

# Craig Emerson, MP

Minister for Small Business, Independent Contractors and the  
Service Economy  
Minister Assisting on Deregulation

## Address to the Sydney Institute

12 June 2008

### ‘Prosperity and fairness in a market democracy’

“*Market democrats* support opportunity for all in a market economy. They see the role of government not in fettering the market but in harnessing the power of the market for the public good. *Market democrats* believe in expanding opportunity, not the welfare state, by providing an excellent education to all children. *Market democrats* are the champions of competition and compassion”.

### Towards a unifying political philosophy

Tonight I want to propose a unifying political philosophy that embraces the universal values reaffirmed in the Millennium Declaration and applies them to public policy making. Embedding these values of freedom, equality, solidarity, tolerance, respect for nature and shared responsibility in a political philosophy offers the prospect of creating a new political consensus on a future direction for Australia.

That political philosophy – prosperity and fairness through opportunity for all in a market democracy – finds a comfortable home in the Australian Labor Party.

When last in government, Labor made itself the party of competition and compassion, a tradition that is being carried on by the Rudd government. But in the application of this philosophy, the Rudd government acknowledges that the policy approaches of the 1980s and early 1990s need both renovation and innovation as we develop modern responses to the new challenges of the 21<sup>st</sup> century.

In this political philosophy the role of policy makers is to allow the market to create prosperity and out of that prosperity to expand opportunity, not the welfare state. In the market democracy so fashioned, citizens enjoy freedom, self-fulfilment and sovereignty over the state, not subjugation to the state through financial and regulatory welfare.

This is the philosophy of like-minded people whom I call *market democrats* – the modern Labor champions of the traditional Labor values of prosperity, fairness and compassion. *Market democrats* harness the power of the market for the public good. They dedicate themselves to remedying social disadvantage out of prosperity by

giving every child the opportunity of a quality education through excellence in teaching and high-quality school facilities. *Market democrats* understand that simply providing opportunity to the underprivileged does not guarantee it will be taken up. That's why *market democrats* support underprivileged children and their families through early childhood development and early intervention programs.

In my remaining time tonight I will take you through my thinking and condense it into ten beliefs of *market democrats* as a guide to public policy making in the 21<sup>st</sup> century. Then I will happily invite questions and comments from you, the audience, in the hope of a robust, rewarding exchange of views.

## **The morality of self-interest**

Are markets immoral, impersonal devices that sap citizens of their decency and humanity, or are they a vehicle for achieving a prosperous and fair society? To answer this, we need to determine whether the driving force behind markets – self-interest – is moral or immoral.

As an 18-year-old Catholic churchgoer who had just cast my maiden vote for the formation of the first federal Labor government in 23 years, I began to question the morality of self-interest. Could self-interest be reconciled with a social conscience?

Bombarded by the strong convictions of Sydney University's left-wing political economy lecturers Ted Wheelwright and Frank Stillwell and the equally strong convictions of right-wing orthodox economics professors Warren Hogan and Colin Simkin, I struggled with the motivation behind giving money to the church coffers during Mass.

Wasn't this really an act of selfishness, driven by a desire to feel better about myself? How was this any different to tax avoidance by the rich, itself an act of selfishness by people who gladly accepted the benefits of shady green parks, law and order and the defence of the country without contributing to their cost?

Obviously these are the debates of the great philosophers. But they go to the heart of value judgements about the morality of a market economy – or as it was then known, capitalism.

Three years later my churchgoing had become more sporadic. As an honours student in economics I ploughed through the writings of Adam Smith, David Ricardo and Karl Marx. Both Ricardo and Marx drew inspiration from Smith. Marx married Smith's labour theory of value with his own values in intellectualising a moral superiority of workers over capitalists and the collective over the individual – a marriage whose offspring were socialism and communism.

Marx is correctly identified as the father of socialism, but how ironic it is that Smith's supporters and critics regard him as the father of laissez-faire capitalism, when he was, in truth, a staunch critic of powerful business interests and a champion of public education for the children of the poor. As Dr Carmen Lawrence observed in her valedictory speech in the federal parliament in September 2007, 'Adam Smith was a very strong proponent of the need for institutional controls and the insertion of

humane values into the operation of the economy, because he recognised the limitations of market forces'.

