

CREATIVE DISTRACTION



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Editors' Note

We wake up from our election hangovers confused, bewildered and of course, sober. Perhaps we wake up to find the realisation of our political and economic imperatives. Perhaps we realise that society today will not allow our goals to be realised. Or maybe it's not important to us. Read this magazine! Did that flow? Who cares? This is only propaganda right?

In response to that question, everything is propaganda whether you like it or not but with *Creative Distraction*, you (whatever your ideology, or worldview may be) have the chance to make your input to the complicated web of information that is the media. *Creative Distraction Issue V* has a wide range of ideas from Jimmy Liu's take on the music industry to Greg Bihari's perspective on population growth. Josiah Munro asks the question "is there such thing as rational economics?" and Archie Chapman and Matt Ogg raise issues concerning John Howard's policies and free trade. Enjoy this feast of knowledge, or lack-there-of. However you take it, remember, it's all propaganda!

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We would love to release these pamphlets more frequently so if you have anything to say, say it! This magazine is a forum that you can join. Write us letters, criticize our writers, praise our writers, and if you have the ability, write us an article, so people can praise and criticize you! It's all good fun. Indulge yourself with a good read,

Prerna Mankad, Matt Ogg and Justin Hardman



KaZaAnomics

Jimmy Liu

In the one of the biggest and most controversial challenge to ever to face the music industry, have the record labels only themselves to blame?

Mention the likes of Napster, Kazaa, or Gnutella to any of the top record label executives, and they'll berate about how the millions of people who, by illegally downloading music each day, infringe copyright laws, steal intellectual property, and destroy the livelihood of hard-working artists in the process. Then when the rhetoric's over, he or she might drive off in their big red Ferrari. It is widely accepted that peer-to-peer (p2p) sharing of music and other copyrighted data has been both an explosive and controversial by-product of the freedom of exchange phenomenon that is known as the internet.



At any given time, two to three million users are logged on to Kazaa, exchanging millions upon millions of songs, movies, software, and pictures for free. One estimate alone puts Kazaa's retail value at over \$2 billion a month. P2p has also found itself entangled in a legal quagmire, with the industry seemingly willing to stop at nothing to see the back of p2p, while the networks attempt to alienate themselves from the actions of their users. But do the record labels themselves have a case to answer for?

Economies of scale tells us that the average cost of production declines as the number of units produced increases. These reductions in cost are often translated into cheaper goods for the consumer. This also, to an extent, explains why the entertainment industry is dominated by only a few very large multinationals.

Economies of scale are evident in nearly all industries where new technology and increasing consumer demand are the driving forces behind change and innovation: from cars and light bulbs, to computers and mobile phones. Movies on VHS tapes used cost five-to-ten times more to both produce and consume twenty years ago (and this was without the special features). The same trend was evident in portable CD players. Today, you could get a movie on VHS for less than \$20, and Discmans rarely cost more than \$200. As more and more people owned VCRs, it became apparent to the movie industry that they could be making larger profits if they decreased the price of tapes.

So why then, despite increased sales in CDs and CD players, has the price of a CD remained stagnant? The industry believes that music can be associated with other public goods like bridges or roads (although technically roads and bridges are not public goods). They cost a lot to create, but once they're around, many people can enjoy them at low cost. Just as the government supports bridges by giving builders a concession to collect large tolls, even though your trip costs them a minimal amount; it supports music production by granting a copyright which enables the artist to collect from listeners, even though copying a song costs almost nothing. Hence, downloading music for free off the internet is like taking a detour around the toll booth. Even if you don't get a ticket, you've taken a free ride on someone else's investment.

This explanation does take a few steps in explaining the inflated costs of CDs. However, why then was there a relative decrease in the price of cassette tapes and vinyls? If the average cost of pro-



ducing CDs, cassette tapes and vinyls (with identical copyrights) are roughly the same, then shouldn't they all be sold at roughly the same price too?

