

ENTERPRISE BARGAINING AND PRODUCTIVITY

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When the Australian Industrial Relations Commission, in April 1991, refused to introduce a principle for enterprise bargaining, it was sceptical of claims that enterprise bargaining would raise both the level and rate of growth of productivity. An examination of productivity data for the years between 1964-65 and 2010-2010 shows little evidence of any boost to productivity that could be attributed to enterprise bargaining. The trend growth rate after 1991 was less than in the preceding 27 years. There is some evidence of a rise—sometimes characterised as a ‘surge’—in productivity in the later 1990s. Since then, the productivity record has been poor. The suggestion that the ‘surge’ was due to enterprise bargaining has little or no empirical basis. Analysis of productivity at the industry level indicates that different industries had widely different productivity experiences, with little sign that enterprise bargaining was a significant cause of superior performance. The Commission’s scepticism has been vindicated.

A FULL BENCH OF THE AUSTRALIAN INDUSTRIAL RELATIONS commission, of which I was a member, dealt in April 1991 with applications for increased award wages and for the adoption of a wage-fixing principle that would allow for ‘enterprise bargaining’. Notwithstanding the support for some form of enterprise bargaining expressed by most of the parties to the proceedings, the Commission rejected the proposal. In doing so, it noted the superficial character of the parties’ agreement, as evidenced in the diversity of suggested forms that enterprise bargaining should take. The form proposed by the ACTU, for example, would allow for bargaining at the enterprise level for over-award payments related to increased productivity or profitability. Proposals

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by employer groups did not envisage agreements about over-award payments; nor did they contemplate that profitability would be a criterion. The Commission was right to be sceptical about the alleged consensus.

One of the Commission's fears was that enterprise bargaining, especially of the over-award payment variety, would revive the wage break-outs that had bedevilled economic policy in the 1970s and the early 1980s. This fear, it has to be said, has not been realised. The reasons for that lie outside the scope of this paper; but I think that the Commission overestimated the strength of the unions, just as the unions overestimated their own. Another fear was that enterprise bargaining would lead to a less egalitarian wage structure. Whether that fear was justified is an issue that may be pursued in other papers given at this forum.

The Commission was also sceptical about the forecasts of productivity gains emanating from enterprise bargaining. It said:

It was an assumption of many of the submissions that Australia's productivity growth is obstructed by unsatisfactory workplace practices and industrial relations. Despite the emphasis with which this was sometimes asserted, no evidence was presented which would support any assessment of the relative importance of workplace arrangements and other factors affecting productivity growth, such as technological change, product design, markets, the education and training of the labour force and the quality of management. ... Suggestions of a potential for major productivity growth in devolution of industrial relations to the workplace are grounded upon no firm evidence – at least, none that is before us. Steps to be taken at the enterprise level will – to an unknown degree – 'unlock' some of the benefits offered by the post-1987 reforms. But it is important to eschew unwarranted expectations, both because they may engender mistaken policies and because of the ill-effects which might attend their eventual disappointment. (*National Wage Case April 1991*, print J7400)

A leading source of the notion that enterprise bargaining would drive productivity gain was the BCA. Its Employee Relations Study Commission, chaired by Frederick Hilmer, said in 1993:

The situation facing the average Australian enterprise is that it is about 25 per cent below best practice in terms of productivity broadly defined, that is, including value and timeliness effects as well as cost per unit. The enterprise's best competitors are assumed to be continuously improving performance at 6 percent per annum. This figure is consistent with the performance achieved in the best Asian countries, though it may well be less than the performance of the best enterprises. If the Australian enterprise seeks to catch up to best practice by the year 2000, then the arithmetic requires it to increase productivity at 11 per cent per annum on a sustained basis. Few firms are achieving this goal and for the economy as a whole to reach international standards of best practice our national rate of productivity increase would have to triple or quadruple. In short we are facing a challenge which reform to date has been unable to meet.

It might be argued that the reason why required productivity increases are not being achieved is due to weak management rather than the inadequacies of reforms to the

industrial relations system. It has become commonplace for management to be criticised for a lack of skills in award restructuring and workplace reform. ... However, even if one accepts that employee relations management is an under-developed skill among Australian managers, one cannot leap from this fact to the conclusion that Australian management is poor and that managerial reform alone, without fundamental reform of the industrial relations system, will lead to the required rate of improvement (Hilmer, Angwin, Layt, Dudley, Barratt, and McLaughlin (1993: 92-93).

