

# “The power of simple theory and important facts”: A Conversation with Bob Gregory

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## Abstract

*Bob Gregory contrasts ‘the presuppositions of Royal Parade’ of 1950 Melbourne with the present outlook of himself and Australia at large. He outlines the evolution of his methodological position from the University of Melbourne student to the Canberra policy advisor, and defends that position from criticism. He recalls the genesis of the Gregory Thesis, and advances his account of the decline of trade unionism, the impact of the welfare state on household formation, and Aboriginal unemployment.*

Bob Gregory is Professor Emeritus at the Australian National University, and one of the most influential shapers of Australian economic policy in the last generation. He was elected Fellow of the Academy of Social Sciences in 1979, awarded the Order of Australia Medal in 1996, and made a Distinguished Fellow of the Economic Society of Australia in 2001. He was interviewed in his Canberra home in June 2007.

**WC:** *Let’s begin with your childhood. I’ve read the tribute in the Economic Record (Chapman 2002) and I’ve read the interview recorded at the National Library of Australia (Moyle 2002), and there’s some dissonance between the two accounts. The picture which we received of your childhood in the Economic Record is that you were, to use the phrase deployed, ‘lower middle class’. But, in the interview at the National Library you recall of your childhood that your father ‘made a reasonable sum of money, was reasonably rich at the time’. Isn’t there a dissonance there?*

**BG:** Yes. I need to be more precise. My situation was not straightforward in that I was neither well-off nor poor. I will start with my father’s background. My father left school at 14, as did all members of the family. My father’s family, when he was young, was much poorer than my family when I was young. He had grown up in a wood-yard in Brunswick. The family delivered wood in the winter and ice in the summer. There were at least two horses stabled in a normal suburban backyard. You can imagine the mud, flies, horse manure and so on. With this background Dad had no access to capital when he left school.

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Within a year of leaving school Dad had started his own business with a suitcase on the front of a bicycle. It was in 1931. He brought books to people's homes, the woman paid sixpence a week, then he came back and changed the books the next week. He was a travelling library. After a while, he began to sell stockings. Stockings were expensive and housewives were looking for ways to get credit to buy them. By the time he was 21, he had made enough money that he owned a small car and his business now extended to all clothing, on credit. By the standards of the '30 he was well off, sufficiently so that he could buy a house in Pascoe Vale when he got married at 25 years of age. Pascoe Vale was the suburb where working-class people who had done reasonably well in Brunswick and North Melbourne would move to. It was the north-west frontier of Melbourne in the late '30s.

Although Dad had a prosperous business, the family had little spare money. Almost all the money went back into the business to provide capital for growth. The major asset of the business was the money people owed. Hence, a good year for business meant increased debtors and shortages of capital. Dad was asset rich but income poor. For handkerchiefs, for example, I used shirts cut up. But when Christmas came, if I wanted a football, I was given one. We had a phone; there was a time when that was the only phone among the neighbours. (We had the phone because Dad needed it for business). So, if you counted the family assets my father was doing well but we lived frugally, very much the same as everyone else in the neighbourhood. When we had lamb once a week, apart from chops, we bought 'two tooth'.

**WC:** *What's 'two tooth'?*

**BG:** Two tooth is a one-year-old lamb. It has two teeth and is rather tough. The leg of lamb lasted Sunday dinner, Monday dinner and Tuesday dinner. Sunday we ate the roast. Monday we ate the cold lamb (maybe two or three thin slices each) and Tuesday we ate the hash (the leftover lamb cut up and fried/boiled with potato and carrots). Nowadays, a household of that size might eat one leg in one sitting. We were frugal. I can still remember that the slices were too thin and there was never enough for me. One of the questions social scientists often ask of the poor in surveys is, 'Could you quickly raise a thousand dollars if you had to?' Well, we could do that. We lived frugally, but we were not poor.

**WC:** *Can you articulate the attitudes of the household?*

**BG:** I think our household attitudes were similar to all the families in the street. The prevailing attitudes of the neighbourhood were not those that you would find in a very poor area. Everybody belonged to a married-couple family with 2.3 children, there were no alcoholics to my knowledge, no one got shot, no robberies (although we were robbed once), no domestic violence. It was somewhere between a working-class and a middle-class neighbourhood. There

was no such thing as 'a tradesman's entrance' which I have seen used as a definition of middle-class housing in the eastern suburbs of Melbourne.

Everybody in my street, Royal Parade, thought that the right thing to do was to keep their children in school past 14 years of age. Everyone was very keen on education and very influenced by the Depression years. Everybody thought of themselves as upwardly mobile (through their children) but no-one thought of sending their children to university; although many thought of the schoolteacher option.

Neither parent was ambitious for me, in that I was not excessively encouraged to succeed. Dad never mentioned careers to me, and Mum only wanted me to be happy. I guess the most important thing was to get married to a nice girl, have children, keep the marriage together and remain close to the family. Family was very important. As far as I know, my parents did not have close friends outside of the family, with perhaps one or two exceptions. And, in any event, their friends never visited the house for dinner.

My mother was always home and never worked in the labour market after marriage. This was true of all the women in the street. She was always there for me. My father got drafted in '42. So I was brought up during my first three to seven years by two women; my mother and my mother's step-sister. One of my war memories from that time was that Mother used to threaten my sister and me that, if we didn't behave, she would run off with a Yank. I guess that shows how old my mother was, what people were thinking about and how much impact the Americans and their money was having in Australia. Running off with a Yank was a very common phrase. And then, one night a Yank arrived home. He gave me an American Air Force hat, and popcorn to cook, which I'd never seen before. Corn popping in a dark kitchen with a wood stove can be very exciting. The Yank ended up marrying a friend of my aunt's (she had brought him home). There were no plans for running away by my mother and I didn't really feel threatened or on the verge of abandonment.

**WC:** *Was it a family in which politics was important?*

**BG:** Oh, no, no. We never discussed politics. That was a no-go area. The only one time I can ever remember hearing politics discussed was when the Viet Nam war was on and my sister was for the war. I knew that there were two parties — Liberals and Labor (bosses and workers) — but that was about it. The other no-go area was religion. There was a big divide between Catholics and Protestants that was rarely talked about except that they should not marry each other.

**WC:** *Is there any reflection that you want to make on the contrast between being 10 years old in the late 1940s, and being 10 years old today?*

**BG:** In Royal Parade, when I was 10 years old, every family owned their own house, all men and young people were employed, every mother stayed home

and looked after the kids, the diet was identical in all households, and everyone had been born in Australia or the UK. So I sort of thought that everybody in Australia was much the same. Indeed, before 18 years of age, I thought the street represented all Australia and that the richer and poorer people in the street represented the range of Australian experiences as a whole. I had never seen a rich neighbourhood — a Toorak, for example — until I was 20 years old. I can even remember the day. I met people who were poorer, because of the wood-yard in Brunswick: but I can't remember meeting more than one or two 'non-Anglos' until I was a teenager. The person who was most different from me in the neighbourhood looked exactly like me, but was a Catholic and hence went to a different school and had to marry a Catholic. It was a remarkably homogenous neighbourhood and my belief, at the time, that the street spanned the broad fabric of Australia shows how homogenous neighbourhoods were and how children did not travel much within a city. There was a very high degree of homogeneity.

Does that mean everyone was extremely secure and not frightened of change or differences? Not at all. I believe in that society everyone tried to create and maintain homogeneity. The desire for homogeneity was very strong. I could not go to a family party and drink sherry, for example, because that would set me apart because everyone drank beer. I would be seen to be trying to 'put on airs'. Looking back, the forces for homogeneity seemed overwhelming, although I thought the situation was normal. I suppose it was part of a class system, although no-one thought of it as that.

