

National History Challenge 2009

Australian Prime Ministers: Triumph over Adversity

Bob Hawke and the Floating of the Australian Dollar

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In December 1983 the Hawke government floated the Australia dollar meaning markets determine its value instead of the government; even though there was serious opposition from all sides of the political spectrum. Today, because of Hawke's actions during that time, Australia can stand proudly in this globalised world as a foremost nation and economy.

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Bob Hawke is Australia's longest serving Labor Prime Minister. During his eight years in office, he faced numerous challenges ranging from international issues and conflicts to domestic equivalents. However in despite of these adverse conditions Hawke succeeded in many areas such as reintroducing the Medicare Program, increasing awareness about the environment, starting reconciliation steps with Indigenous Australians, introducing reforms in education and much more. But perhaps Hawke's greatest achievement was the globalisation and deregulation of the Australian economy, bringing it out of its traditional and protectionist roots and thrusting it onto the world stage. Throughout his four terms in office he endeavoured, overcoming adversity, to make Australia the international nation it is today. His first achievement and perhaps most crucial, was the floating of the Australian dollar in December 1983; called, *'one of the most significant economic policy decisions of the era, if not in Australian history all together.'*¹ As a result of the float, the value of the Australian dollar became determined by Australian and overseas investors. This opened up its economy to world markets and was a key step in Australia's emergence into the globalised world.

Hawke and his government inherited a nine billion dollar deficit when they came into office in March 1983. This economic crisis heavily influenced many of Hawke's decisions. With unemployment above 10% and record high inflation the government believed that the only solution was to increase the efficiency and competitiveness of Australian industry and fight their way out of the downturn. To do this the idea of deregulation was drafted to Hawke. The suggestion of deregulation first originated from a 1981 inquiry into Australia's financial sector by Sir Keith Campbell during the Fraser Government. His proposal included floating the Australian dollar, tearing it away from its protectionist background of being pegged². A floating exchange rate is a system whereby the rate of a country's currency is determined by market forces without any intervention from the government.³ For much of its history, the Australian dollar was pegged to the British pound. A pegged rate is a system whereby the rate of a country's currency is set at a particular level in relation to another currency.⁴ In 1946 the Australian dollar was altered to become a fixed rate against the US dollar and in 1971 changed to a moving peg based on the US dollar (the Australian dollar's value was chosen in comparison to the currency it was pegged to). Finally in 1974 the dollar was changed to a

¹ Bob Hawke, Prime Minister and policies (1972-today)

² History of the Reserve Bank (http://www.rba.gov.au/AboutTheRBA/History/history_of_the_rba.html)

³ Financial definitions (<http://www.financial-elearning.co.uk/D2002/terms/defs/fdefs.htm>)

⁴ Financial definitions (<http://www.financial-elearning.co.uk/D2002/terms/defs/fdefs.htm>)

moving peg against a basket of currencies known as the Trade Weighted Index.⁵ In 1983, the general practice on valuing the dollar was that every morning the Governor of the Reserve Bank and the Secretaries of Treasury, Department of Finance and Department of Prime Minister and Cabinet would agree on a value that would be set for the day. This system was considered archaic by many as it was especially prone to unpredictable jumps and falls in the dollar due to the distinct lack of unity with the markets (the officials who set the value had very few limitations on what value they could decide).

The suggestion of floating the Australian dollar and implementing other deregulatory measures had always been a right wing view. The assumption that the Australian Labor Party, traditionally very protectionist about economic freedom, would support such an idea was preposterous. Labor tended to support tight control and regulation of the economy. Hawke realised that in an age where billions of dollars could be transferred across the world in minutes, the need for a better financial system in Australia was essential. During the late 1970's and early 1980's the global mood was shifting in favour of financial deregulation and Australia needed to change as well before it was too late.⁶ However, before Hawke could do that he needed to convince his own party. Hawke already had a few Labor supporters including economic advisors Ross Garnaut and Eddie Visbord, Finance Ministers, John Dawkins and Peter Walsh, Treasurer, Paul Keating and a few other Labor members but he needed more if he was going to achieve his goal of a free economy. To rally support, Hawke commissioned a new report about deregulation to *'shake the Campbell report free of its Fraser Government origins and dress it in Labor cloth.'*⁷ The updated report recommended several deregulatory measures that would revolutionise Australia and its economy. While some continued to voice their opposition about the float, support began to swell as more of the Labor caucus began to jettison their old views and beliefs in favour of a modernised, internationalised economy.