Smith, the professed father of capitalism, warned that admiration for the rich and powerful was 'the great and most universal cause of the corruption of our moral sentiments' (Theory of Moral Sentiments, p. 61). And he fingered contemporary government as a conspirator with the wealthy against the poor:

*'Civil government, so far as it is instituted for the security of property, is in reality instituted for the defence of the rich against the poor, or of those who have some property against those who have none at all' (Wealth of Nations, p. 715).*

Smith accused businesspeople – merchants – of constantly conspiring against consumers:

*'People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the publick, or in some contrivance to raise prices' (Wealth of Nations, p. 145).*

In their conspiracies, merchants enlisted the support of governments to protect them from competition at the expense of consumers, causing Smith to warn that 'the proposal of any new law or regulation of commerce' that arises from the merchant class 'ought always to be listened to with great precaution' (Wealth of Nations, p. 267).

But if these systems of preferment were removed, Smith saw virtue in the freedoms so created:

*'...the obvious and simple system of natural liberty establishes itself of its own accord. Every man, as long as he does not violate the laws of justice, is left perfectly free to pursue his own interest his own way, and to bring forth his industry and capital into competition with those of any other man, or order of men' (Wealth of Nations, p. 687).*

Smith considered openness and freedom would yield social good through the power of self-interest:

*'It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest' (Wealth of Nations, pp. 26-27).*

Prosperity is gained through this 'invisible hand' (Wealth of Nations, p. 456) of buyers and sellers pursuing their self-interest in an open, competitive economy.

Yet Smith did not see this as utopia. He foresaw the debilitating effects of the division of labour in an industrial revolution that had not yet begun, predicting that menial, repetitive behaviour would create men 'mutilated and deformed' (Wealth of Nations, p. 788).

As a 21-year-old, I began to see the world as Smith had: that the most prosperous nations were those with open, competitive economies, whose individuals are motivated by self-interest – but that these societies were by no means free of injustice and disadvantage or moral corruption.

Though Smith, a true humanitarian, believed that all children were born with equal talents, I worried that low self-esteem of the socially excluded was perpetuating disadvantage. The political right had a different view; that those who failed to break out of the welfare dependency into which they were born were lazy and indolent, deserving of no sympathy or support from the state. Conservative politicians of the 1970s used the term 'dole bludgers' to absolve them of any responsibility to look behind the receipt of welfare payments to the underlying causes of dependency.

It was not until I reached the age of 29 that I joined the Australian Labor Party, as a recently-appointed economic adviser to Senator Peter Walsh in the new Hawke government. Peter did not insist on Party membership but on rigour in defence of a strong economy and the truly disadvantaged (as opposed to 'rent-seeking spivs', 'hairy-legged Stalinists' and anyone guilty of 'economic treachery').

An even younger Stephen Conroy, electorate secretary to Canberra MP Ros Kelly, convinced me to join the Party. As a new recruit to the Mt Ainslie Branch, I almost lasted just one meeting where the main topics of discussion were the composition of the disputes committee and fundraising. When I naively suggested that any funds raised should go to St Vincent de Paul, I was howled down by seasoned aspirants for election to the ACT Assembly.

But as a new recruit to the ALP I again began to ask: is there truly a conflict between self-interest and moral behaviour and is there a conflict between morality and markets?

Some say competitive markets bring out the worst in us – greed and avarice. Oddly they don't say the same about the Olympic Games, football or cricket, netball, music and dance competitions, all based on our most competitive instincts.

As Bob Hawke used to advise me as a fresh recruit to his staff in 1986 when teaching me the intricacies of betting on horse racing: 'Son, in any race, back the horse called Self Interest, because you know it will be trying'.

But self-interest is not synonymous with selfishness. An athlete is not selfish for wanting to win a tournament, but is self-interested. A singer is not selfish for wanting to win Australian Idol. An artist is not selfish for wanting to win the Archibald Prize, nor is an author for wanting to win the Booker Prize. A scientist is not selfish for wanting to achieve a breakthrough ahead of other scientists.

