

ECONOMICS

Discuss the effects of microeconomic reform on product and factor markets in the Australian economy.

Microeconomic reform within the Australian government seeks to reduce inflationary pressures and promote long term sustainable growth through a consistent positive shift in aggregate supply in the circular flow. This shift is achieved through encouraging structural change to improve the efficiency, flexibility and productivity of the production process of goods and services, as well as labour, otherwise product and factor markets.

The Australian government is largely responsible for microeconomic reform, and has implemented an extensive program of deregulatory policies over recent decades to combat inefficiency. Within the financial sector, measures such as the floating of the AUD (despite its macroeconomic impacts) and the removal of banking competition barriers have forced the industry to become more technically efficient, reducing product prices. The reallocation of capital resources has enabled huge increases in investment, fundamental in propelling capital accumulation and deepening, contributing to greater economic growth. However the onset of the global financial crisis in 2008 brought to light the necessity of financial regulation in maintaining economic sustainability. Thus, regulation within the finance sector has remained steady in recent years, compromising decreased prices and production costs. Similarly, the agriculture industry has undergone deregulation through demonopolisation in domestic wool, wheat and dairy industries, forcing the price of products to more greatly reflect market forces. Consequently, a shift has occurred towards farms of greater production efficiency. Farm production has increased significantly over the past 15 years, with production value increasing by 26%, with the number of farms decreasing by 16%. This has also increased Australia's international competitiveness within export markets, most crucial in the last decade due to the highly protected nature of the international agriculture industry.

Australia's transition towards a free market has required a significant decrease in protection levels since the 1960s. Through this process of trade liberalisation, Australia has achieved an average tariff level of 1.9%, increasing structural change towards greater productivity. Whilst the structural change has had an immediate negative impact on the derived demand for factor markets in the short term, long term change has reflected a shift to industries where Australia has a comparative advantage. This is evident in the deterioration of Australia export portfolio, with manufacturing decreasing from 13% in 1990 to 10% in 2010, and agriculture decreasing from 23% to 10% of total composition. Conversely, Australia's mineral resources exports have increased from 33% to 53%, marking the shift towards industries which can achieve greater economies of scale and comparative advantage. Global trade integration policies in trade agreements have made way for a sustained high demand for Australia's mineral resources in key Asian markets.

In order to reduce the inefficiency of key government assets, Australia's Public Trading Enterprises have undergone degrees of corporatisation and privatisation. Corporatised enterprises such as Australia Post and EnergyAustralia are run independently with a profit motive, with EnergyAustralia run in direct competition with other private institutions. Similarly, the Australian government has privatised businesses such as QANTAS, Telstra and the Commonwealth Bank to improve technical efficiency through increased competition. This has helped significantly decrease the costs of products in these industries, extending demand and simultaneously forcing a higher output of its factors of production, often increasing employment in line with industry expansion. The recent National Broadband Network programme is planned to follow this pattern of privatisation; the government has sought to build the infrastructure under its own regulation, before selling off the asset.

Crucial to microeconomic reform is labour market policy in achieving a balance between a high level of productivity and workplace equity. Thus, Australia has experienced a vast change in labour market towards policy dependent on federal and state politics. The Workchoices Act of 2005 sought

