70	30 091	13,651	1,187	14,837	49%
1970-71	33,089	14,514	1,336	15,851	48%
1971-72	36 089	16,040	1,467	17,508	47%
1972-73	n a.	19,852	1,702	22,001	—

(Source for the preceding figures Reserve Bank Statistical Bulletins, Australian National Accounts, Treasury White Paper, National Income and Expenditure, 1963-64).

VERNON COMMITTEE REPORT

Commenting on this, the Vernon Committee Report said, inter alia, "The volume of credit may be measured in various ways. For the purpose of studying the impact on the economy of variations in the volume, however, it is normal to consider changes in the supply of money, defined as currency and banking deposits held by the public, **because this aggregate is directly affected by, among other things, credit creation.** The report went on to say: "If more bank credit had been made available, the rate of growth of the money supply would probably have been higher, the actual result depending on any changes in the other elements entering into the money supply, particularly the Government's cash position and movements in international reserves. To decide whether the money supply has been fully consistent with growth and stability requirements, it would be necessary to study in detail the part played by changes in it over the whole period, particularly at turning points in business activity. Credit has not always been available in adequate amounts to particular persons or for particular purposes. and growth may have been temporarily checked at particular times through credit stringency . . . The general level and price of credit, that is, interest rates, can be influenced in many ways by the monetary authorities — the Commonwealth Government and the Reserve Bank. Government fiscal policy may be designed to bring about a particular effect on monetary conditions. For example, when the Government is a net borrower — that is expenditure is greater than receipts — the liquidity of the banks may be increased. The opposite may occur when the Government is a net lender. The Reserve Bank, through its credit policy and in particular through changes in statutory reserve deposits ratios can affect the ability and willingness of banks to lend . . . "

However, what is not explained is why, despite an enormous escalation in the volume of money in recent months, the ratio of this increase to the Gross National

Product is **diminishing.** All evidence points to a growing disparity between incomes and prices. What is required, then, is a use of a percentage of the increase in the volume of money **to increase the purchasing power of incomes without at the same time increasing prices.** Had some of the recent growth in the money supply been used in a price subsidy scheme without a balancing cost impact, inflation might now be no more than an unpleasant memory.

COST COMPENSATION SCHEME

During the war, increases in wages were met through a cost compensation scheme. The employer was reimbursed by the Government, and consequently did not have to charge increased wages into the prices of his products. It is in this, and similar directions that the solution to the world's financial dilemma must be sought.

OVERSEAS EVIDENCE

As mentioned earlier, Britain used price compensation during the war years and kept it on subsequently for foodstuffs.

An article in a British Agricultural journal, **The Southern Farmer** (Nov. 1969) describes it thus:

"The price of food to the consumer has been kept reasonably low — certainly much lower than in the countries of the Common Market — in accordance with one of the better and most basic principles of the true Welfare State. Where the subsidies may go in the first place — whether to farmers directly, or to fertiliser companies and other manufacturers, distributors or merchants, is a matter of little consequence; they end up in the pockets of the consumers by providing them with food at considerably lower prices than they would otherwise have paid — **possibly lower, indeed, than the bare cost of production.** At the same time, the system has enabled the farmers of this country to build up what has become one of the most efficient agricultural industries in the world. While there is often well-justified criticism of the relative inadequacy of particular annual determinations to provide adequate margins for investment, or even a satisfactory income for many producers, the system has at least protected the farmers for the worst vicissitudes of the market, and provided a climate conducive to efficiency and stability in the industry".

FOOD PRICES SOAR

Britain's entry into the E.E.C. was however conditional on the dismantling of her cheap food subsidy system. Within months of entry, food prices were soaring, and the housewife was up in arms. A report from Chris Pritchard in London which appeared in the **Sun-Herald (Sydney)** on July 29th, 1973 described it thus:.

" . . . Food prices this week continued to soar. Baby foods, yoghurts, cheeses, sweets, chocolates, biscuits and crisps all went up (with motor tyres and other items) by as much as 9%, following a Prices Commission's set of rulings which is regarded as a heavy blow to the family budget. According to the Labor Party Shadow Chancellor of the Exchequor, Mr. Denis Healy, the new round of prices means that nothing is left of the last "lollipop" Budget except the stick. Since Britain's wage and prices squeeze began last winter, **6,700 grocery price increases have been approved by the Prices Commissioner** . . . Food is now 16% dearer in Britain than it was a year ago — and angry trade unionists claim that while prices have continued to rise dramatically during the supposed "freeze" wages have not taken a parallel jump . . . Critics of the Government believe that other factors, besides rising world prices, are contributing to the high cost of shopping in Britain. One factor repeatedly blamed for the rampant inflation is decimalisation. It caused confusion, destroyed traditional standards of values and still causes some shoppers almost to feel they are in a foreign country with "strange currency" . . . Also blamed is the European Economic Community — even though the Government denies that Britain's entry into the Common Market has yet affected prices.