Athletes, singers, artists, dancers, authors and scientists are self-interested but this does not make them selfish. Some may be arrogant and rude, some selfish, others humble and altruistic, but all are self-interested. Without self-interest, economic and social progress is impossible.

The Hawke government began opening up the economy, dismantling the regulatory shackles that had been progressively applied over decades of mainly conservative governments. I came to understand that those Liberal-National Party governments were not champions of *free* enterprise but of *private* enterprise (although they quite liked the ideas of socialising private losses by bailing out insolvent businesses). The conservatives were keen regulators, protecting their private business supporters from competition at home and from abroad.

Labor was making itself the party of competition and compassion. Out of the proceeds of growth, the Hawke government was lifting school completion rates, supporting the parents of poor children to keep them at school. My moral questions were being answered through the competitive yet compassionate philosophy of the Hawke and Keating Labor governments – a philosophy that sat easily with Adam Smith's Theory of Moral Sentiments and the Wealth of Nations. There was, I concluded, no inherent conflict between markets and morality.

Competitive markets rely on self-interest, not on selfishness. Competitive markets don't penalise altruism. Successful businesspeople can and often do display great altruism. Bill Gates is one of the world's great philanthropists, while the entire world has benefited in one way or another from the revolution in information technology at Microsoft that made him rich. John Singleton quietly contributes millions of dollars a year to Australian charities out of the success he has enjoyed in the fiercely-competitive advertising and radio industries. Some other successful businesspeople are greedy bastards who get ahead by refusing to pay their suppliers and sub-contractors money that it owed to them. Such selfishness is immoral but self-interest is not.

So what does this mean for us, today, at the start of the 21st century with a new Rudd Labor government in Canberra?

Traditional Labor values of prosperity, fairness and compassion fit well with supporting an open, competitive economy that rewards effort, risk-taking and entrepreneurship and where opportunity, not welfare, is available to all.

## **Competition works**

Competitive markets reward effort, risk-taking and entrepreneurship and they encourage innovation essential to the growth of a market economy.

The forces of competition create pressure on businesses to be efficient and to come up with and apply new ideas for application in producing goods and services valued by consumers.

Yet markets are chaotic and wasteful. Predicting the prices produced by markets is always hazardous. Markets force businesses to close, wasting the building renovations and obliging employees to seek work elsewhere.

But far more wasteful and chaotic are central planning and governments pretending to be good at running businesses in so-called mixed economies.

One of the most valuable ideas put forward at the 2020 Summit was from Jane Bennett, a Tasmanian cheese-maker. Ms Bennett observed that 'one of the things that Australians are not good at is permitting failure and recognising that it is a component of innovation'.

In this cheese-maker's experience, failure was the mother of success. It is only through trying and failing that risk-takers end up succeeding. Such is the power of competition.

But markets cannot provide the solutions to all human needs. In social groupings, self-esteem derives from how we believe our peers see us. When we offer ourselves for work and the offer is accepted, we are being told that what we have to offer – our skill, our talent, our commitment – is valuable. That's why so much of our self-esteem is bound up in our work. A well-paid job is an indication that others value our work and are willing to give up something of value for it. Yet there is also great value in unpaid work, whether it is parenting, care-giving or volunteering, since it is on the basis of these rewards that strong communities are built.

## **Fairness in a market economy**

Fair societies can flourish in open, competitive economies. By allowing self-interested behaviour in competitive markets to create prosperity and using some of the proceeds to extend opportunity to all, a transition from self-interest to the public interest is attained. The challenge of government is not to fetter the market to achieve fairness but to harness the power of the market for the public good.

This is the philosophy of a *market democrat*, a modern incarnation of the traditions of the Hawke and Keating governments, later imported by Tony Blair, re-badged and refined as the Third Way.

Hawke and Keating Labor responded in the 20<sup>th</sup> century with creative solutions for the times. Rudd Labor is developing modern responses in meeting the new challenges of the 21<sup>st</sup> century.

## **What is fairness?**

Fairness has traditionally been assessed on the basis of how equally or unequally incomes are distributed. The social goal of greater equality of incomes was formulated during times of material deprivation. Yet poverty in the 21<sup>st</sup> century in affluent countries like Australia is not primarily caused by inadequate incomes, but by the interrelated influences of poor education, poor health, breakdown in social relationships, gambling and substance abuse. Few mentally-healthy, well-educated people live in poverty.