However even though Hawke was managing to garner support, the Australian economy continued to worsen. But the dollar's value did not reflect this, instead it was kept at an unrealistic level and was seriously damaging Australian industry's competitiveness. The US was also struggling; however their dollar was falling and at a rapid pace. Investors started moving their money into Australia where they could achieve a profit on the higher valued Australian dollar. The resulting wave of investors crashing onto Australia's shore meant even more havoc with the dollar's value. During the later part of 1983 the value became more and more erratic as the officials tried to defer the investors away

⁵ Forex-education: The Australian Dollar (<http://au.biz.yahoo.com/forex-education/australian-dollar.html>)

⁶ Martin, Stephen, Labor and financial deregulation: the Hawke/Keating governments, banking and new labor, pg 279

⁷ Hawke, Bob, The Hawke Memoirs, pg 235

from Australia. This game of cat and mouse meant it was impossible to predict the dollar's value; and still money was gushing in. As more and more capital circulated throughout Australia, inflation surged and interest rates became just as unpredictable as the dollar. It was obvious to Hawke and his newly converted Labor supporters that a change was needed. *It was now just a matter of timing.*⁸

By October 1983, Hawke decided it was time to act. Taxpayers were losing millions of dollars a day and it looked as though this was going to continue indefinitely if nothing altered. However, his government had only been in office 7 months and many of his colleagues were still learning the ropes, including his treasurer. Paul Keating, even though he became one of Australia's best treasurers, had little experience in economics and finance when he was first given the ministership. He relied heavily on his staff and advisors at Treasury for support while he found his footings. This dependence concerned Hawke slightly; some in Treasury were opposed to floating the dollar because it meant they lost control of the dollar's value. Leading the adversaries was Secretary of The Treasury, John Stone. He had the ear of Keating and ferociously tried to change Keating's opinion on floating the dollar. His attempts came to fruition on the 27th October 1983. A meeting had been called to discuss the immediate floating of the dollar; however, Stone's opposition and his ability to influence Keating resulted in the float not going ahead. Instead a compromise was struck; rather than being set in the morning, the dollar would now be valued the evening before. This meant the value became more predictable. Also, the forward exchange rate, the rate set each day for a currency transaction with payment or delivery on a future date, was floated.⁹ It was obvious that this compromise was temporary and that the float was going to happen eventually. Stone had defeated Hawke on this occasion; but Hawke knew that next time it would be him who would emerge triumphant.

Even though the agreement on the 27th October went some way in opening the door to floating the dollar, it did not drastically improve Australia's economic position; money was still pouring into Australia. On the 8th of December, the last day of the parliamentary year, news reached Hawke and his colleagues about an estimated \$800 million that was heading Australia's way.¹⁰ Such volume could not be sustained by the Reserve Bank resulting in the economy being swamped, interest rates dropping and inflation rising.¹¹ This was the final straw; it was now or never to float the dollar. Stone continued to oppose the plan, with talks continuing well into the night. Hawke by now had much

⁸ Kelly, Paul, *The End of Certainty – Power, Politics and Business in Australia*, pg 82.

⁹ Financial definitions (<http://www.financial-elearning.co.uk/D2002/terms/defs/fdefs.htm>)

¹⁰ The day that protectionism died in Australia (www.theage.com.au/articles/2003/12/05/1070351790567.html?from=storyrhs)

¹¹ Martin, Stephen, *Op Cit*. Pg 170

support including Keating himself and it was just Stone and his deputies Dick Rye and Des Moore that were preventing the float from going ahead, which wasn't enough. At 1:00 in the morning, Hawke sent a message to Paul Keating, *'We've just got to do it.'*¹² Hawke was tired of Stone's protests and was ready to bypass his opinion completely.

The next day, market trading was suspended and Hawke and Keating met with senior members of the Reserve Bank and Treasury, including Stone, Reserve Bank Governor Bob Johnson, Deputy Governor Don Sanders and Chief Manager of Financial Markets John Phillips. The decision had been made; the float was to go ahead. In his Memoirs, Hawke recounted the historic event:

'The Bankers led the charge. They were heartily sick of riding the tiger of an exchange rate pegged daily. At the end of each day they were left with the price tag on inward flows, holding their breath about tomorrow and the next day and every day thereafter. The time had come to let the dollar roam free and to let money move in and out of Australia unshackled by regulations, they said.'¹³

Both Hawke and Australia were sick and tired of their outdated, unpredictable system. Both Treasury and the Reserve Bank were ready to act. However there was still uncertainty in the air. No one could accurately predict what would happen to the dollar's value when the float occurred. It was impossible to tell whether the dollar would rise, enticing even more investors, further deteriorating the economy; or fall, allowing Australia more competitive power. The Reserve Bank's best bet was that the dollar would fall slightly, deterring investors and increasing competitiveness. Still, opponents such as John Stone argued that floating the dollar would increase its value dramatically, tearing Australia's small economy apart. But either way it went, Hawke and his colleagues were agreed, the pegged system was obsolete and had to be replaced. The decision was made, without the backing of Stone; the float would go ahead. At 3pm cabinet approved the submission to float the dollar and remove exchange controls from Monday December 12th 1983.