The first time in my life I started to become aware of heterogeneity in society was when I was at university. Some of the university students I knew went to India for the summer. I could not imagine doing that. Why would they want to leave Australia? Where did they get the money? Everything you want is here: a nice garden, a car to wash, children to raise, books to read, football to go to; so why would anyone want to go anywhere else? Indeed, I did not really want to go overseas to do a PhD. I've changed completely since that time and now I am always travelling and actively seeking out heterogeneity, and there are more people like me today. Homogeneity is now more or less regarded as boring by a fairly significant number of people.

The other big difference between then and now is the position of children. When I was young the house was the adult castle and almost forbidden to children. Neighbourhood children were not allowed in your house and even the family's own children were kept out during daylight hours. I never went into anybody's house. No child came into my house. You would stand at somebody's back door and yell out, 'Can Billy come out to play?' So that's changed too, in my house today children come and go all the time. Kids sleep over. I never slept

over in my childhood and I certainly did not want to. Today, strangers go to the refrigerator for food. I could not directly access food when I was young.

**WC:** *Is that just 'kids' liberation', or is there something else going on?*

**BG:** It's partly related to income. Possessions in the house were important and kids might break things or jump on lounges or sit on chairs. We had two of the four rooms in our house where children were not allowed to go unaccompanied — the dining room and the lounge. These rooms were kept for visitors who might come perhaps once a week. They would eat in the dining room, where there would be a gas fire. Good pieces of cutlery and crockery would come out of closed drawers for entertaining. Then, after the dinner, the doors would close until the next time, perhaps Sunday week. Any special possessions the family had, like nice furniture or glass displays, were always hidden away in these rooms and never seen until guests arrived. It is weird that so much space in a small house was rarely used.

The house was also very dark and I would not want to be inside anyway. In a family of three children there would usually be two small bedrooms and the only space was in the kitchen with Mum and to be there was not a good idea. The kitchen was tiny, and the family lived in the kitchen. Mum prepared meals there and she did not want the kids under her feet. It is entirely different today. Children share all rooms at almost all times.

I guess one other difference was that the house was very regimented, again perhaps because it was small. At any hour of the day you could predict what was happening and where everybody would be. I had the same breakfast every day at the same time, went to school, ate dinner at six o'clock on the dot, was into bed at half-past seven, had a set weekly dinner menu. The only entertainment was listening to the wireless. When we were at the table at dinner time there was very little discussion at all. The radio dominated. My father would read the newspaper.

**BG:** *What newspaper was it?*

**BG:** The *Herald*. And he was quite keen on reading newspapers. I think my father was a very intelligent man, certainly a very perceptive person, but, he did not talk much and we never really had a long and serious conversation (by the way, I cannot remember my father's father ever speaking to me. Silence ran in the family). My father worked on his business at night and I cannot ever remember a serious discussion at the dinner table. Every member of the family sort of lived their own life, or that was my impression. My family was extremely happy. I cannot remember my parents fighting. Indeed, it took me a long time, even as a young adult, to distinguish between fighting and an intellectual argument. In my family a vigorous discussion was a fight, and not an intellectual argument. If you tried to start an intellectual discussion you were being difficult

and very quickly the subject was changed or people drifted off. I think of my family home as a silent place in which no-one had a conversation except to say, 'What happened at school today?' I would answer 'nothing much'.

I was a very keen reader. Dad and I would compete for the paper. The rest of the family could not get a look in. There were no books (novels) in the house, but as I said before, anything I asked for I got. The *Herald* published books each six months or so with titles such as *Animals of the World*, the *History of Australia*, *Everybody's Encyclopaedia* and so on. I would say 'I want this book advertised in the *Herald*', and Dad was happy to go to the *Herald* office in town to get the damn thing. Now, Dad was a very busy business man; he had his customers to look after. But I wanted these books so he had to go and buy them. And I would read the books over and over again. I knew a lot about animals. I read comics in great numbers. (I was heavily into swapping comics and this was thought to be unhealthy — 'you don't know where they have been'.) I started reading novels and other things when I went to High School and could access the public library. I read strange things like the *Best American Plays of the Fifties*, *The Best of American Humour*, Tennessee Williams.

**WC:** *One event in your sort of youth which I'd like to talk about is that at the age of 14 you contracted polio. You said in the National Library interview: 'My own view is that polio explains where I am now.' You said that, but it wasn't explained.*

**BG:** When I was 13 I went to a special high school. In those days the schools were graded. There were only half-a-dozen high schools in Melbourne. (When I think back, this is outrageous: only half-a-dozen high schools for all Melbourne!) I was the ideal little boy in the sense that I was captain of the school football team, house captain, played the piano, big in athletics, great on the street, and came in about twelfth in the class rankings; a true all-rounder. I was keen on school work, paid attention and competed, but I only studied at school, never at home. Never studied for exams and did not do homework.

One day, in April, I was training for football on a Tuesday and I began to feel stiff and I had to go home. The next day I had to leave school and go to bed. The doctor came and said to Mum, 'He's either got the flu or polio'. Polio was a very bad thing. People died or might be paralysed for life. It attacked lots of children. By Friday my leg wasn't better, so I went to hospital. I felt fine (apart from flu symptoms) and was optimistic. In bed you don't know you can't walk. It was only after 14 days when they got me out of bed that I discovered that I could not walk. Then I spent nine months in bed. They strap you to an iron frame, your feet are in plaster casts and then your parents take you out of the frame twice a day and exercise you for half an hour. So my father, before and after a hard day's work, had to exercise me. He could move my affected foot but I could not. It remained still. Some days I would say, 'Oh I think I can move

a toe or I think I can feel something' but I couldn't really. It must have been heartbreaking for them but not so bad for me.

My parents were trying to get me up and out of bed by Christmas. So two weeks before Christmas I got up walked 10 feet. The next day I walked 20 feet. The next day a hundred feet, and so on.

**WC:** *This was a breakthrough for you.*

**BG:** Yes. I could always walk a bit but they wouldn't let me. I was well behaved and never broke the rules. When school started I was allowed to go for half a day. I wore a calliper on one leg and I was allowed to stand at the back of the class. The doctors did not want me to sit down. I had missed one whole year of school and had gone up a class but was not worried. So, I stood at the back of the class and in came the maths teacher. I couldn't understand a word he was saying. I felt sick with the realisation that it may not be that easy to catch up the missed year. I was worried because I wanted to stay in the class with my mates.

So, I came home every afternoon and started working by myself. I couldn't play sport, couldn't do any of those things that I used to do, so I had time and I started studying seriously for the first time. Within four months, I was top of the class. I had never had this success before. But once on the work/academic treadmill, and achieving success, it was hard to get off and here I am now.

**WC:** *So it's a relatively simple story: polio took you away from the football field. Is that it?*

**BG:** I think it's a bit more than that. To be intellectually successful you must be mature, unless you're one of those really brilliant kids. You have to be able to find your way around the disciplines by yourself. I was naturally mature but the polio experience increased my rate of growth of maturity. If I hadn't got polio, my best guess is I would have gone to university, I would have done fine. But I wouldn't have done well enough to become an academic.

Before university, we were told that we will all fail because we will not do enough work, we will be diverted into bars, clubs and so. So the day I arrived at university I go to the library at nine o'clock and I sit there. It's not that easy since I have no idea what to do. I just sit there and figure out that if I wait something will happen. Every day I go at nine, leave at five-thirty, read books read lecture notes and so on. On Fridays I stay home so I could rearrange all my notes; put little red dots against things I couldn't remember. And, at the end of the first year I topped my classes, three out of four. Even today I am amazed at how I got there. I probably knew as much as the lecturer as to what would be on the exam and so on.