If poverty in Australia is no longer primarily a poverty of incomes but a poverty of opportunity, the goal of a fairer society is best pursued through a more equal distribution of opportunity than through a more equal distribution of income.

A nation's people are not better off if all live on equally low incomes. Of course it is unfair if the rich get richer while the poor get poorer. But why should governments

seek to prevent the rich from getting richer if the poor also get richer as a consequence of the wealth creation process?

Imagine two societies. In one society the poorest ten per cent of citizens each have an annual income of \$30,000 and the wealthiest ten per cent have average incomes of \$3 million per annum. In the second society the poorest ten per cent have average incomes of \$10,000 per annum while the wealthiest have average annual incomes of \$100,000. The second society has a more equal distribution of income than the first, but its poorest people are three times poorer than those of the first society. Is this more equal society a fairer society than the more prosperous society?

Albania, Bangladesh and Ethiopia have more equal income distributions than Australia, but most would agree that Australia's society is fairer. Many Australians earning below-average incomes choose to forego higher pay in favour of spending more time with their families and friends or just relaxing or playing sport. By doing so they are making measured income inequality worse but, through free choice, they are making their own lives better.

### **Must fairness clash with prosperity?**

Can a society have more fairness only at the expense of prosperity? Critics of markets argue that they are inherently unfair; that they need to be regulated in the name of fairness. It was less than three decades ago when the Australian government imposed a ceiling on home mortgage interest rates, said to be aimed at preventing low-income earners from being priced out of home ownership. Banks gave loans to better-off couples with long savings histories. The poor missed out. Rent control works the same way: the better-off are offered the rental accommodation and the poor miss out as the total supply of premises for rent is restricted by the ceiling on rents.

The goal of *market democrats* is prosperity and fairness through opportunity for all in a market economy. *Market democrats* strive for a more equal distribution of opportunity. If opportunity is equally distributed, incomes in the future will be distributed more equally. Prosperity and fairness become partners not rivals.

Yet *market democrats* recognise that past injustices leading to an unequal distribution of opportunity leave a legacy of poor earning capacity. The low-skilled might be in work, but their incomes may be so low as to deny them the ability to provide genuine opportunity for their children through a quality education. In these circumstances low income causes low opportunity.

The vulnerable will fall on hard times through their lifetimes. They might lose their jobs in an economic downturn. Housing rents might soar during housing shortages, as they have done in recent times, making life especially harsh for renting age pensioners. Emotional trauma might take the vulnerable out of the workforce. Young single mothers whose children need their care and attention will suffer financial hardship without income support.

A fair society should support the weak and the vulnerable who have low or no income-earning capacity, such as the working poor, the aged poor, the mentally ill and those so physically impaired that they simply cannot work.

But for those out of the workforce who have income-earning prospects, perpetual income support payments without any effort to remedy the causes of disadvantage are not the pathway to a prosperous, fair society; they are a perilous road to welfare dependency, low self-esteem and servitude to the state. 'Sit-down money', as Noel Pearson describes this welfarism for Aboriginal communities, has the same psychological impact in non-indigenous communities.

## **Collectivism in a market democracy**

In a market democracy there is a role for collectivism. Humans are social beings; through most of our lifetimes we behave collectively. We don't accept that someone who has failed to take out private health insurance should be left to die in the street. We gather together for sport and are happy that governments subsidise the cost of the playing fields. We enjoy a family barbecue in the park just that little bit more when we see other families enjoying themselves. We warmly embrace a sense of community.

The Australian trade union movement remains a large, community-based organisation. Through its support for the weak and the vulnerable, for its pursuit of decent treatment in workplaces, the union movement is a force for fairness in a market democracy. But as Labor is doing, the trade union movement must continue to modernise if it is to survive and prosper in Australia's open, competitive economy.

Seeking to use industrial muscle to gain pay rises in excess of productivity growth is inflationary and ultimately self-defeating. Modern unionism can involve offering a bundle of services that are attractive to members. These services can extend beyond representation in workplace bargaining to support for lifelong learning, financial, tax and legal advice and advice on superannuation, private health insurance and even personal counselling services. These modern unions would be available to represent members not only in collective enterprise bargaining but in providing advice on individual bargaining.

