

## Small Government Feeds Entitlement

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Joe Hockey's speech was more than a simplistic assault on social security payments - it exposed deep contradictions in the Libs' economic policy. NM economist Ian McAuley explains

Joe Hockey's speech to the UK Institute of Economic Affairs — "The end of the age of entitlement" — has provoked swift and well justified responses from informed commentators such as Peter Whiteford and New Matilda's Ben Eltham and Sarah Lumley who point out that, in comparison with similar countries, Australia has a small and carefully targeted social security system. In fact, some of our programs such as Newstart are best described as parsimonious.

His speech is more than a straightforward assault on social security payments. Hockey has revealed the currents of economic thinking that are influencing the ideas of the Liberal Party and what may be more generally called the "right" of politics, here and abroad. In doing so, as explained by Annabel Crabb, he exposes basic policy conflicts which are likely to emerge more prominently as the Coalition is forced to reveal its policies.

His speech aligns with the mainstream political "right" (rather than the fringe in the Tea Party and in European anti-immigration movements) and in doing so it reveals a confused and simplistic notion of government, a misunderstanding of the origins of the redistributive "entitlement" system, and a fundamental difference between his way of thinking and that of Tony Abbott — a way of thinking rooted in traditions far removed from general "right" or Liberal Party thinking.

To take these three issues in turn.

First, Hockey is a champion of "small government", a notion which is sacred to many on the Right but which is devoid of meaning. The notion is that government is an unproductive burden on the productive private sector. Therefore, if the size of government can be contained or shrunk, there will be economic growth and prosperity. Hockey specifically mentions high-growth Asian countries as cases to support his point.

It is easy to find examples of governments which have, indeed, followed the path Hockey describes in his speech. In the Mediterranean countries governments have spent much more than they have raised in taxes and much of that spending has been on welfare "entitlements" to use his term.

But he conveniently ignores other European examples, particularly the successful Nordic countries and Germany, where public spending is in the order of 40 to 50 per cent of GDP. He ignores countries in South America and Africa which have small governments and dimly poor growth. And in citing successful Asian examples he ignores two important characteristics of those countries — a young age structure which eases demand for social security and health payments and their strong public spending on education and infrastructure. Hockey, in his speech, actually lumps education in with other "entitlement" programs, rather than as an investment in human capital.

What counts for economic success is not some simplistic measure of "size" but rather the quality of government. Failure to provide essential public services such as health care and education can be major impediments to economic growth, as can misdirected or poorly administered government expenditure. Also, measures of "size" fail to capture the regulatory scope of government. Regulation can enhance economic performance or impede it, depending on its nature. Conservatives often treat all regulation as "bad", overlooking the essential role of regulation in setting the road rules for a market economy.

Any discussion of the "size" of government should start with a clear distinction between what economists refer to as government "own purpose expenditure" and "personal transfers". The former includes a range of public services — defence, education, health care, environmental protection, infrastructure and so on, collectively known as "public goods", which generally provide economic benefits in their own right. The latter consists of pensions, family allowance payments and so on. What characterises personal transfers is that the individual receiving such payments is generally free to spend them as he or she wishes; they may be spent on food and shelter or on poker machines and liquor.

Hockey hints at this distinction, but he does not make it clearly. That's unfortunate, for he fails to see how the neoliberal policies of the political "right" themselves have contributed to the dependence on social security transfers and to the culture of "entitlement".

That leads to the second issue — the origins of the "entitlement" culture.

It's an easy assumption that governments on the "right", committed to the free reign of markets, are mean on social security payments.

In fact, that is not the case, and the counterintuitive explanation is simple. In a seminal 1994 paper "Distributive Politics and Economic Growth", Dani Rodrik and Alberto Alesina, both of Harvard University, point out that neoliberal policies result in widening distributions of income and that in order to sustain political legitimacy such governments have to spend heavily on social security transfers.

Wide income disparities are seen as a minor collateral cost of the economic progress which neoliberal politicians believe result from market liberalisation and these disparities can be rectified, in part, with social security transfers. In fact, it has been common practice for such governments to fund expenditure by diverting expenditure away from public goods, and that was certainly the policy of the Howard-Costello Government.