**WC:** *Let's talk a little bit more about Melbourne University. You are doing a Bachelor of Commerce.*

**BG:** Yes, well it turns out I only had two choices: I could do law or commerce; I couldn't do an arts degree. Nobody told me that to do arts I needed a language, and I did not have one. And law took four years, when commerce took three, so why would I do law? Also, I didn't know what you did with a law degree. I was not unhappy about doing commerce because in the back of my mind I had decided at high school that the best life was to be a teacher or, failing that, I could be an accountant (I thought accountancy was the way into top management in a big company!!). My dad thought accountancy was good insurance and I did too. At the end of the first year, it suddenly dawned on me that if I continued to do well I could be a university academic. Once I realized this I devoted all my energy to getting good grades. I thought that to be a university teacher was heaven on earth. And I still think so. I still can't understand why my best students don't take the academic option. It is so wonderful to do what you like, not be bossed around, learn things and so on.

**WC:** *And how did you find economics?*

**BG:** I loved it. Some of it was silly stuff really, except for the macro, but I loved it. I liked the logic, I liked the diagrams and I felt that I was learning about secrets of how the world really works.

**WC:** *The syllabus was silly?*

**BG:** Well, we did some silly stuff like 'what is a co-operative?' I can't believe this now. There were all sorts of silly things in the micro area but there were good things too. I didn't know maths. I used to spend weeks trying to work out why if marginal revenue is above average revenue average revenue rises. And then if marginal revenue is falling, how come that doesn't tell you that average revenue is falling? What is an elasticity? I spent so much time thinking about these little things which should have been obvious. I was very good at geometry, so I loved shading in little triangles, although I never really believed in consumer surplus. The lecturers were very competent but rather dull, with notable exceptions.

**WC:** *Were there some good lecturers?*

**BG:** There was one person that I came into a lot of contact with who was clearly an exceptional academic role model who loved economics and a great teacher. That was Max Corden. Max was clear when he explained things. Max knows what he knows and knows what he doesn't know and makes no attempt to hide it. And that impresses a young serious student. Max, at that time, was my ideal of an academic. He also generated the feeling that you could do as well as he did if you worked a little bit more. That helps a lot. If I was taught by someone who appeared to be a genius, and I could not imagine doing as well, then I would give up. What's the point? Max used no notes. He would do his economics in a way which looked as though he was discovering it for the first time. He was the



first person I met who clearly thought of economics as a whole and thought it was the most important thing in his life. He has had a tremendous influence on me. There were other impressive people — Richard Downing, Joe Isaac — but they did not affect me like Max did.

**WC:** *How do you end up at the LSE rather than anywhere else?*

**BG:** First, I did not want to go to America and do course work. And I could not see how my wife would like America. She did not want to leave Australia or travel, and only did because of me. So I thought England was the best place — that meant LSE, Oxford or Cambridge. I was the best student, number one or thereabout in Australia, so my problem was that the [Commonwealth] Scholarship people may have wanted to send me to Oxford or Cambridge. But I was not going to go to snobby places like that: I had heard that they would not let students walk on the lawn. And Melbourne had had a number of really good tutors, good people who had come back from Oxford and Cambridge without finishing their doctorate, so I was a little scared as well. I just thought they were not very good places.

**WC:** *To come back without a doctorate?*

**BG:** Yes. There were quite a lot of people who came back without finishing. And you didn't have to be too smart to figure it out. They were good honest workers, so there must be something wrong with the place they went to. Others had returned from LSE with degrees, which they often got within two years — Dick Snape and Roy Webb were two who were just in front of me. So I went to the LSE to do international trade and to get close to Lipsey, who was quite a young giant in those days.

I thought I was very well trained but when I get there I discovered that I was not. That came as a bit of a shock. I volunteered for the first seminar on demand theory (I knew Hicks's *Value and Capital* backwards and I was sure I knew it better than anyone in the class). The lecturer said: 'You have to contrast, Marshall, Hicks and Samuelson. Also discuss the Slutsky effect.' I said 'Who's Slutsky?' And what had Samuelson got to do with demand theory? (I had never heard of revealed preference). Also, I didn't realise that 'Marshall' was not actually Marshall. 'Marshall' was code for a particular specification of the utility function and demand curve. I had read Marshall and his Appendices in great detail and he seemed pretty clear to me. So I had a huge brawl with the lecturer who kept saying Marshall's demand theory was something different from what I had read in the *Principles*. I accused him of not having read Marshall. It was funny. So, the professor is saying 'That's not Marshall' and I'm saying 'Well, yes it is'. I felt a little disappointed in my background at that point and felt that Melbourne was not up to date and had let me down. I don't think that was fair of me though because some of the class, visiting LSE for a year, had done the US PhD coursework program and naturally they knew a little more of modern

mathematical economics than I did (or, given the student composition, than you could teach at Melbourne).

**WC:** *In the interview at the National Library, you recall:*

Popper said to the class ‘What is the data? Where is the data?’ he said. ‘See! You don’t know, because you don’t know how to use theory to guide you’. I was so angry, I wanted to jump up and say to him, ‘What is a theory? Where is a theory? See, you haven’t got any data to know what to theorize about.’

*What was all this about?*

**BG:** At the LSE I begin to move quickly away from the style of economics I had been taught at Melbourne and become intensely interested in trying to discover how the world works by looking at data. I came to believe quite quickly that I would rather trust data than an academic thinker who had spent their life in the ivory tower. So I went to Popper’s lectures as part of trying to come to grips with what I thought economics should be. The way I like to think about economics is that it is silly to try and separate data and theory, as though one comes before the other. You need both, more or less simultaneously. So I was disappointed in some of Popper and his cheap debating tricks. I feel even stronger today that this part of Popper — ‘theory first, then data, and good economics is about testing theory’ — is not really that useful. It elevates theory to a level that it does not deserve. I prefer something like the following: Let’s try and figure out the world by looking at data with the minimum of theory and then, after we get a good idea of what is going on out there, try and explain it. Few people work this way. In fact, hardly any.

**WC:** *But the data is in your head. It’s a construct, right?*

**BG:** Well, it is and it isn’t. If you want to have an intellectual philosophical argument about methodology with me then I am sure you will win and I will lose. But the argument should be about how to make progress in economics. I just think, especially for me, that ‘theory first’ and ‘facts are just constructs’ is not the right way to think about economics as a working discipline. I feel quite strongly that it is a very bad way to think about economics. I came from a Depression background; I never experienced it, but it had a huge impact on me. I wasn’t interested in economics as a philosophy, or a set of abstract ideas. For me, the ideas had to have relevance and they have to be about something that is obviously important for people lives. I have always become angry at theories of the Depression, for example, which stress the supply side of the labour market. No looking at the facts supports that position.

For me the data sorts out what is important and what is not. I still hold this view today. I always start my research with the minimum of theory and with only the vaguest of idea of what I am looking for, except that I have to believe

that the search, when finished, will lead to important results and that practical men will see that it is important.

**WC:** *Hang on: surely it is the theory that tells you what's important and what's not important. The data tells me that Australia's current account deficit is 7 per cent of the GDP. Theory tells me whether that is important, or unimportant.*

**BG:** No. There are many theories of the current account, and each has been fashionable at different times, and their popularity was based on fashion and not the facts. To work out what is important in explaining the balance of payments you need to look at the data. When the fashionable theory of the current account balance was monetary, a theory economist used to argue for near-instant adjustment of the current account if the money supply was changed. Similarly, when twin deficits was popular as a theory, economists argued that to change the government budget balance would change the current account. The data reveal that this is a very silly idea.