to override the inefficient overlap of state and federal industrial awards, as to increase national productivity. This was replaced by the Fair Work Australia Act 2007 to replace 4300 state and federal awards to just 122 modern awards. This simplification has enabled the promotion of productivity without compromising wage equity. Despite this, a number of safety nets remain in the award system, such as the National Employment Standards, under the understanding that consistent standards of employment are necessary to avoid hysteresis and ensure the long term sustainability of the work force. Collective enterprise agreements cover a large proportion of Australia's workforce, defined by their flexibility to bargain away standards such as leave and working hours, whilst passing an employee 'Better Off Overall Test'. This policy has also helped increase human capital through a rise in the participation rate as those who had previously been unable to work under the award system are accommodated for. This increase in supply has simultaneously decreased pressures on labour costs, enabling lower costs to consumers, thus decreasing inflationary pressures in the long term. Since the 1990s, the Howard Australian government deemed the centralised wage system as no longer appropriate for the Australian economy, and has thus increased wage decentralisation to increase the efficiency of the allocation of resources. The following Rudd and Gillard administrations however have slowed this process down, but nevertheless shifting towards decentralisation. Furthermore, along with decreased inflationary pressures, the decentralised wage system increases workforce flexibility, reducing the non-inflationary rate of unemployment and helping maintain unemployment at a sustainably low level. Conversely, a centralised system may lead to wage-push inflation due to an imbalance in bargaining power, potentially leading to a wage inflationary spiral. However, the government maintains the power to prevent this from occurring through rigorous regulation of enterprise agreements. Most recently, the Gillard Government's main reform has come through an increase in education and training programmes. This has been met with greater subsidisation at universities and increasing training places for students pursuing a trade. In 2009 Job Services Australia was established to increase the organisation of private employment services. These services are paid on the basis of placing the unemployed in jobs, thus increasing the motive to place positions. Job Services Australia, as well as Skills Australia also seek to reduce Australia's large skill shortage (estimated 240 000 by 2016). By increasing the employment and training opportunities for Australia's working age population, the government seeks to increase participation rates and decrease unemployment, contributing to lower inflation and higher standards of living nationally.

Australia's National Competition Policy seeks to promote competition by reducing the influence of monopolies and removing provisions at advantage particular enterprises. The establishment of the Australian Competition and Consumer Commission remains chiefly responsible for this policy, working effectively to promote the impacts of structural change while maintain a high degree of workable competition. Amongst the practices that the ACCC does not condone include price fixing, price discrimination and monopolisation as to prevent high industry barriers or decrease competition. Such contestable competition forces businesses to operate efficiently, decreasing prices within product markets nationwide. The National Competition Policy also regulates the level and cost of access to crucial infrastructure otherwise privately owned, additionally enhancing competition. The introduction of the policy in 1995 has helped the significant decrease in the CPI. Where it averaged 7.2% in the 1980s, the National Competition Policy in combination with other crucial microeconomic reform policies has assisted the decrease to an average of 2.7% in the 2000s. In line with the Policy, the Council of Australian Governments was formed in 2007 with a reform agenda aimed at creating greater cohesion on microeconomic reform at a national level. The Productivity Commission estimates that by 2032, health and education reforms could potentially increase GDP by 6% due to higher workforce participation, whilst also promoting a sustainable level of inflation.

Most recent industry innovation policies have sought to increase the proportion of business innovation by 25%, encouraging the development of more efficient ways to raise productivity as to become more competitive. Such measures are highlighted by the 45% Research and Development Tax Credit encouraging such expenditure by private institutions. However, the overall impact of innovation policies on product and factor markets is skewed by the time lag on their implementation. The Australian government has heavily promoted the adoption of technology in industry, attempting

to increase the level of technology within current students with the iPad Student Discount Programme. The government intends that this increased use of technology will follow into the workforce.

Taxation reform seeks to distort or change the allocation of resources in the interests of the nation. However, distortion through the implementation of industry taxes can inhibit productivity and consequently the product prices as is the case with the recent Mineral Resources Rent Tax. Conversely, tax reform through the removal of tax exemptions and concessions can take away the productive advantage of particular industries, forcing structural change towards more efficient practices. Much alike labour market policies, tax reform may not always reflect a shift towards higher productivity, but rather what is deemed to maintain a sustainable allocation of resources that will most greatly add to national income and standards of living without significantly increasing inflationary pressures.

Due to significant structural change during the 1980s and 1990s as a result of microeconomic reform, the creation of new reform has slowed due to the decreased necessity for structural change. This is most evident in Australia's productivity; falling from 2.1% throughout the 1990s, to 1.2% in the 2000s. Nevertheless, product and factor markets remain influenced by the level of government intervention in seeking to balance the promotion of competition, productivity and long term sustainability of Australia's product and factor markets.

Plan:

Deregulation

Protection

PTE reform

Labour (wage determination, decentralisation, education programmes)

Nat Com Pol

Innovation

Tax reform

Terms: Increase in AS, technical, allocative and dynamic efficiency, Nairu, cost push Inflation, 7.2CPI 1980s 2.7CPI current

Effects on markets; increased wages, increased productivity, increased human capital, increased competition, decreased prices and costs, innovation, structural change and structural unemployment.