Of course not! As any student of economics would be proud to testify, the more plausible reason was the hunger for profits. CDs are superior to cassette tapes in every way. They last longer, sound better, and can locate the song you want in an instant. Consequently, the price of CDs stayed artificially high throughout the 90s, with the industry knowing full well that consumers did not have a choice.

Enter the internet. Along with mp3s and the growing popularity of CD burners, this new medium for recorded music distribution caught the industry napping. Having swept across cyberspace like a wildfire, a real substitute for CDs emerged, with consumers now able to download all their music for free, instead of paying over-inflated prices for CDs.

Once stirred however, the record companies did not embrace this new form of distribution (as it had done so with CDs and cassette tapes) but rather, it launched an all out attack, taking the p2p networks (and even some of its users) to court for millions of dollars in lost revenue. The exercise proved, and continues to prove fruitless, as where one network would be forced to shut down or retract from the dark side, half a dozen new ones would pop up. Copy-protecting CDs hardly even made an impact.

The big question is, if the record industry had reduced the price of CDs, and used the new digital medium to its own advantage rather than to fight it, would p2p ever have taken off in the way that it did? Probably not (although there will always be people who try to get something for nothing, the same ones who record songs off the radio). The popularity of Apple iTunes in the US, which sold more than 70 million songs in its first year alone, proves that people are willing to pay a small price to download music, rather than risk facing legal action or rip off their favourite musicians. P2p may never have reared its ugly head had there been a few iTunes roaming the digital landscape (getting the ACCC's approval for the big record labels to set up shop together would have proven a challenge however).

Overall, p2p is here to stay in a music industry which will never look the same again. Record companies must learn from the mistakes they made in dealing with p2p, so that when the next big thing arrives, their artists' livelihood will not be placed in jeopardy in order to make some profits in the short run. Because in the long run, you can't stop the music, or p2p.



Free Trade?

Matt Ogg

It was April this year that in Washington, not Canberra, a free trade agreement was signed by representatives of Australia and the US, carving a deal that would apparently lead to greater economic prosperity for the Australian people. It was so great in fact that John Howard claimed, "it's not perfect...but the best we could get in the circumstances".

With the war in Iraq still raging strong, and the conservatives adamant not to give in to the will of terrorists, there's no better time for a bit of bonding between these two nations, after all, there's no better way to bond than to bully.

But let's not get to rash – first we must analyse what free trade entails in theory and then compare this to what it entails in reality, and why, like communism, socialism or enforced democracy, the theory itself cannot be achieved in its purest sense, because the means towards it are hindered by self-interest. Today, decision-making is made by the very few who are deemed deserving, while many suffer, not just in the third world, but in the western world also.

Free Trade in theory takes into account comparative advantage, a theory whereby trade occurs in a specialist sense, and resources are used to their maximum capacity. A protectionist policy on trade however means that this is not possible and industries that would otherwise fail are given security by tariffs, quotas, subsidies and the like. However, The Australian/United States Free Trade Agreement (AUSTA) does little to erase barriers for America, and does little to help Australia. As John Quiggin stated in the previous edition of *Creative Distraction*, this Free Trade Agreement is "nothing of the kind".

In the deal, market access for sugar was missing, and American farm subsidies have not been lifted. On top of this, our cultural industries such as music, entertainment and the media are under attack. The doors for importing American culture have been opened wider, and those of Australian cultural identity have been left to idle at the mercy of the wind.

On the other end of the spectrum however, many businesses praise the agreement.

"The Agreement will provide massive opportunities for Australian companies of all sizes to gain access to the world's largest market," said Hugh Morgan, President of the Business Council of Australia. The agreement claims that billions of dollars of increased trade will result between the two countries and that 99% of manufactured goods will become duty free. But should we believe this? History would think otherwise.