Let me try to give you an example of what I mean. Here is the latest issue of the *New York Times Review of Books* [see Kristof 2007]. The most interesting article in this issue is on Banerjee and his co-editors. They address the question, 'How do the Poor Live?' They have 30 big cross-section data samples across countries, and they take a dollar a day as the poverty line and look at what people below a dollar a day are doing: how much is spent on food; how many children they have; what is their life expectancy; their body mass index; do they borrow money; and so on. There is no explicit sophisticated theory articulated anywhere. There is no worrying about different indices of poverty and how they may be derived from different utility functions. Of course, there is a very crude implicit theory to help them decide what to look at. I find their approach particularly appealing, because it is not driven by textbook theory and not driven by complex theory. At the end of the day, I'd much rather find out how the poor live than spend my time worrying about measuring the adequacy of a dollar a day or worrying about the theory of poverty indexes.

**WC:** *But what is 'the poor'?*

**BG:** This I regard as the wrong question. The poor is anybody living with less than a dollar a day income.

**WC:** *Yes, but why do you call that 'poor'?*

**BG:** Well, almost any low income number will do. You take an income distribution, and draw a line. We can write many, many articles about whether it is a sensible poverty line but that is not really that important. Practical experience shows that where the researchers draw the line will not make a difference to understanding the important question, 'How do the poor live?'

**WC:** *How do you know that?*

**BG:** Good judgement and common sense. I want to know how the poor are living. Worrying about the definition of the poor will lead me away from that question, so I make the call on a dollar a day. Of course, I do a little work looking at a dollar a day to check, but I do not want to get involved in measurement or theory that is not at the centre of the issue that I am looking at. I really do think that there is so much to learn about what is actually happening in society. Remember I said earlier how I grew up in a homogeneous society and thought that my street represented Australia. All the time I want to get a better idea of what the world is like. Isn't this common sense?

**WC:** *Common sense is treacherous isn't it? Your common sense might be very different from the next person's, don't you find?*

**BG:** True, but I feel that too many of us think we know what is going on in the world and we do not look hard enough at the reality. I think academic economists know too little about the world and it is getting worse. Take the latest industrial relations debate, which I feel very uneasy about: people have been ringing me constantly over the last six months or so asking me what the country should do about its industrial relations laws. I feel very inadequate because I have not been able to find a way to collect the facts so that I can make judgements as to what matters and what does not. I have always felt, and I still feel increasingly strongly, that the hardest thing to know is what is happening in society.

My son works for the mining industry. He is based in Sydney. He works 14 hours, 16 hours a day, five days a week. At the end of the five days he flies down to Melbourne, spends the weekend on his farm, and Monday he flies back to Sydney. The oil industry pays him a great deal of money. If he does not like his package he renegotiates and more or less gets what he wants. Industrial relations laws are not a part of his life. My stepdaughter works in the hotel industry. She may work 12 hours a day, no breaks, no morning tea, no lunch and no afternoon tea. The contract is for a fixed amount of money, which is worked out as minimum pay for eight hours a day. If she works more than eight hours a day, the marginal pay is zero. She cannot negotiate. She works on a take-it-or-leave basis. She has no power. So if the workplace relations changes are moving Australia towards the world of my stepdaughter then the reforms are a major step backwards. If they are moving the world towards that of my son, they are OK. If they have no effect, then who the hell cares? So, in order to make a judgement I need to figure out how many stepdaughter jobs there are and how many son jobs there are and how the proportions are affected by the reforms. To do this, I have to know the numbers and how they are changing. Theory can't tell me the answers *a priori* and theories about liberty or justice or freedom to negotiate cannot tell me what to do. Incidentally, one of the reasons I feel frustrated is that we do not seem to collect the right numbers in this area.

**WC:** *You mentioned earlier that you were quite dissatisfied with theory.*

**BG:** Yes, I am now. As time has gone by I haven't found new developments and refinements of theories to be very illuminating. I have found increasing my knowledge of data and improving my data-handling skills give me a better rate of return than worrying about new theory, with one or two exceptions. Let me give you an example. Do you know the current unemployment rate in Australia?

**WC:** *Four something per cent.*

**BG:** Suppose it's 4 per cent. Let me ask you a different question. Suppose next week 400 000 jobs are created. What do you think would happen to the unemployment rate?

**WC:** *It would have to fall, wouldn't it?*

**BG:** [Laughing] Not necessarily. Do you know why? It depends on the nature of the jobs created. If they are women's jobs, then the unemployment rate doesn't shift. If they are part-time jobs, again the unemployment rate does not shift. Only when the jobs are male full-time jobs will unemployment fall and then the fall is not one-to-one for each job created. You wouldn't know this complexity by looking at theory. First, you would not focus on male and female jobs and, second, you would not focus on full-or part-time jobs and it is only after looking at the data that you discover that these classifications matter and that they can explain some of the puzzling macro outcomes we observe with unemployment changes.

Let me give you another example. The most influential work I ever did in terms of affecting my views of the labour market and the importance of data was the work on Equal Pay for Women. When I was at the Industry Assistance Commission, we were working on the protection level of textiles. We were going to recommend a substantial reduction in protection. Everybody was worried about what would happen. I said the obvious thing to do was to look at cases where protection has been taken away and see what happens. But we couldn't find any examples. So I asked a different question: Can we find a change in an economic variable that impinges on the textile industry that is similar to taking away protection and see what impact it has? I then discovered that Australia had just increased women's wages by 30 per cent (The Equal Pay Judgments). That's exactly the same as taking away protection for a female-job-intensive industry relative to a male-job-intensive industry. So, I then started to look at what happened. Female employment did not fall very much, despite the 30 per cent wage increase. That affected my views forever on segregation, discrimination, the power of institutions, the importance of wages and the relevance of economic theory because none of the theory focused on any of the crucial issues in this example.

**WC:** *Hang on: you're including female government employment in that data.*

**BG:** The government/private-sector split does not make that much difference. Private-sector employment is a bit more responsive to the wage increase, but not much.

**WC:** *Some people say the sector split matters more.*

**BG:** Look at the data. It doesn't show much difference. So, the low employment response rate to such a large change in real wages shook me up a lot. It turned out, at that time, that there was hardly any substitution between women and other factors of production. As a very rough approximation to reality at that time you could think of the world as follows: women were secretaries or sewing machine operators and men were bosses or metal workers. Substitution was minimal. I had not realised, at that time, how important gender segregation was in the workplace. It was never mentioned in any of the economic courses that I took.

**WC:** *I wouldn't want to let this just drop here. I sometimes wonder if this 'Let the data speak' attitude is not so much 'Let the data speak' as 'Let's substitute a cruder theory for a more sophisticated theory'.*

**BG:** Yes, as I said earlier, there is an emphasis on simple theory but I would not want to call it crude for the purpose to which it is being put. We have to be careful what we mean by 'crude' and 'sophisticated'. So often 'sophisticated' means putting effort into aspects of theory that are not very important for the problem of interest. When empirical results depend on the nature of the utility function, for example, then you know you are being too sophisticated. I may be a bit unusual but I think first-year economics is incredibly powerful.

**WC:** *You say you like supply and demand and yet so many people would think of your research as putting a discount on supply and demand. I mean the whole women's thing in 1973?*

**BG:** It is true that you cannot look at facts without any theory, so when you approach data you need to be a little bit organised. And I do like demand and supply as organizers but that does not mean, at the end of the day, that the best approximation for some problems is that the demand curve is very steep or the supply curve very horizontal. In the women's work, the demand curve is very steep and the supply curve definition becomes very complicated.

**WC:** *Can I return to LSE, and ask about Max Steuer?*

**BG:** Max Steuer had some of the characteristics of Max Corden, but he was primarily interested in trying to put simple theory and empirical facts together. Max didn't know, and didn't care, about sophisticated economic theory. His views are very similar to mine. Whether I got these views from him, or developed them independently, I don't know. He (Reader) and I (student) were always trying to figure out what really mattered, theory and data wise, for any particular

problem. We both had a high degree of agnosticism and wanted to start research with the minimum of complex priors.