So what can Mr. Heath do? The experts see four choices for him: He could increase agricultural supply by paying bigger subsidies to producers and reducing import controls. **He could subsidise consumption by making payments to food manufacturers in the form of cash or tax relief and ensure that these benefits were passed on to the consumer . . . "**

"STAGFLATION" — "SLUMPFLATION"

Unfortunately for Mr. Heath, he did not come up with the right answers.

After implementing the very wage and price controls he had campaigned against in the previous election, he was dismissed ignominiously from office, to be replaced by Mr. Harold Wilson — but presumably the same set of advisers who had surrounded his predecessor. All they seemed capable of was the coining of new words to describe the worsening position, prompting the following anguished letter in **The Economist:**

> "Dear Sir — First "Stagflation" and now "Slumpflation". Is the description of the economic situation really beyond the capabilities of the English language as to require such hideous inventions? Yours, etc., A. G. Burton".

Commenting on Mr. Wilson's first budget, **The Economist (March 30th, 1974).** said: "The Trade Unions asked for £500m. a year of food subsidies and that was what they got on top of the £50m. a year subsidies approved by the outgoing Heath Government . . . Mr. Healey told the Commons that the subsidies should cut any rise in food prices by 6%, which means 1½% off the retail price index . . . It is only a few weeks since Mr. Heath gave dairy farmers an extra £180m. a year, in order to hold mixed prices at their present level. Consumption of milk would fall sharply without the subsidies, as it would also fall if the dairies rationalised their distribution and cut out daily deliveries . . . "

On the other hand, what Mr. Wilson gave to consumers with one hand, he took away with the other, and the new price subsidies are to be financed out of increases in indirect taxation, particularly Sales Tax! But latest reports show a halt in the spiral of food prices in Britain, with a drop in certain quarters.

CONCLUSION

The whole question of inflation and economic stability has been given new emphasis with the results of the latest Premiers' Conference in Australia (June, 1974). The States are being forced to budget for heavy deficits in the coming financial year. One State is now considering the resumption of State Income Tax.

The Australian, June 17th, 1974, under the heading "Banana republic inflation looming", quotes Dr. D. Ironmonger, the Deputy Director of Melbourne University's Applied Economic and Social Research Institute, as saying: "We face a hyperinflation rate of more than 20% next year, with massive stagflation and large-scale unemployment . . . Dr. Ironmonger believes the Government must tackle the problem with a mixture of radical measures. He believes the Government must ease the credit squeeze now, **cut indirect taxes and also provide extra subsidies in the forthcoming budget to keep prices down".**

QUEENSLAND PREMIER'S PLAN TO BEAT INFLATION

Only one government leader has put forward similar ideas to date — the Queensland Premier, Mr. Bjelke-Petersen. He took with him to Canberra for the recent Premiers' Conference his own plan to meet inflation. Only one national paper quoted his plans. They deserve wide attention as a sane and practical alternative to the ominous collection of oppressive policies now being implemented.

The Australian (June 7th, 1974) quoted Mr. Bjelke-Petersen as follows:

"The Queensland Premier, Mr. Bjelke-Petersen, will present his own plan to beat inflation to the Premiers' Conference today if the Federal Government's proposals disappoint him. The plan — based on an expert Queensland Govts. study he commissioned for the conference — will call for a freeze on income tax and a reduction or elimination of sales tax . . . Mr. Bjelke-Petersen will also ask the Federal Government for money to be used to keep the price of basic food items down for the Consumer . . . "Our study showed that each leap-frog movement forward of prices and wages is amplified by the tax factor", Mr. Bjelke-Petersen said . . . He would tell the conference the higher inflation goes the greater income tax and sales tax make the wages-price gap. "The answer is to freeze taxation", he said. "A more forceful step must surely be to reduce or eliminate sales tax. This would do more in one stroke to put value back into the dollar than any rash of tariff cuts, restrictive credit controls and so on. Mr. Bjelke-Petersen said many items on the Consumer Price Index were subject to sales tax — "not just sales tax, but ever-increasing sales tax. As prices rise, so does sales tax . . . He would tell the conference if sales tax were eliminated the price of everything from lollies, cakes and refrigerators to cars would come down. "This would have a double-barrel effect because it would reduce Federal revenue and its spending, but at the same time give consumers television sets up to 27½% cheaper and cars more than a quarter off", Mr. Bjelke-Petersen said.