Membership of unions need not be limited to employees; independent contractors could be members (some already are) or they could subscribe to a bundle of services through payment of an annual fee or a one-off fee for a smaller bundle of services appropriate to the particular needs of the contractor.

Unions offering such services to independent contractors would be doing so under commercial law in competition with employer organisations, law firms and anyone else who wanted to compete in the open market. This is a modern expression of freedom of association in an open, competitive economy.

## **The role of government in a market democracy**

In a flourishing democracy government serves the people. Yet at every twist and turn, governments come up with new taxes and new regulations that subjugate the people to the state. By intervening, taxing heavily and regulating, governments have sought to restrict individual freedoms, stifle initiative and inhibit self-reliance.

In a market democracy governments should serve the people instead of seeking to subjugate the people to the will of government through high taxes and heavy regulation. By allowing markets to reward hard work, risk-taking and entrepreneurship without unnecessary interference, *market democrats* advance freedom and self-fulfilment.

If governments are to bring out the best in people they should not erect disincentives to creating prosperity and good social behaviour such as honesty, initiative and creativity. Governments must not imprison the disadvantaged by subjugating them to the state, robbing them of self-esteem and condemning them to a life of dependency; governments must liberate them by providing opportunity for all in a truly fair society.

Let us not make the disadvantaged the experiments of social engineers yearning for a different social order but lacking the stomach to practice it in their own lives. It is this social experimentation of romanticising traditional life in the harsh outback that has caused Australia's most vulnerable – indigenous people – to be trapped in misery. Good on Warren Mundine and Noel Pearson for exposing the immorality of those asserting moral superiority but whose pomposity perpetuates the disadvantage of our indigenous brother and sisters. And good on indigenous affairs minister Jenny Macklin for having the courage to set her own course.

*Market democrats* oppose the relentless expansion of the welfare state, where higher taxes are used to obtain revenue for recycling – often to the same people – in return for political support. This was the hallmark of the previous Liberal-National Party government and, judging by the objections of the Opposition Leader, the Shadow Treasurer and the Shadow Minister for Families to means-testing the baby bonus and family payments for stay-at-home mothers, remains a defining feature of the Coalition.

The modern welfare state extends beyond recycling tax revenue; it is a state of ever-expanding government regulation. This *regulatory welfare* reinforces the culture of dependency, by discouraging people from taking responsibility for their own actions and their own lives. Regulatory welfare is inimical to a market democracy, since it discourages individual initiative and business risk taking.

*Market democrats* think of markets first and, only where necessary, strengthen or complement markets with efficient regulation. In a market democracy, regulation is justifiable in strengthening markets and remedying market failure. But the previous conservative government thought of regulation first, presiding over what the Business Council of Australia describes as the creeping re-regulation of business. This is why, in a process initiated by Kevin Rudd, Lindsay Tanner and I are so vigorously working with the States and Territories in cutting back overbearing, inconsistent and overlapping Commonwealth and State business regulation.

## **Establishing property rights**

Regulation to establish and enforce property rights is necessary for the proper functioning of a competitive economy. Why buy fruit from a greengrocer when you

can steal it? Why pay people to work when you can obtain their labour through violence, coercion or slavery? Why save money when anyone can take it from your bank account? And why invent something that anyone can copy from the first day of invention?

But poorly-defined property rights can lead to extremely wasteful activity. If laws relating to property rights are vague or poorly written, enormous energy and resources can be devoted to litigation to establish property rights through the courts. It took Australia and East Timor several years to reach agreement on the ownership of oil in the Timor Sea between the two countries. In the absence of any agreement, exploration would not have occurred, to the detriment of both countries.

As society progresses and new scientific or technological breakthroughs are achieved, new laws need to be written to establish property rights over new goods and services. For example, genetic engineering has necessitated a new set of laws to establish property rights over genetic material.

Only where property rights are clearly-defined, well-established and enforceable can goods, services and other property be bought and sold and wasteful disputes kept to a minimum.