Before I went to LSE I used to think that to make progress I would have to know everything about theory and its details. I would go to a seminar and tick off the equations one by one as I figured them out and then I would get stuck between equation three to equation four, for example, and I'd spend my time trying to work it out. I would then miss the whole point of the seminar. I did that for a long time. I would even read the footnotes! But with Max, the seminar would begin and Max would suddenly say: 'I know what you're talking about but that is not the way to do it. What you should be doing ... etc'. He would take us away from the detail and try to get us to focus on the big issue. I was terribly impressed. Max always seemed to know what was important, and what the issues were.

I hate seminars where everybody is into 'back in school mode' and sits there quietly or makes trivial points about things that do not matter. I try to get into the seminar discussion nice and early, so we can all be involved in what should be the big issues. Max was the first person I met that did that. Later, I found that in most of the top US schools, at least in labour economics — Chicago, MIT, Harvard, Princeton — there are people like Max. They never discuss detail, they never discuss technique; they discuss what should be done and whether what is being done is sensible. They assume that the presenter can look after the detail.

The other person at LSE that influenced me was Frank Brechling. Frank believed in working on big applied problems and trying to sort them out. He was not the sort of person who said: 'Oh, let's read all these articles on investment, summarise them and then work out how to add to the literature.' He would say: 'The UK is going through an investment boom; let's look at what we can learn.' He would try and work things out for himself. It was often said about Frank that the technical quality of the paper may be terrible but, gee, it is an interesting paper. He was on the frontier — simple theory and data — but it was his frontier. He taught me a lot. Frank moved to Northwestern in the mid '60s and became chairman. He hired me.

**WC:** *Tell me a little more about Northwestern.*

**BG:** Northwestern is in Chicago. It's a university which as ranked between twentieth to thirtieth and its ranking goes up and down a lot. It's a bit in the shadow of the University of Chicago. Frank was a drinker and a sociable person and would have cocktail parties in his home for the seminar presenters. All the students would come because they were always hungry — they devoured the bread and cheese — and afterwards Frank would take the seminar speaker and me out for dinner. Nobody else wanted to go; everybody was too busy. So in my first year at Northwestern I had dinner with Klein, Kindelberger, Mundell,

Leontieff, Samuelson, all the stars. That was interesting. They all had one thing in common: they were all unbelievably committed to economics. They did nothing else for 24 hours every day. I thought that the big difference between them and me was not so much native brilliance (putting aside Samuelson, of course) but stamina. They could keep focused on a problem forever, without losing interest. I could last about an hour.

I really had a really good time at Northwestern. It was so exciting. Everyone was so professional and hard working. I wrote an article in seven or so weeks, sent it off to the AER; it was instantly accepted, subject to change. The editor loved the empirical work — it was important and simple, all those things I have been arguing for — but he wanted me to put in a theoretical section focused on the monetary theory of the balance of payments ('Ah ha!' you might say). I said, 'No. No way.' So I tried to develop a different framework that fitted the facts better — this was an original paper, not derived from current theoretical models — and Frank helped me. It was a famous paper in international trade at that time — but the first draft was better. I read the paper a decade ago and found that I couldn't follow the theory that I spent so much time putting in.

**WC:** *Why did you come back to Australia?*

**BG:** Melbourne University said 'Come back'. My visa ran out; I thought that I wouldn't make it in the US; and I promised my wife I would return. Melbourne made me a wonderful offer (a reader position with promise of a chair the following year). But I believed that if I returned to Melbourne I would become Chairman, be a professor and that would be the end of me. Bill Phillips had been hired at ANU and he had hired me at LSE and he wrote, "I'm putting together this team of wonderful young people (Turnovsky, Terrell, Byron and more): come and work in full-time research in RSSS.' So I came here but I negotiated a job; one-half research and one-half introducing coursework to the ANU at the graduate level. I would try and move graduate teaching here towards the US system. So I introduced a coursework Master's. I also wanted to get involved in government. I thought that if I came to ANU that would put me into an ideal position for involvement with the public service.

And after two years I was sitting in my room in the ANU, and I got a phone call. The guy said, 'Alf Rattigan here. I want you to come over and talk to me.' I said, 'I can't, I'm too busy.' He said, 'Oh. Well when can you come?' I said, 'After work, if you've got time.' He said, 'I'll send a car.' I thought, 'What is this — a car?' I had no idea who Rattigan was, but if he was sending a car he must be important. Rattigan offered me a job at the Tariff Board, as head of the research division, which paid about 20 grand more than a professor at ANU. I said, 'I would quite like that but I can't really leave my university. I do not have tenure.' He said, 'I'll fix it; I'll ring Jack.' Of course, I didn't know who Jack was.



**WC:** *Jack?*

**BG:** Jack Crawford [the Vice Chancellor of ANU]. Next morning, Jack Crawford rings me up, and asks me to come over and says 'Alf Rattigan wants you; you must go. Don't worry about tenure.' So I go to the Tariff Board. That was another defining moment of my academic life.

At the Tariff Board I discovered that simple economics, well explained, was even more powerful than I had thought. In general, people don't understand the analysis of policy problems well, but if you can apply simple economics clearly and explain the problem well it can have a very big effect. You can have a huge influence. My time at the Tariff Board changed my whole view about writing and who I should write for. I redirected my work to Australia and to Australian problems and I wrote as simply as possible. This does have some costs. I've written very good papers, but it is hard to publish internationally when the problem is Australian and the theory and technique is a bit simple by journal standards. Foreign-journal editors loved the equal-pay paper but in the end said it was too simple. My guess is that I would have had trouble with the first hysteresis paper too, except that I gave it at an invited conference. Summers and Blanchard took it up and developed the theory more.

**WC:** *Let's talk about that paper you wrote in 1976: the Gregory Thesis and all that.*

**BG:** This was the first 'booming sector' paper (or, at least, I developed it independently) and, like the first hysteresis paper, it was drawn from Australian experience. I got the idea from being in the public service. It was incredible luck and good timing. The big idea in my mind was not so much the booming sector but the methodology which no-one else had used. The methodology goes like this. If you want to know the effect of B on A and you can't see any variation of B, then look for a C that varies and affects A in much the same way that B would do if it varied. Then, if you can put the variations in C into variations in B equivalents, you are home. I hope that is clear. I really think this way of thinking about things was neat.

I was working on the possible effect of a 25 per cent tariff cut. But we had never seen an across-the-board tariff cut, so we did not really know how it would affect the economy. At the same time, the exchange rate was changing. Then I thought to myself, 'Well, an exchange-rate change is exactly the same as the import tariff change on an import-competing industry in the short run. So maybe I can use the exchange-rate experience to tell me about the potential tariff experience.' But the exchange-rate change can be a monetary phenomenon and that was not what I was focusing on. I needed a real exchange-rate change to give the idea more credibility. The rapid increases in mineral exports were generating a real exchange-rate change and I decided to link that to the tariff change. I worked the theory and numbers out fairly quickly, but I couldn't figure out how to sell this idea, in a simple way. I worked for a year and a half

trying to find a way to sell it. I had tradable, and non-tradable sectors and goodness knows what else in the model but I was struggling to make it clear and simple. One day I went to a seminar by Max Corden at the Treasury, and then Max suddenly said, 'If I assume that the terms of trade are fixed, I can place exports and imports along the same axis.' And as soon as he said that I could see how to present my ideas.

The paper had an enormous effect. It was talked about in universities, parliament, newspapers, everywhere. People loved the paper. I was living in Northwestern, I got phone call after phone call from the press. They wrote many articles, drew two big cartoons of me in the *Weekend Australian*, drawn from a passport photograph. I was glad I was away.