"Consumer support — which has now been called subsidies — of food would make potatoes, bread and butter, etc. cheaper. These moves would particularly help the low income earner. I don't know how the man on the basic wage can survive now".

Mr. Bjelke-Petersen's proposals are all the more courageous for the fact that the State President of his own Party, the National Party, ridiculed the idea of consumer subsidies only three years ago, in two major articles in the Queensland Country Life. No genuine argument was put forward, and the criticism was no more than a blind defence of the National Party at a time when the rural crisis was becoming politically embarrassing.

A SUMMARY

The expansion of all new credits through capital production and through wage increases merely increases costs which must be recovered through higher prices. Every time a wage increase is awarded by the Arbitration Court — generally because the value of previous awards has been eroded by price increases, industry must obtain from the banking system large sums of new credits, on loan, to finance the wages. New credit is created and reaches consumers in higher wages. But as they increase costs, and subsquently prices, their value is destroyed. It is elementary then, that there must be a Government policy which will ensure that new credits are of **permanent** value. This can be done by applying them to **reducing prices,** instead of **inflating** them. A reduced price level would mean a genuine and permanent increase in purchasing power. This policy would at one stroke completely destroy the power of subversives in the Trade Unions, to whom financial and economic dislocation are an essential ingredient of industrial friction and confrontation. Wage-earners would be receiving **real** benefits in increased purchasing power through lower prices.

Modern industry is based on series-production. The result is that if financial costs in a basic industry such as the coal or steel industry are increased, these are progressively multiplied during the series. Therefore, a comparatively small amount of new credits applied to subsidising prices in basic industries offsets the necessity for inflationary credit expansion with each step in production. This was the concept behind the subsidising during the war years of items in the C Index Series used to adjust the basic wage.

The machinery for starting on a scientific basis is being used — but in reverse, to **INCREASE PRICES.** The consumer approaches a retail counter, indicating what he requires. Immediately the true price of the article required is inflated by the sales tax. Sales tax is a direct inflationary tax. The retailer has to collect the tax — an unpaid government agent — and then send it to the Taxation Department, from which he receives a receipt.

Consider the following: All Sales Tax to be abolished. Retailers are invited to enter an agreement with the Government under which they mark down the prices on selected items (clothing and food, for example) by an agreed percentage; keep a record, send these to a Government Department, or to a Central Bank acting for the Government, and receive back the amount by which they have reduced prices. They can meet their obligations to the wholesaler, the manufacturer and producer. The consumer's purchasing power is genuinely increased. Consumer control is maintained, as it should be, in a free-enterprise system. There may be increased demand for these cheaper items, thereby stimulating production. Everyone benefits permanently.

The fundamental issue is: If new financial credit can be created to inflate prices, producing growing social unrest, **Why cannot the same credit be used to reduce prices, and remove the threat to free-enterprise and individual freedom?**

Financial and economic stability is linked not only to individual freedom and prosperity, but to the future of the Federal system and the survival of the smaller governments — State and Local Governments. Whether inflation is to be conquered depends largely on the resolution of State Governments.

It is tragic to contrast the attitude of the New South Wales and the Queensland Governments, both in the hands of the Liberal-National Party coalition. The New South Wales Government seems only too anxious to fall in with any demand placed on them by the Commonwealth. The latest weak-kneed attitude in applying a consumer tax and boosting other charges can only lead to further antipathy from electors to State Governments.

Queensland, on the other hand, is led by a man who is a genuine States Righter, and because he means what he says, he has become one of the most successful leaders in Australia. He has in consequence the regard of the majority of Queenslanders — in no wise diminished by the continual adverse publicity from the media.

If the States are to survive, a new type of leadership is required — a leadership which will not trade principles for votes Such as do so usually end up with neither.

Mr. Bjelke-Petersen's plan for beating inflation requires wide and active support. It is a beam of sanity in a darkness of confusion and compromise. Given such support, it will amaze many how other politicians climb on the bandwagon.

There is nothing accidental about inflation. It is a deliberate policy being used against the free society It has been defeated before, under circumstances more adverse than those of the present. It can be defeated again, if the means to do so is placed in enough responsible hands before the final chance has gone.

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