## **When markets fail**

Nobody seriously claims that all markets are perfect. Departures from the competitive model are called market failure. Where market failure occurs, a case can be made for government intervention to correct for the failure. But whether or not government intervention is a good move depends on the nature of the market failure, the complexity of the task of remedying it and the competence of the government.

The circumstances of market failure are quite specific – far more specific than the wide range of situations over which regulatory welfarists seek to justify government subsidies and price regulation. Genuine market failure arises in circumstances of monopolies and other forms of anti-competitive behaviour; unevenly-held information; positive or negative spill-overs (otherwise known as externalities); public goods; and common resources like fisheries and water.

## **Anti-competitive behaviour**

Businesses conspiring against consumers undermine competitive markets. Adam Smith warned that monopoly is the great enemy to good management. Regulation against anti-competitive behaviour is essential to the efficient functioning of markets.

But great care needs to be taken to ensure that competition laws and practice do not, in fact, stifle competition by protecting inefficient businesses from mergers and takeovers by more efficient operators. Inefficient, poorly-run businesses should be subject to takeovers or mergers by or with efficient, well-run businesses, as long as the resulting entity behaves competitively against other rivals. Two business rivals in an industry might be constantly at each other's throats to the benefit of consumers while five businesses might collude against consumers through price fixing. It is not

the share of businesses in a market that matters but whether those businesses are behaving competitively.

Market democrats protect competition from business, not business from competition. That's why the Rudd government, through competition minister Chris Bowen, is proposing to replace the previous Coalition government's so-called Birdsville amendment to the Trade Practices Act, which is based on market share, with pro-competitive amendments based on the misuse of market power.

### **Unevenly-held information**

Markets function better where information is widely dispersed. Buyers and sellers come together when they know of each other's existence. A buyer wanting a higher-quality used car will pay more if he or she is able to gain enough information to be able to distinguish between a quality vehicle and a lemon. Well-run businesses are more able to attract debt and equity financing than inefficient businesses. Financiers can direct capital to efficient, innovative businesses and away from poorly-run ones if they know what's going on inside those businesses. That's where the share market comes into play. And it's why governments insist on public disclosure of all relevant information. It's why governments outlaw insider trading – buying and selling shares in publicly-listed companies on the basis of inside information that is not publicly disclosed. It's why laws are written against providing false information to financial markets.

But as in so many walks of life, overly-zealous regulation relating to disclosure and corporate governance can do more harm than good. The most visible costs of overbearing regulation are the compliance costs to all businesses, including those that are well run. But the biggest costs are less visible and more pernicious. They are the costs associated with reduced commercial risk-taking by managers. A more risk-averse business community will generate less prosperity since it will be less innovative. Remember the message of the Tasmanian cheese-maker. Everyone bears the cost, not just the affected businesses.

This is why Financial Services Minister Nick Sherry is working on dramatically simplifying the disclosure documents required of financial advisers, making them at the same time both shorter and more effective.

### **Spill-overs**

When a business produces and sells a good or service that has wider benefits to the community over and above the benefits that accrue to the business, it is said to have produced a positive spill-over. A biomedical research business might achieve a scientific breakthrough from its research and development that allows other researchers to advance the state of knowledge and achieve further breakthroughs. But since that business cannot capture all of these benefits for its own profit it will under-produce research and development. Innovation has wider benefits for the community, since the new ideas and inventions can be used in a range of applications beyond those available to the innovator and can spawn more new ideas.

A business investing in the education and training of an employee is helping to create a more productive workforce in that business. But those skills are also valuable elsewhere and the employer knows the employee is free to move to another business. The employer cannot capture – or internalise – all the benefits of the education and training.

Education, training and innovation are said to offer positive spill-overs for the wider community. Since a private provider cannot capture all of the benefits of investing in them, education, training and innovation will be under-provided if left entirely to the market; the market fails in providing goods and services that offer positive spill-overs.

A role exists for government in supporting activities that offer positive spill-overs. That is why governments offer subsidies or tax breaks for private sector research and development. It is why governments fund universities to undertake pure scientific research that, in its own right, has very little direct commercial value, but which adds to the total body of scientific knowledge. And it is why governments get directly involved in education and training.