**WC:** *The story sold itself, do you think?*

**BG:** Yes, to a large extent. The timing was good, the paper was simple, but what helped in parliament and the press was a politician from South Australia, Chris Hurford, who said that the Gregory thesis was the greatest idea since Keynes. And the reason it resonated was that manufacturing was going under and no-one seemed to know what was going on; and my paper suddenly made it all clear. Everybody loved it. Everybody could use the story. At this stage I was not as confident a personality, and I was not used to being a public figure. I was glad I was away. And that experience changed my life because it built up my confidence in the public arena. The idea spread overseas and was taken up by others but renamed — 'the Dutch disease' or 'the booming-export sector problem'.

**WC:** *In 1982 you gave a lecture in formal circumstances with the title 'The Slide into Mass Unemployment'. Reading it now, 25 years later, I'm also struck by your description of what we would call 'enterprise bargaining' as, quote, 'an extremely radical proposal ... Such a proposal would be seen to be an attack on the very raison d'être of unions, which is to change the balance of power ...'*

**BG:** Did I say that? '*raison d'être*'?! I'm amazed; somebody must have put that in my speech.

**WC:** *'... between employer and employee by bringing pressure outside.'*

**BG:** The purpose of that paper was to develop the idea of hysteresis in the labour market and to explain why unemployment may not impact as much on wage levels as theory might suggest. I did talk about implicit contracts between firms and their workers and the effective freezing out of outsiders. I was making a case for an Accord process to set wages so that outsiders could be brought into employment and their wage interests would be implemented by the centralized wage-fixing authority.

Between 1973 and 1975, award wages increased dramatically. So, after the wages boom and high unemployment set in, the question was: what to do? Fraser went back to reinforce a centralised wage-setting system, which I more or less

approved of. The idea was that the centralised system could hold nominal wage increases to a much lower level during an expansion because the promise of indexation by the centralized wage-fixing authority would stop unions from seeking excessive nominal wage increases. The centralized wage system was to freeze average real wages. Then within three years the average wage level would be the same that would have been predicted on the basis of past trends. That real wage level should restore full employment as productivity increased during the interim.

But, for some reason, around the world, and in Australia, productivity growth slowed up dramatically. So projecting the required full-employment real wage on the basis of past trends turned out to be incredibly wrong. Indeed, during this period the real wage–productivity nexus theory of employment turned out not to be very helpful as a guide to policy.

**WC:** *We don't have centralised wage setting at all, now. Is that a good thing? Or was centralised okay for its time? Or was it a mistake?*

**BG:** I don't think centralisation was a mistake; I don't see how it could be. We have a fairly equal wage distribution and also we have equal pay for women. Both these outcomes were delivered by the centralised wage system.

**WC:** *But women's pay was unequal for 60 years under a centralised system.*

**BG:** That's correct. Centralisation is not sufficient for particular outcomes. But it is a policy instrument that can be used if the will is there. Fraser more or less kept the centralised system, as did Hawke for most of the '80s.

My interpretation of history is that towards the end of the Accord during the late 1980s the unions began to destroy the centralised wage system. I still do not know why a sensible union movement would do this. The union leaders said that getting rid of centralisation was about creating an efficient labour market, which would be better suited by enterprise bargaining. It is certainly true that union officials had little to do under the Accord and the stronger unions had become unhappy with it. They found themselves in the situation that they could not respond to worker demands for wage increases. In the long run, therefore, the Accord process destroyed much of the power of the union movement; it destroyed the grass-root relationships between the local union official and workers. The trade union leadership knew this, but was confused. The leadership liked the power of being near the centre of government, and having a centralised wage-fixing Accord process delivered that, but it also knew that the Accord was destroying the grass roots of the union movement.

Eventually, Kelty and Keating set about destroying the centralisation system. I was quite shocked, because if you look at the union rhetoric of enterprise bargaining it is the same rhetoric used by General Motors Holden; it's the rhetoric of big companies. The rhetoric says that the unions and the bosses will get

together and sort out what goes on in the company. To anyone who works in a small retail store or a small business, the workers and the bosses do not get together. In small companies, the workers have no power. So the unions were giving away their coverage that was delivered by the centralised system.

**WC:** *What used to happen under the centralised system?*

**BG:** With a centralised system, wages are more or less delivered to all workers once a year, whether they are union members or not — the wage goes up for every one. My father used to have small shop — two employees — and everybody got their wage increases from the award.

**WC:** *And nowadays he would negotiate?*

**BG:** No, he wouldn't negotiate. He would just set the wage and only adjust when it became too out of kilter.

**WC:** *So the upshot is that enterprise bargaining only works for General Motors. There is no bargaining at the enterprise level for small enterprises?*

**BG:** Most people know that. The unions know that. If you have a child who works in a small retail store you know that. Many of these small retailers don't pay the kids for the first two weeks in the job. They claim, after the event, that this period is training; then, after two weeks, they let many of the new workers go. If anyone complains to the unions, the unions say 'Too bad, what can we do? We can go down there and sort this out on Monday but there's 400 of these complaints a week and, in any event, next week the employer is back to his old tricks.'

**WC:** *I want to clarify things; the Accord was bad for the unions because it destroyed their grass roots?*

**BG:** Yes, in the long run.

**WC:** *But enterprise bargaining is also bad for the unions, also because it destroys their grass roots?*

**BG:** Not quite. Enterprise bargaining destroys the coverage. If you are worried about a contradiction you need to realise that centralised wage fixing is not the same as an Accord. Centralised wage fixing had much more flexibility than an Accord process, which is one extreme example of how centralised wage fixing might work. Without a centralised wage system the natural state for unions is to be small and to be primarily located in large companies. Remember that under the Australian centralised system we were all *de facto* union members in that any wage agreement was delivered to us all without having to be union members. The centralised system magnified the power of the union and that is why I could not understand why the unions would want to give it up.

There's no going back now and that has worried me a little. Some of the advantages of the centralised system can be delivered by the state. It could

regulate the number of weeks holiday, the length of a standard work week, maternity leave, and so on. But historically the state has not done as well as the centralised wage system in delivering good outcomes for workers. In the US, for example, many workers receive no holidays in their first year of work and then from the second year they get two weeks. Of course, in the US they have never heard of long-service leave.

**WC:** *Why are you so pessimistic about the role of the state?*

**BG:** The state in Australia will tend to let minimum wages erode towards OECD averages in most variables. Look at what Howard tried to do. He was saying that freedom was the right to trade away holidays as if this trade-off was a) based on equal power between employer and employee and b) could easily be traded back again.

**WC:** *Can we talk about your relationship to the Hawke government?*

**BG:** I have never been closely involved in the political process. I have always thought of myself, in what I would call a sweetly naïve way, as a disinterested academic who tries to help out by explaining policy issues. So I try to explain policy options to think about, rather than play a strong advocacy role. People like my work, so I receive lots of offers to become involved. I was lucky enough to be on the outskirts of the Hawke government from the beginning. I was offered a job in the Prime Minister's department.