In economic forecasting, to get an idea of what the future holds, one must look at the past to try and get an idea of how certain decisions will result, and of what the motives of certain decision makers are. The first parallel I will draw is the US/Canadian Free Trade Agreement signed in January 1989. In the case of Canada, a country very similar to ours – a lot of land, not enough people - there was the dilemma of long run productivity vs. short run growing pains. Certain business flourished but one third of industries that had the largest tariff cuts fell 11% in output, and employment fell by 15%. In the case of Australia, our long-run benefits serve industries that aren't even in favour of our comparative advantage and our short-term losses, not to mention our long-run losses in terms of our identity, could be shattered.

American President Bush joined the moral debate in May 2001 before the Council of the Americas, saying, "Open trade is not just an economic opportunity, it is a moral imperative. Trade creates jobs for the unemployed" and it provides "new hope for the world's poor." The case of Canada would prove otherwise in regards to unemployment and the following two examples will underline that this statement in its entirety is far from correct in reality.



In his book *Open Veins of Latin America* Uruguayan journalist, Eduardo Galeano asks the question, "Why is Latin America poor?" Why is it that this part of the world, so wealthy in its resources and a key provider of the raw materials that make the western world thrive, has such a low level of wealth? He concludes that capitalism has made it the situation so. In order to thrive he states "capitalism requires access to cheap and easily exploitable resources, both of the human and natural varieties."

Lets get things into perspective. Capitalism at its finest goes hand in hand with free trade, yet a part of the globe, enriched with natural resources, is somehow poor because of it. This just accentuates the fact that when people act in self-interest, as economic theory shows, certain parties will be worse off, and what can be seen as the best economic strategy for one party, might not be the best for another. In our sense this is that certain Australian businesses will profit, and the Australian people, and the Australian culture will not.

The final parallel is the agreement on textiles and clothing (ATC) signed in 1974 with a goal of a phased lowering of tariffs and quotas allowed under the multi-fibre agreement (MFA). It was said that by 2005 it had the potential to increase third-world earnings by US\$127 Billion. 2005 beckons, and the US have lifted quota restrictions on only 6% of imports, and the EU less than 5%. We then ask the question, can free trade agreements and their promises be seen as reliable? Or are they merely a political tool of bonding between powerful nations, and weaker nations?

Ever since Curtin turned back the ships, told Churchill were to go, and Australia turned to America as its new leader, the alliance has been strong. But alliances, like appearances can be deceiving and it is time, not for Australia to reject America as an ally, but merely to stand up for itself. We are rich in culture and natural resources, and we have many neighbours that have a deep seeded hatred of all that is American. Perhaps we could keep our friendship with the US, and do what is best for our own interests. Economist Ross Garnaut stated that the AUSTA could "harm the multilateral trading system and Australia's interests globally and in the region."

Before we make rash decisions that aren't quite perfect we must remember that Texas, the home the President, was once owned by the great Spanish Empire –It was essentially Mexican. But somehow along the line, the United States got the edge over Mexico and today one is the leader, and the other is a third world nation. The world we live in today is capitalist and in this type of world, winners take what they want and suckers take what they can get. The pecking order of the world is changing and is it really wise of us to cling so tightly to something so unreliable? We must remember Australia has the ability to make choices and it is up to us to ensure we make the right ones.



Howard's Lack of Vision

Archie Chapman

The Australian Labour Party has long been accused of catering for special interest groups at the expense of the Australian economy. But recent evidence suggests that the Liberal party is doing an even better job. In this essay, I will argue that the Liberal Party, under the auspices of John Howard, has merged economic and social policy in such a way to benefit wealthy and powerful members of society, at the expense of general Australian welfare, resulting in a breakdown of social cohesion. This has two manifestations; in Howard's lack of economic vision, and in his divisive and populist nationalistic social agenda.

Howard's lack of economic vision

This is the second period of time that Howard has been in a good position to undertake economic reform, and twice has his ability and vision been questioned. In fact, Howard himself refers to the period he was Treasurer for the Fraser Government as "the seven wasted years." In the period of Howard's leadership of the Federal Government, the Australian economy has undergone the longest sustained period of growth in thirty years. But, in contrast to the claims of senior Liberals, most of this growth has not come about from the small number of reforms undertaken by current government. Rather, the current boom is the result of reforms, deregulation and privatisation undertaken by the Hawke-Keating governments, and in some part due to tariff reforms in the 1970s by the Whitlam government.