In contradiction to Stone's dire prediction that the dollar would go through the roof and destroy the Australian economy indefinitely, the dollar floated down; rising only slightly in March 1984 to US 96.5c. Then the dollar started to fall, by the end of 1984 it was at US 84c before freefalling in early 1985 to US 65.8c.¹⁴ This 30% depreciation demonstrated that the old system had seriously overvalued the Australian dollar for years resulting in its economy feeling the consequences. A new, competitive, diversified and larger economy emerged; dramatically assisting in lowering deficits and

¹² Hawke, Bob, Op Cit. pg 242

¹³ Ibid, pg 244

¹⁴ The day that protectionism died in Australia (www.theage.com.au/articles/2003/12/05/1070351790567.html?from=storyrhs)

bringing Australia out of recession. Even the unsupportive Stone said the float was beneficial in 1984:

'I personally believe that the decision made by the present government on 9th December last [1983] will stand as its greatest achievement when all else has been forgotten.'¹⁵

Stone had resigned less than a fortnight before he made this address. He accepted that his actions in trying to prevent the float were unnecessary. He also acknowledged that Hawke had beaten him and was right to do so.

As a result of the float in 1983, Australia finally gained the title of a globalised nation. No longer was it the inward facing, English speaking nation drowning in a hemisphere where Asia ruled supreme. The float also opened the door to many more deregulatory measures including, direct controls on interest rates were removed, foreign competition in the banking sector was allowed, the two-airline policy was abolished, competition in the telecommunications industry was permitted, the phasing out of textile, clothing and motor vehicle protection and the reduction of all tariffs to 5%. By granting Australia a floating exchange rate determined by global not just domestic sources, Australia could now withstand economic shocks and remain a competitive and reliable currency. During the 1997 Asian crisis, countries such as Indonesia suffered a loss of US \$171 billion in their GDP.¹⁶ However thanks to the float in 1983 the Australian dollar fell from US 78c to US 55c. Before the float the dollar would have depreciated, but not by 30%. As a result, the economy would have been forced into recession. Instead Australia prospered and competitiveness increased dramatically. Today the Australian dollar is the sixth most traded currency in the world; accounting for approximately 5% of all foreign exchange transactions despite the fact that Australia's economy only comprises roughly 2% of the global market.

Bob Hawke faced many challenges in his attempts to float the dollar: an inexperienced government, a non-supportive party, an ever-worsening economy and huge opposition from John Stone. However, even in the face of adversity, Bob Hawke battled on and triumphed. He defeated his opponents and created the foundation on which the modern, globalised Australia we bear witness to today has grown. In 'The End of Certainty', Paul Kelly wrote:

¹⁵ John Stone, 27th August 1984– '1929 and all that....' – Shann Memorial Lecture

¹⁶ Asian Financial Crisis (http://en.wikipedia.org/wiki/1997_Asian_Financial_Crisis)

'The float transformed the economics and politics of Australia. It harnessed the Australian economy to the international market place – its rigours, excesses and ruthlessness. It signalled the demise of the old Australia – regulated, protected, introspective.'¹⁷

During his times as Prime Minister, Hawke faced much adversity, but he achieved even more. In an interview by 'The Age', he nominated five categories of which he felt he had left a legacy. Those include bringing Australian's together, international relations, egalitarianism and the environment. Finally his fifth category, of which he is proudest of, his economic legacy.

'I'm very pleased that the general consensus of the economists in this country and abroad is that the present strength of the Australian economy owes a great deal - in fact is based upon - the reforms that we brought about in the 1980s.....When we came to office the Australian economy was in a sclerotic condition. We were no longer the lucky country, where the world was just buying our wool and our wheat and our meat and our minerals. It was much tougher and we were not going to be able to compete in that world if we didn't change the economy pretty basically - and we did.'¹⁸

¹⁷ Kelly, Paul, Op Cit. P77

¹⁸ Bob Hawke on his loves, legacies and life after politics
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