But care needs to be taken in the design of government policies to boost the supply of goods and services offering positive spill-overs. Poorly-designed tax concessions may be little more than a gift to businesses if they simply reward research that would have been undertaken anyway. Government involvement in education and training does not mean there is no role for competitive markets in the supply of these services.

Unfortunately not all spill-overs are positive. Negative spill-overs are most commonly associated with environmental damage. When the costs of air, water and noise pollution are not fully borne by the polluter, market failure occurs. A business that pollutes a river or the atmosphere does not bear the full cost of producing the good; some of that cost spills over onto the broader community.

*Market democrats* argue that market solutions to market failure usually will be more efficient and effective than clumsy, ill-considered government regulations.

## **Public goods**

Market failure occurs in the supply of what are known as public goods. A public good is one whose use by one consumer does not reduce the supply available to other consumers. Two examples are the defence of a nation and the transmission of radio and television signals. Once a military defence system is established, additional citizens, whether from immigration or natural increase, can benefit from the nation's defence without reducing the availability of defence to other citizens. And when radio or television waves are emitted, extra people tuning in do not reduce the availability of those signals to existing listeners or viewers.

Competitive markets cannot supply enough of a public good from the community's perspective. Free riders would need to be excluded and different prices charged to different consumers, depending on the value each consumer placed on the public good. Competitive markets are incapable of this sort of price discrimination.

Governments might therefore be better suited to supplying genuine public goods like national defence, security against terrorism and licences to transmit television and radio broadcasts. Of course, governments can contract out some of these services to private providers such as defence equipment and defence clothing suppliers and private television and radio businesses. The crucial role of government is in determining the optimal amount of a public good that is provided from the community's perspective, since a private market cannot do this.

## **Common resources**

Another form of market failure arises in cases of a common resource where no user has the right to exclude other users. Fisheries are a good example. It's not in the interests of anyone that the resource is over-fished, though it is in the interests of each individual to take as many fish as possible. But, since each individual cannot exclude the others, the fishery will be depleted if left entirely to the market. A role exists for government to limit the number of people fishing and the catch that each can take. Governments appropriately issue fishing licences and close fisheries for parts of the year to allow fish stocks to replenish.

The same applies to ground water resources and surface water entitlements. If everyone had unrestricted access free of charge, the resource would be destroyed and no-one would benefit.

In cases of common resources, governments have a role in issuing use entitlements and in restricting the total number of entitlements issued. This cannot be done by competitive markets. Again, market-based solutions, such as trading in water permits, can be the least-cost way of remedying the market failure of common resources.

## **Failing the market**

Businesses seeking protection or new government regulations commonly seek to justify these interventions on the basis of remedying purported market failure. They assert that the playing field isn't level or that they need help against 'unfair' competition. Some are brazen enough to claim that the penetration of imports from low-wage Asian countries is evidence enough of an uneven playing field. Since when did a level playing field require all countries to have the same wage rate?

Some businesses beat a path to my door seeking cash payments, tax breaks and law changes to give them an advantage over more efficient rivals. They want the benefits of competition in the rest of the economy in the form of lower input costs, but not competition in the markets into which they sell. These public champions of a free-enterprise Australia want the government to give them a little piece of socialism in their own industries.

## **Expanding opportunity in a market democracy**

Disadvantage in wealthy countries like Australia can be traced to one major deficiency: poor education. If we can fix education we can fix most disadvantage. Education begins in the very early years with early childhood development.

Early childhood development will be impeded in dysfunctional family situations – in violent homes, in families where a parent or both parents suffer from depression or engage in substance abuse or addictive gambling.

In wealthy countries, many highly-intelligent, brilliant young people miss out on a good education. In the poorer communities of these countries, these bright children are inculcated with the belief that they aren't cut out to excel at school and that they certainly should not aspire to a university education.

Too many teachers in poor communities, struggling just to administer pastoral care to the children of broken, dysfunctional families, accept and reinforce these prejudices.

A couple of decades ago, decent people rightly condemned and rejected the view of extremists that black people were genetically less intelligent than Anglo-Saxons. Chauvinists argued that women were genetically inferior to men, because they had smaller brains. That ignorant, despicable argument was cut to pieces by decent people.