The GST, the only real reform Howard has successfully pursued, has been successful, but a GST is hardly a revolutionary idea. (In fact, due to reforms such as the GST, the Government is running a surplus, while average household debt has grown uncomfortably large). Real tax reform, including superannuation, maternity leave, and social security reform have been either ignored or denoted "special interest" issues that do not apply to the whole of society, regardless of their moral weighted. The attempted reform of the social security system, resulting in the creation of Centrelink and the tendering out of provision

job search facilities to the private sector, hide a more sinister undertone of social engineering; the true mark of a manipulative conservative.

Howard's nationalistic social agenda

The inequitable distribution of the benefits of recent growth in Australia have been exacerbated by Howard's social agenda. Pushing a populist platform of "user-pays," Howard has stripped support from the unemployed (work for the dole) without offering either job or training opportunities, and without reforming an income tax system that provides huge disincentives to take up work (through very high effective marginal tax rates). He has even suggested extending this program to people unable to work due to disabilities, under a banner of "social inclusion." All of this while the top marginal rate of tax has been reduced. Australian Aborigines, who face more than their fair share of social impediments, have had funding cut and their peak representative body, ATSIC, disbanded. Universities and higher education facilities have had funding cut, with the Liberal party pushing for the operation of market-type funding arrangements which do not promote the long-term research in basic sciences and technologies so essential for economic growth.

The Liberal party stance is not well thought out, and Howard's collection of poor economic policy and divisive social policy is tearing the fabric of Australian society apart.



A man with vision?



Even More on Population Growth

Gregory Bihari

A great many views have been expressed regarding the further expansion of the Australian population. At one end of the spectrum, Malcolm Fraser once opined that Australia should seek to expand its population to fifty million citizens by the year 2050. At the other end of the spectrum, the environmentalist, Tim Flannery, has suggested that Australia should aspire toward reducing its population to between six and twelve million. As noted by Peter Dawkins and Paul Kelly, the editors of *Hard Heads, Soft Hearts* (2003, p. 91), few experts currently consider either of these goals as realistic. In my essay, in Volume II of *Creative Distraction*, espousing neither of these radical views, I argued that the Commonwealth government needs to develop a population policy, based on the maximum number of people, given current states of affairs, that the Australian environment may safely accommodate, *ceteris paribus*. I emphasised that such a number would be by no means set in stone, but would be open to revision, once we learn better how to flourish in harmony with nature. In questioning many of the traditional justifications for immigration, I made clear my personal belief that population growth needs to be moderated. However, my purpose was not to pluck some figure out of my head, and propose it as the desirable size of Australia's population: to do so would have been uninformed and arbitrary. In developing a goal for population growth, the government needs to engage in widespread consultation with the electorate, and with environmental scientists whose expertise lies in this field. The end product may well be closer to the views of either Fraser or Flannery, but what is important is that expansion is carried out with some specific target in mind, and that there is clear evidence that such a goal furthers the interests of Australia and her people. This position struck me as moderate, and common-sense, and yet, it has proven to generate an avalanche of controversy. Since the goal of the article was to encourage debate, one might suppose that its objective was achieved. However, unwilling or unable to rationally engage with the content of the my argument, it must be conceded that both published responses were disappointing. On the one hand, I received a vicious personal attack, and on the other, a sophisticated piece of irrelevance.