The preference for cash transfers over public services aligns with the neoliberal idea of "individual choice": according to neoliberal philosophy individuals can make better allocative decisions than public servants. That philosophy is easy to embrace if one ignores the well-established economics of market failure which set a clear division between what governments do best and what markets do best — in other words the accumulated wisdom which lays the foundation for successful "mixed economies" providing a mixture of public and private goods.

It's always easier to rely on simple slogans such as "small government" rather than to understand the complexities of economics, particularly when those slogans serve so many vested interests.

The other way in which neoliberalism has contributed to the culture of "entitlement" is in its devaluation of government. Ronald Reagan set the mood when he said "Government is like a baby. An alimentary canal with a big appetite at one end and no sense of responsibility at the other."

Just earlier this month the Centre for Independent Studies celebrated "Tax Freedom Day", referring to April 5 as the day when the average Australian has paid off his taxes and can start creating wealth through real economic activity for the rest of the year, because up to that point his income has gone to the black hole of the taxation authorities.

If one believes that government is intrinsically unproductive, and that taxes "confiscate" one's income (to use the word of the CIS), then of course one is entitled to try to get some of it back — as an industry subsidy, as middle class welfare, or as an undeserved pension payment. That's a long way from what should be thought of as taking money away from economically useful activities such as education, infrastructure and environmental protection.

Hockey is right to draw attention to the growth of welfare transfers as a burden on public revenue. He neglects to show how neoliberalism itself has contributed to the problem, and he neglects to show how, under neoliberal governments, these payments have come at the expense of economically productive services.

And he conveniently ignores the traditional philosophy of Labor and Social Democratic parties, which have preferred to see people in well paying employment, rather than being dependent on welfare transfers, and have supported those public investments which contribute to an economy which has less need for welfare transfers.

This moves into the third issue, the differences between Hockey and Abbott.

Abbott has made no secret of his attachment to welfare, particularly middle-class welfare. His proposals on maternity allowances, "nannies" and restoring subsidies for those holding private health insurance are strong examples.

He promises to increase welfare largesse while cutting taxes and government expenditure. He could do this only by cutting expenditure on government "own purpose" programs.

At first sight this may appear to be pure opportunism — a belief that his promises can avoid fiscal scrutiny (as they did in the 2010 election). But they could be a manifestation of a deeper philosophy, with roots in his own ethnic religious background.

It is not enough to put Abbott's philosophy down to his Catholic religion, because Catholicism has many different economic and social strands, ranging from the Marxist "liberation theology" movement through to

the far right Opus Dei movement. Hockey, Turnbull and Abbott are all Catholics, as is Keating, but they all have very different economic philosophies.

In the early 20th century there arose among a group of English Catholics, including GK Chesterton and Hilare Belloc, a movement known as "distributism", based on the teachings of Pope Leo XIII in his 1891 Encyclical *Rerum Novarum* on the "Rights and Duties of Capital and Labor". That encyclical, a reaction to the secular forces of capitalism and communism, was a belated response to the industrial revolution.

The distributism movement romanticised an earlier pre-industrial order. It was opposed to big business and to big government and was even opposed to technological progress, because the technologies of the industrial revolution had upset earlier social orders. It envisaged a return to a romanticised feudal order, glossing over the horrible realities of historical feudalism, in a naive belief that a modern version of feudalism could be governed by Christian morality and by a sense of noblesse oblige. It is best described by the oxymoron "feudal socialism".

An earlier champion of distributism in Australia was BA Santamaria, who exercised his influence through the trade union movement. Echoes of his philosophy can still be found in some of the more conservative unions and Abbott seems to have taken up where Santamaria left off. His opposition to the NBN, to carbon pricing, and even to electronic health records, can all be seen in the light of not only a mistrust of government but also a fear of "disruptive technologies" — the very developments which give capitalism its energy. His opposition to market-based solutions to climate change is consistent with a fear of the power of secular forces, particularly ones that operate through the amoral mechanism of the "invisible hand".

These aspects of Abbott's conservatism do not sit easily with the traditions of the Liberal Party (or, indeed, with the majority of Catholic politicians). As the Party's policies become subject to more scrutiny, we can expect to see more of these ideological tensions emerge. Hockey has raised policy questions which are much more relevant to our future than political trivia such as Julia Gillard's wardrobe and politicians' private peccadillos.