**WC:** *Did you accept the position?*

**BG:** Yes, but just for two days a week. It wasn't a great success because I was too slow and I do not think you can work in the PM's department part-time. I made a mess with the first budget. And this is a really fun story. The Prime Minister's department had done some work which showed that the employment and budget projections were far too optimistic. There seemed to be no way that employment could grow at the rate that the PM promised. As a result, there was no way the budget forecasts could be met. Hence, taxes might have to be increased, or at least not reduced. The Prime Minister's department had tried to explain this but the Treasury — Keating — took the opposite line and asserted that there was no problem. The PM's people said to me: 'We tried to tell the Prime Minister and he will not listen: you have to go and see him; he will listen to you.' This was a very dangerous thing for me to do but I said, 'Fine, since it doesn't matter if I lose my job.' So I arrive in the PM's office and Hawke is pulling his ear, and he's beautifully dressed. He was just like the cartoons they used to draw of him. I say: 'Prime Minister, I don't think you really understand what's going on.' He doesn't seem to be interested and then all of sudden Keating bursts in and abuses me. The public servants from the PM's department stood there in absolute silence, and yet they had sent me in to fight their battle. Anyway, I get back to the office and the head of PM's department calls me in

and says: 'The Treasurer has demanded that you be sacked, and I've been chastised for giving you access to preliminary budget papers.' So I said: 'Well, first of all I haven't done anything wrong. Second, I don't care whether I'm sacked or not.' He said: 'Well, I'm not going to be pushed around by Keating.' So I stayed. Anyway, after the event my forecasts were wrong and Keating's were right. Within a month or two I had left for the Australian Chair at Harvard.

One year later, after I returned from Harvard, I was sitting in my office, and I suddenly got a phone call from Keating. Will I come and have lunch with him at Manuka? Sure! I figure that he was going to offer me the Statisticians' job [at the ABS], which was open. I rather liked this idea but I didn't really want to leave ANU, so I spent all morning trying to figure out should I say 'Yes, for three years' or 'Could I do it part time?' or if I could parley this job into a new job of statistician's advisor, which I could do part time, and so on. So I go to lunch and Keating says to me, 'Why aren't you doing more for the Labor government?' I said, 'Nobody has asked me to do anything.' He said: 'Oh, well would you like to be on the Board of the Reserve Bank?' I instantly said 'Yes.' He said: 'Don't you want to hear anything about it?' I said: 'No; I will take it.' He'd obviously forgotten about the other episode I mentioned earlier. Or else he may have forgiven me.

**WC:** *Tell me about the Reserve Bank Board meetings. Is there genuine discussion and debate at these meetings?*

**BG:** Well there are many answers to this question; one is what the discussion was like for me, and another is how the discussions affected the outcome. As a Board member the discussions and supporting papers were just wonderful. The bank staff members were right on top of things. In academia we do not have the resource support to compete with them. They are producing papers from a department of maybe 20 research economists; three or four may have a PhD, and another four or five may be on their way to one, and the Board submissions is more or less all they do. It is great.

The Board members, however, are a mixture. The businessmen are good at understanding what is going on in their part of the economy but they know little monetary economics. And that can be a bit of a problem for the discussions. I once asked in a meeting, after I managed to get some forecasts, 'What's the inflation figure? Is that the CPI or the GDP deflator?' That generated absolute chaos and showed very bad judgement on my part. One of the Board members said, 'What's the GDP deflator?' Well, 25 minutes was spent over trying to explain the GDP deflator and, of course, it was of no importance for any decision we might make. That discussion made it very clear to me that our Bank Board is a representative board to give Australians a feeling of security because of the important people on the board. But the academics think of the board as more of a debating and analytical group and that it is not.

**WC:** *Tell us about the 'Recession we had to have' from the vantage point of the Bank Board.*

**BG:** It was pretty obvious from 1986 that we should start tightening monetary policy, and we were getting ready to. You could feel the need for a tightening, more and more, and then, in October 1987, the stock market crashed and no-one quite knew what was going to happen. So, decisions to tighten were delayed until things became clearer. When we did move, we moved sooner than other central banks. But we were still too late. Asset prices were getting completely out of hand and, strictly speaking, they were not our business; but we were increasingly worrying that the asset-price boom would spread to the labour market, wages would go up and inflation would get out of control. The information we were getting was that a large wage breakout was about to begin, and Bill Kelty felt that the accord would collapse. But wage outcomes in the current data were not that high.

**WC:** *So the suggestion was that in terms of inflation we were on the verge of a 1974-style breakout?*

**BG:** Yes, Bill Kelty kept saying that he personally was preventing wages from bursting out and it was becoming increasingly difficult.

**WC:** *But we ended up in this god-almighty recession. Doesn't it look too tight in retrospect?*

**BG:** Maybe yes and maybe no. It all depends on whether you are prepared to give the recession credit for the low-inflation regime of the last 15 years. Anyway, Chris Higgins and I thought unemployment would increase much more than everyone else — we thought unemployment would increase to about 7 per cent. Others kept saying that real wages had not increased; hence, unemployment would not increase much. This was an application of the real wage overhang model that had been so popular in the mid 1970s. They argued that all that would happen was that tight monetary policy would burst the asset bubble with little real effect on the economy. I should also add that few people knew how bad the situation was to become with the private banks. The private banks came to the Board more than once as monetary policy was being tightened and told us that they saw no problems. They were a long way out in their forecasts.

**WC:** *What was your position?*

**BG:** I supported the interest rate increases, especially at the beginning of the upswing in rates, but I wanted to ease earlier than we did. As we got into the recession I could how see deep it was going to be, but I suppose by the time I was really worried others could also begin to see problems. So when should we have eased? Bernie Fraser was very slow at easing. His view was that it was clear that the economy was going to suffer in terms of output loss but let's make sure

that it is all worth while, and we get the low inflation we want, and drive inflation out of the system.

**WC:** *So he's an anti-inflation hard man?*

**BG:** [Bernie] Fraser was an anti-inflation hard man during this period, which is interesting because he was also pro growth most of the time and very worried about unemployment. I thought we were too slow in easing up and I wanted to come down in terms of interest rates much more quickly. The others stayed with Bernie and I did not push too hard. But after the event there was a big payoff from the recession and the longer this long boom continues without inflation the better the payoff becomes. The payoff is still accumulating.

**WC:** *How would it be a payoff?*

**BG:** I'm talking about the low inflation payoff. After all, the true object of creating a recession is not to create unemployment for its own sake.

**WC:** *Around about the same time that you were appointed to the Bank, you were appointed to the Institute of Family Studies and you stayed there for 11 years.*

**BG:** Once you're on the Board of the Bank, you get offered all sorts of jobs. I was also on the Australian Science and Technology Council. You learn a great deal from these experiences and coping with problems.

**WC:** *What problems?*

**BG:** Well, one problem is being an economist on a board where no-one else is an economist. Depending on the nature of the board you can very easily become the nasty person.

**WC:** *Why?*

**BG:** Well most of the members of these boards believe in things that economists do not. The Science council was particularly hard. On ASTEC, scientists would argue 'everybody knows that unless we double exports, Australia will not grow at 50 per cent (whatever that means), and we will not lead the world (whatever that means)'. 'Everybody knows that we have to have a space program because unless we do we will only be a nation of farmers.' 'We need to double the number of scientists to promote economic growth', and so on. So the economist becomes the nasty man who argues against all these positions. This is really difficult because you don't like being thought of as a nasty, negative person, especially if you are really a nice person. You also need to choose which battles to fight and which to let go, which is also stressful.

**WC:** *On the Institute of Family Studies web page we read that the purpose of the Institute is to promote the understanding of factors affecting family stability in Australia. I also note in another interview you tell the interviewer that women in Australia are increasingly 'marrying the state'. So I throw that over to you: are women marrying the state? What about family stability in Australia?*



**BG:** I hate the phrase 'marrying the state' but it is sort of true in the sense that for one in five children, most of their income comes direct from the state and through the mother. It is quite an amazing fact. How has this come about? At one extreme, these changes may be largely coming from the fact that so many women can no longer find a suitable male partner that can provide the economic resources for them and the children: so many of the men are unemployed, so many of them have low real wages, and so on. Or it could be that these large changes are coming from the women's movement, the increase in freedom associated with more work in the labour market and the increase of freedom that comes from not having to rely on a male income provider. Large social changes are not easy to analyse in a way that establishes causal relationships.