That one can be opposed to immigration without being opposed to immigrants is a point too

fine for crude intellects. Despite the importance of the present topic, it does not receive the attention it deserves, largely because, regardless of how forcefully one stresses that one's opposition to immigration is not racially motivated, there will always be malicious individuals who will choose to assume the worst, and will throw around irresponsible and unsubstantiated accusations. The response in Volume III was a valuable example of the kind of bullyboy tactics that such individuals employ with glee. Their attack is focussed upon not the theory, but the theorist; upon not what is said, but what is not said. And insofar as their poisonous pens work not to further debate, but to silence it, they are pusillanimous muck-rakers, and the enemies of reason. Those sufficiently courageous enough to publish dissentious opinions must expect to attract the venom of so many stinging flies. It is the duty of those of us for whom freedom of speech is not a theory, but a practice, not to be silenced by such thuggery.

Before moving on, one point needs to be made about the blasé attitude the author of this response recommended. Her 'She'll be right, mate,' attitude to population growth is exactly the kind of dangerously apathetic position that Australians need urgently to correct. That the world population is forecast to stabilise at an alarming thirteen billion, far from being a reason for complacency, is exactly why this issue needs serious attention. The question that still needs answering is, *how many of this thirteen billion can Australia currently safely accommodate*. It stands to reason that so long as there are nations less affluent than Australia, there will be prospective migrants. Hence, if Australia wishes to remain a lucky country, we must voice a resounding rejection of those who think the problem of overpopulation will go away by itself.

Fortunately, the second response, in Volume IV, was of a more suitably civilised tenor. It must be granted that the article was a valuable contribution. However, its primary value was as a telling example of many economists' tendency to conceal a lack of substance beneath a glass bead game of mathematical formalism: beneath its bells and whistles, it proved to be ultimately vacuous. Its author went to considerable lengths to prove, mathematically no less, that the amount of food an economy is capa-



ble of producing is not a constant quantity, but is dependent upon its level of technology, and other contingencies. This banal fact, which no one today would deny, was really never in question. With modern breakthroughs in agricultural science, I doubt anyone for a long time has seriously entertained the idea that the growth of food production constrains Australia's capacity to expand her population. My original argument was that the expansion of Australia's population places further, unnecessary strain on her fragile ecology: the rejection of Malthus, in Volume IV, said absolutely nothing to answer this. With Australians responsible for more greenhouse gas emission per person than any other nation, and with the mountains of non-biodegradable plastics we consume every year, it is patently obvious that we are not currently living in harmony with nature. Without fundamental changes to the way we live, the more people, the more environmental impact. That one can point to dingos, foxes, rabbits, cane toads, or feral animals as arguably greater perpetrators of environmental damage than humans (even though all these species were introduced to Australia by humans) does not lessen the damage of which we are all guilty.

Despite the differences of their approach, both articles were alike in one significant respect: they were both entirely negative. Both articles attempted to find fault with my reasons for advising caution with regards to further population growth, but neither were able to offer positive arguments to demonstrate that further population growth would lead to net gains for the Australian nation. Those who propose change must prove that such change is recommendable. If my critics think that further population growth for Australia is desirable, then the onus is upon them to prove that such a policy is advisable. As I noted in my second article, in Volume III, whether one refers to the Neo-Classical growth model, or to Solow's endogenous model of economic growth, it is agreed that population expansion is a hindrance to a nation's economic performance. That population growth dilutes a nation's capital per head is a widely accepted macroeconomic fact. Figures quoted in Quiggin's *Great Expectations* (1996, p. 15) suggest that for every further one per cent Australia's population is allowed to increase, the rate of our economic growth per person falls by 0.4 per cent. Add to this the undeniable environmental damage, and the additional strain placed on our already overstretched public goods, such as our dwindling public health and education systems, and it's increasingly clear that Australia has more

to lose from further population growth than it has to gain.

Some people wrongly think that humanitarianism demands we support immigration. But the opposite is the case. In the less developed world, it is generally the best and the brightest who have the capacity to immigrate. Consequently, immigration is the process by which the developed world brain drains less developed countries. Immigration helps retard progress in the underdeveloped world, and for this reason, those who care about the plight of the starving billions must say *no* to further immigration.