Yet to this day there is a general acceptance that children living in dysfunctional, welfare-dependent families just aren't as bright as those living in affluent communities.

How would the better-off have fared if they had instead lived in a household where the only book is a telephone book? Would they have been able to learn if every day they went to school hungry, if their mother was routinely beaten by their drunken father, if they were bashed at home, if they were sexually abused?

What makes people believe that abused, bashed, hungry children are genetically less intelligent than the children of doctors and lawyers? Isn't it equally plausible that they are just as intelligent as their better-off peers but that they never get the chance to excel?

Children living in poor communities and dysfunctional families do not enjoy the same opportunity in life as those living in affluent suburbs and in positive, harmonious families. It's not their fault and they shouldn't be condemned to an unhappy life by the circumstances into which they were born.

Expanding opportunity in a market democracy starts with wiring the brains of infants through the nurturing care and attention of loving parents. Where parents cannot do this alone, governments can play a role in supporting them through early childhood development programs.

Never before has the wealth of our nation been so directly connected to the well-being of our people. The campuses of our pre-schools, schools, training colleges and universities are the places where economy meets society, where good economic policy *is* good social policy.

A society that loves learning is an open society, a creative society. A creative society lifts the human spirit in a vibrant community.

Kevin Rudd's education revolution is designed to help fashion an imaginative, creative society that provides opportunity for all children. Education Minister Julia Gillard, also the Minister for Social Inclusion, is working with Jenny Macklin, the Families and Community Affairs Minister, on early childhood development and early intervention programs, including the Government's policy of universal pre-school for four-year-old children.

## **Market democrats in the community of nations**

Australia as a market democracy can be a cause for good in the community of nations. Rich countries condemn poor countries to ongoing poverty through barriers to imports, corrupting global markets and thwarting the efforts of developing countries to create their own prosperity. Locking poor countries out of rich-country markets and then sending them aid simply masks the injustice of trade restrictions.

*Market democrats* support global trade liberalisation as the primary remedy for poverty in poor countries. That's why Trade Minister Simon Crean is working so hard on re-starting the stalled Doha Round of multilateral trade negotiations.

## **Market democrats as custodians of the environment**

*Market democrats* accept the role of custodians of the environment both on our ancient continent and in the global effort to arrest environmental degradation. *Market democrats* consider that environmental challenges need to be assessed on the basis of the best scientific evidence, not on a desire by evangelists to create a non-market economy that eluded them upon the collapse of the Soviet Union in the late 1980s.

Market-based solutions are well-suited to rectifying or avoiding environmental damage. A well-designed emissions trading system allows the market to identify least-cost ways of reducing carbon emissions. That's why Climate Change Minister Penny Wong is working with the other economic ministers on an emissions trading system for Australia.

## **Achieving prosperity and fairness in a market democracy**

*Market democrats* are the modern Labor champions of the traditional Labor values of prosperity, fairness and compassion. *Market democrats* support:

1. reward for effort, risk-taking and entrepreneurship in an open, competitive economy as the best way of creating prosperity;
2. individual freedom and the supremacy of the people over the state, not the subjugation of the people by the state through financial and regulatory welfare;
3. harnessing the power of the market for the public good, to attain fairness out of prosperity, not fettering the market with heavy regulation;

4. government intervention only in tightly-defined situations of market failure, not anti-competitive government protection and regulations;
5. expanding opportunity, not the welfare state;
6. government income support for the genuinely needy, subject to mutual obligation upon those who have genuine income-earning prospects;
7. equal opportunity for every child to a high-quality education as the golden key that unlocks two doors – to prosperity and fairness – in a competitive, compassionate society;
8. creating stronger communities and collectivism through good social behaviour encouraged by the self-esteem gained out of reward for effort;
9. Full participation in the community of nations to rid the world of poverty and oppression, led by the liberalisation of world trade; and
10. Custodianship of the environment through preserving biological diversity and playing a full part in a global collective effort to limit greenhouse gas emissions.

A modern Labor philosophy of prosperity and fairness in a market democracy is faithful to Labor traditions while offering creative responses to the challenges of the 21<sup>st</sup> century. I commend these ideas to you for your consideration.