There are a couple of policy responses. One is to make it as easy as possible for women to get out of bad family situations if they want to, and another is to make it less attractive for women to be on welfare for a long time.

**WC:** *How do you do that?*

**BG:** Well, there are two ways: push and pull. What the government has been doing recently is push. The new policy is to try and restrict access to welfare after the child turns eight and to create an environment where the mother more or less has to go to work in the market place.

**WC:** *Over eight?*

**BG:** If the children are older than eight, the mother can no longer access the sole-parent pension, and she is placed on Newstart and must seek employment. The sole-parent pension has two advantages for the mother: she gets more income per week — maybe \$20 or \$30 — and she keeps more income if she goes to work (the clawback is less than for Newstart).

**WC:** *Will they just decide to be poor?*

**BG:** Many will be poor. The policy balance is not quite right. It should be more positive in developing employment opportunities.

**WC:** *Let's talk about invalid pensions; what can we do about invalid pensions?*

**BG:** I suppose the first point is why has there been such a rapid growth of invalid pensions. My view was that when more focus is placed on enterprise bargaining the firm becomes more productivity conscious and the worst workers are removed. Once their link with employment is broken, they find it difficult to get back into a secure job. So, if the bargaining process is changed and moved to a firm focus, the potential arises for more workers to become disconnected from the labour market. And that, of course, describes exactly what has happened over the last few decades. That's why we have so many invalid pensioners and why the number on welfare is so large in Australia.

**WC:** *So this 4.2 per cent unemployment which we presently have is an illusion?*

**BG:** It's a complete illusion. I haven't checked the data recently but last time I checked the ratio of disability pensioners to the workforce was about 7 per cent, whereas in 1975 the proportion would have been about three-quarters of 1 per cent. So either Australians have become incredibly unhealthy, or the Disability Support Pension recipients are the types of people who would have been employed in earlier times. I believe the latter.

**WC:** *Why?*

**BG:** I tried to outline one of the reasons above. Another part of the explanation is the state of macro demand. There was a big economic shock in 1975, which created more unemployment and made it harder to get jobs. Those with some disability, who were previously doing their job well, once unemployed do not look the same. They appear to be less productive to a potential new employer, so the workers find it difficult to get work. The potential worker also adjusts their behaviour, and appears less attractive to employers. Employers become more wary of them because they have not worked for so long. The only solution is the maintenance of a strong macro economy for a long time so that the employers must choose these workers or no-one.

**WC:** *Don't we have a strong macro economy?*

**BG:** Well, we are beginning to. The labour market is starting to become quite strong [in mid-2007], but only in the last 18 months have the welfare-recipient numbers begun to come down. They had been going up for a couple of years. The downward change in welfare numbers is still a bit weak but, if the economic outcome remains stronger, things will improve. And it looks as though the strong economy is going to continue for a little while, although there is considerable uncertainty out there. Perhaps for the first time in 30 years we are going to start making significant inroads into the welfare numbers.

**WC:** *Let's get onto a big issue, Aborigines. And if I could start off just by kindling a conversation by a quote from a recent paper of yours (Gregory 2006) on Aborigines. Quote: 'Indigenous unemployment as measured is extremely low, but if CDEP is set aside there is no evidence that across the board employment prospects are increasing despite large amounts of public expenditure; despite the very significant improvements in indigenous education there has been very little employment growth. The policy seems to have failed spectacularly.'*

**BG:** There are a couple of reasons for this failure. The first reason is that, to a large extent, failure is inevitable. You cannot take adults who can hardly read and write English, who are noticeably different, who cannot be compelled to attend work, who live where there are no jobs, and then spend money on them and expect to fix the problem overnight. The solution will be slow coming and must be concentrated on the young. I, by the way, am very pessimistic about the ability to make fast progress. The changes required in culture, location and

values for good economic outcomes seem extremely large to me and probably too radical to occur quickly.

There's a qualification I should mention. Policy has been succeeding really well for the Indigenous elite, so it is not all doom and gloom. The top 10 per cent of Aborigines, in terms of education, income and exceptional physical or business skills have never had it better. You can see the elite everywhere now in our society. If you said to me: 'I want you to arrange a dinner party with well-educated and influential Aborigines in the next week', I could find you plenty of well-educated, interesting and successful Aborigines. I could not have done that 40 years ago.

**WC:** *But was the problem existing 40 years ago? I mean, agricultural employment existed.*

**BG:** If we go back to the '60s, Aboriginal outcomes were not better than now. Education levels were very much lower; life expectancy was low. But it was true that there was more agricultural employment. A typical remote tribal group might be on a station near a water hole where, once or twice a year, the Aboriginal men would round up the cattle. A couple of women might live in the house and work as maids and the station owner would look after the tribe, pay them in-kind. The Aborigines worked when needed to round up the cattle and there was a sort of economic understanding. But conditions were not that good. In a remote community you cannot have a school; and even if the community was large enough for a school it was unlikely to be a good school unless it was on a mission.

Remoteness is a difficult problem. If the Aborigines stay in remote areas, outcomes will remain poor. If they move, it will be difficult for them for quite some time. Should you move Aborigines to a town camp in, say, Alice Springs where there are schools but no strong community values? I just think that for remote people economic and social failure is largely unavoidable for quite some time. To discuss Aboriginal policy sensibly, you have to talk about degrees of failure and partial success and what worries me a lot about the current initiatives is that they don't really go to the centre of the problem and their advocates seem to believe that the problems can be fixed relatively quickly. The cure for the Aboriginal problem is not sending doctors to provide medical checks or to move in the army or police. The centre of the solution is to develop a policy structure within which Aborigines can be employed. But that will take a long time. It is going to be a slow process — much slower than is implied in public discussion.

I went to Darwin, two years ago, to give a talk. I had bad experiences. The first was that the only employed Aborigines I saw in Darwin were in a craft shop, and they looked like me: not very dark. In the hotels, all the room cleaning, all the kitchen staff, all the low-paid jobs were done by immigrants and backpackers. I went to see a public servant to discuss this. I did not see one

Aboriginal in the public service offices I walked through. I really do believe that we need public-sector employment quotas in the short term — not a very popular idea though.

My second bad experience was not very long ago in an Aboriginal township in Queensland. All the pre-conditions were right. The community didn't look too bad and it was next to a fast-growing and large tourist town. Yet I was told there was only one Aboriginal employed in the town. The Aboriginal community 'owned' a very popular tourist site but they had done little to develop it. When I talked to people about how to develop the site so that they could turn it into more of an economic resource, I got even more depressed. They were talking about closing access to the tourist site on Sunday morning because the traffic was too dangerous.

**WC:** *Too dangerous?*

**BG:** Well, they said that on Saturday night there was considerable drunkenness and members of the community would wander across the road on Sunday mornings and tourists might kill them with their cars.

I visited another community; this one was very remote. You had to fly in by plane. It was on the Queensland coast. They had an offer from Americans to set up a fishing resort. I said: 'The first thing you do is accept the offer and then negotiate. Write good conditions into the contract. For example, write in that the resort has to employ a certain number of community members, and so on.' But the economic development did not ahead. When I asked what had happened, someone on the [land] Council said: 'The beach is my land; it does not belong to the council and I do not want the development.' The Council said: 'That's right, it is her land.' Then I discovered that this was not a community. The people had been moved from an old mission where different groups had been brought together and they found it hard to live together and reach decisions for the common good. It was very depressing as there didn't seem an obvious way out. Many Aboriginal communities are like that.

**WC:** *Thanks for giving me so much time*

**BG:** It was a pleasure. I enjoyed it. I love to talk. But I am aware that in conversation it is not possible to be as clear as I should, or to provide the subtlety of analysis that I should. I hope, though, you can see the spirit of the remarks.

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