Finally, I would like to address one further 'counterargument' I have experienced. It is probably too stupid to warrant serious attention. However, as a knee-jerk reaction of population growth apologists, it is sufficiently widespread to deserve an answer. These misguided individuals spew, '*What makes you think you have a better right to live in this country than anyone else?*' To answer such people, one needs to respond with but a single word: *democracy*. According to democratic principles, the policy of the Australian government is to be decided by Australian citizens, not potential citizens, or prospective citizens, but solely by Australian citizens. Just as we Australians have no input into the governing of foreign nations, and cannot expect foreigners to take into account our interests and desires when they lobby the governments of their sovereign nations, Australian policy must be formulated to further the interests of Australians, and Australians only. If it is found that population growth constitutes a threat to the net welfare of our sovereign state, the continuation of immigration policies would represent a breakdown of the democratic process.

The most important truths are often the hardest to swallow. And that my position has attracted contention goes some way toward its vindication. Those who have no love for Australia may not find my arguments compelling. But those of us who are committed to the welfare of our nation must be prepared to take a stand. We who hold our nation dear, and demand our elected representatives truly represent our interests, we must not shy away from the mudslinging of scribbling she-wolves. It is time for Australian patriots, one and all, to stand up and be counted.



Rational Economics

Santa Claus, a practical economist and a chronic drunk are walking down a road. Up ahead of them, a hundred dollar bill lies on the road. Who gets it? The answer, of course, is the drunk. The other two are simply mythological inventions.

It's an exaggeration, but like many jokes does contain an element of truth. If economics does have the answer for everything, as it sometimes seems, why isn't this world so much better? Why isn't anything done about society's many problems?

Textbooks abound with examples of gross incompetence by the government. Frank and Bernanke (2004) cite the mass of homeless people in the United States due to price ceilings, while others such as Layton, Robinson and Tucker (2002) laud the concept of immigration and free trade. And this is despite the unpopularity of such topics among both the government and the general population. Howard, for example, is finding this out the hard way with the recent free trade agreement negotiated with the USA.

Yet these aren't isolated incidents. Reality is full of cases where governmental organizations and economists in general vastly disagree on how to solve society's problems. A. Paton's article regarding the Washington Consensus in the last issue is a point in case.

Society has an issue. Economics has an answer, at least equal to if not better than anything the government has to offer. And yet nothing happens. Why?

Put simply, rational decision making by the individual. The majority of the population probably agrees with the idea of removing maximum rent prices. But the small minority are vocal in their opposition, and these people adversely cause the politicians to make choices based upon what will keep them in power come next election time. And who can blame them? After all they are simply acting to follow their personal goals as we all do without remorse.

If a whaler stops fishing for a period then his catch in the long run will be much greater, as the marine life has a chance to breed. But if that whaler doesn't catch any whales, another surely will, legally or not. So people still endanger fish breeding stocks, ensuring they don't lose out on any potential profits. Some benefit, many don't.

The prisoner's dilemma is a classic example of game theory. Two prisoners are held in a cell, and must decide whether or not to confess to their crimes. Each could simply stay silent, and walk out unscathed. Yet the optimal outcome is for both prisoners to admit their guilt, and suffer a small prison sentence in order to avoid the risk of a much larger one.

As in the real world, the best solution is not always the optimal one. Or the solution used.

Economics is, in many ways, a theoretical discipline. It can meticulously describe the problem in detail, and even provide the perfect solution. But ultimately, this isn't a perfect world we live in, and so often the perfect solution just isn't feasible. We aspire to lofty goals, but simply can't reach them.

Sure, we can allow cheap foreign goods to flood the market, and allow Australians to specialize in other products. But a small number of local companies would be harmed, and the political parties would sign their own death warrants in vital seats. We can break up the monopolies enjoyed by large companies such as Ergon Energy and Microsoft. But don't get your hopes up. The opportunity cost to those in control is too great, and so we can wait until the cows come home before any of the above becomes a reality. Even if it is ultimately beneficial for the greater good of the nation.

It is ironic that economics' greatest flaw is also its central tenet. We all act out of rational self-interest, and therein lay humanity's problem.