DEPRESSION OBSERVED
LESSONS IN A BACKWARD GLANCE

Two major depressions have punctuated the past 100 years of Australia's history. For those who believe that history repeats itself, those episodes provide food for thought.
Although the depression of the 1890s was a grim affair it did not take a world war to provide the springboard for recovery. The depression of the thirties did.

Other brokers took a shorter cut to the solution of their worldly problems.
**Charles E. Brown**, insolvent stockbroker, of Elwood, poisoned himself with prussic acid.
Lest anybody think that this is scare talk, let me make the simple observation that some countries are in a depression as great as that endured in the 1930s.

in September 1983 to reassure all that we were not in for a repeat of the twenties and thirties. The conclusions of that Reserve Bank paper began with the statement that in comparing the 1920s and 1930s with the 1970s and 1980s it is quickly evident that there are similarities and differences. Both periods saw a sharp rise in unemployment. That remains true down to today. In fact, since 1983 unemployment in Australia has remained high but it has not moved upwards significantly. While unemployment has remained static during a period of modest growth in output — growth largely confined in the last 12 months to the capital-intensive export area — it does seem that the major factor has been lower real wages.

If that is the case, and few would argue that it is probably the case, then we are in for an increase in unemployment because the recent national wage case signals the end of real wage decreases. Unemployment in 1928 was around 8 per cent — just about where it is now.

The next point of difference identified by the bank was that prices were generally falling in the 1920s and 1930s while most prices have risen — in some cases by a large amount — in the 1970s and 1980s.

It is true that we still have rising prices here — in fact, we have inflation of the order of 10 per cent. But we are out of step with a world that has moved from disinflation (falling inflation rates) to deflation (actual price falls).

Our inflation rate is a matter for concern, threatening, as it does, continuing high interest rates and low investment. Also, in the interests of historical accuracy, it should be observed that prices did not fall in Australia until 1929 with the actual onset of depression.

The next paragraph in the Reserve Bank’s conclusions reads: “World trade fell much more severely from the late 20s than seems likely in the current episode. The rise and fall in Australia’s terms of trade was much larger in the earlier episode. While Australia is still a small open economy its economic base is now much wider; also the external shock has been much smaller in the current episode.”

My response is that the decline in world trade did not take place until 1929 with the onset of depression. Figures released last week by the GATT organisation suggest that world trade is slowing almost to a standstill. The decline in Australia’s terms of trade in 1983 might compare favourably with the experience of the 1920s. That is no longer the case — falling commodity prices, depreciation of the currency and higher prices for manufactured goods provide an entirely different profile to our terms of trade than that which existed a mere two years ago.

And I would quibble with the claim that Australia now has a much wider economic base than it did in the 1920s. We remain a commodity-exporting nation. In the twenties the main exports were wheat, wool and gold. Today coal has replaced gold and while the list of exports is larger it is, if anything, more closely tied to the commodity cycle than it was in the twenties and thirties.

The next point made by the Reserve Bank was this: “Overseas borrowing in the 1920s was on a much vaster scale than in the 1970s. The debt servicing burden is consequently much smaller in the 1980s than it was in the 1930s. Also in the late 20s capital inflow dried up, forcing large adjustments to eliminate current account deficit, whereas in recent times capital inflow has tended to exceed the large current account deficit.”

According to the Reserve Bank’s figures the interest in Australia’s overseas debt as a proportion of export receipts peaked at 29.4 per cent in 1930-31.

In 1985, when our net foreign debt was $52 billion, interest as a percentage of exports was 11 per cent. Currently our net foreign debt stands at $80 billion. No official figures are available on interest as a proportion of exports but if we reckon interest at 10 per cent — which would be a conservative estimate of the hedged interest cost — then interest as a proportion of exports is more than 20 per cent.

Now while that is better than 29 per cent, two points should be made. The figure has doubled in a mere 18 months. Second, most of our 1920s debt was long-term. Most of our present debt is short-term and amortisation plus interest produces a much higher result than was the case in the thirties.

Dominguez Barry Samuel Montagu recently did a back-of-the-envelope exercise on our debt servicing costs and came up with a figure of 68 per cent of exports — a figure it conceded was probably nonsense but a figure which would put us firmly in the Latin-American class.

The other point to remember is that in 1930-31 the Australian balance of payments had moved into surplus on current account. We are now running a current account deficit that is above 5 per cent of GDP — and this is a country which exports a little over 15 per cent of GDP. To balance our current account and merely hold our debt at its present high level would require an increase in exports of more than 30 per cent.

Now we can achieve the same result by other means — by reducing internal demand, for example. That brings up the subject of fiscal policy and the nasty world of politics. I have probably depressed you sufficiently without going down that track.

With a combination of political courage at home and abroad, a lot of luck and a return to prudent behaviour in world financial markets, we can avoid a recession. Such a quadrella is possible — but I agree with Henry Kaufman that the odds are long.

My advice is to get out there and make your first million quickly. Time is running out.

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