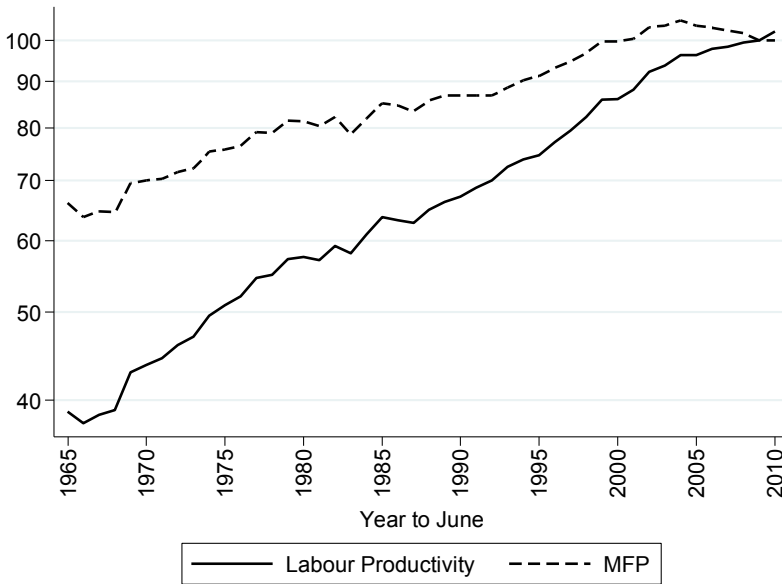
Whereas the ACTU saw enterprise bargaining as the instrument of a restored capacity for over-award bargaining, for most of the employer parties it was a stepping-stone toward a labour market with fewer impediments to the exercise of managerial discretion. Less fettered discretion, they thought, would enhance both profitability and productivity. Their position, it must be said, had high-level support. In response to the AIRC's refusal of an enterprise bargaining principle, the Treasurer (Paul Keating) deplored the Commission's conservatism in clinging to 'the pre-eminent role of the national wage case' and postponing 'a more flexible system of enterprise bargaining'. Only through enterprise bargaining, he said, could Australia 'obtain the great productivity advances available from changing workplace arrangements and conditions'; and only through enterprise bargaining could the wage system become 'more responsive to the changing conditions of demand and supply or to different skills in different regions' (*Parliamentary Debates*, vol H of R 177, p 3067).

There was no empirical basis for the assumption that enterprise bargaining *would* cause higher productivity. At the level of a *a priori* speculation, the links sometimes asserted were along the following lines:

- Enterprise bargaining would cause the employees of the enterprise to feel that they had an interest in the success of the enterprise.
- It would allow employers to buy cooperation by making wage increases conditional on better work.
- It would make for better understanding by employers and workers of each other's objectives, causing behaviour modification conducive to productive businesses.

No weight was given to the contrary hypothesis: that bargaining, bringing with it the sanctions of strikes and lockouts, might actually develop attitudes of hostility and non-cooperation.

The motives of the principal parties were fairly straightforward. For the unions, the objective was to escape from the prevailing restraints on their capacity to make and to prosecute demands for higher wages. They objected to the disciplines imposed on them by the wage-fixing principles and thought that the concessions made by their members under the Restructuring and Efficiency and Structural Efficiency principles had gone far enough. This is well documented by Chris Briggs (2001). For the employers, the goal was to get the workplace control that

Figure 1. Market sector productivity, 1964-65 to 2009-10

Sources: ABS 2006, Australian System of National Accounts, 2005-06, Cat. No. 5204.0, Table 22; ABS 2010, Experimental Estimates of Industry Multifactor Productivity, Australia: Detailed Productivity Estimates, cat. 5260.0.55.002_2009-10.

had been denied to them by the arbitration system and the rights that it accorded to unions. There was a temporary alliance of convenience while the arbitrators were put in their place, but the long-term objectives of the two sides were different and, to a large degree, inconsistent. It has become clear that major employer representatives do not really favour collective bargaining. Where unions do have the capacity to enforce demands, their power is resented. Indeed, it is ironic that employer representatives and conservative commentators, whose predecessors lauded enterprise-level bargaining as the key to higher productivity, now complain so vehemently about the behaviour of the unions. What did they expect?

The Productivity Record

I turn now to productivity data. It is appropriate to set the post-1991 record in an historical context. In Figure 1, we have market-sector productivity between 1964-65 and 2009-10.¹ The figure shows both labour productivity and multifactor

1. The market sector comprises: agriculture, forestry and fishing; mining; manufacturing; electricity, gas, water and waste services; construction; wholesale trade; retail trade; accommodation and food services; transport, postal and warehousing; information, media and telecommunications; financial and insurance services; rental, hiring and real estate services; professional, scientific and technical services; administrative and support services; arts and recreation services; and other services.

productivity; and in each case it shows both the actual annual observations and the trend lines fitted to them. For labour productivity, the trend line corresponds to an annual growth rate of 2.2 per cent; for multifactor productivity, the growth rate is 1.1 per cent. It is obvious that the trends ‘explain’ much of the variance. If you explain the trends, you say most of what needs to be said about Australia’s long-term productivity performance. But if the subject of interest is shorter-term influences such as the shift to enterprise bargaining, it is useful to abstract from the trends and to look at the annual productivity observations as deviations from trend. Figure 2 does this. It shows the annual productivity levels as percentage deviations from trend.

Focusing on the post-1991 period, we see that there was strong growth in productivity in the later 1990s. The timing seems to depend somewhat on whether we are considering labour productivity or multifactor productivity. The ‘surge’ of multifactor productivity began two years earlier than that of labour productivity. On either measure, it ended in 1998-99. There were then a few years of fluctuation relative to trend; and the decline which is now causing consternation began in 2004-05.

I shall return to Figure 2; but before I do so, I want to make two digressions.

One is about the relation between productivity and real wages. It was for long thought that there is a tight relation between the two. Indeed, it was a common

Figure 2. Market sector productivity, 1964/65-2009/10, deviations from trend

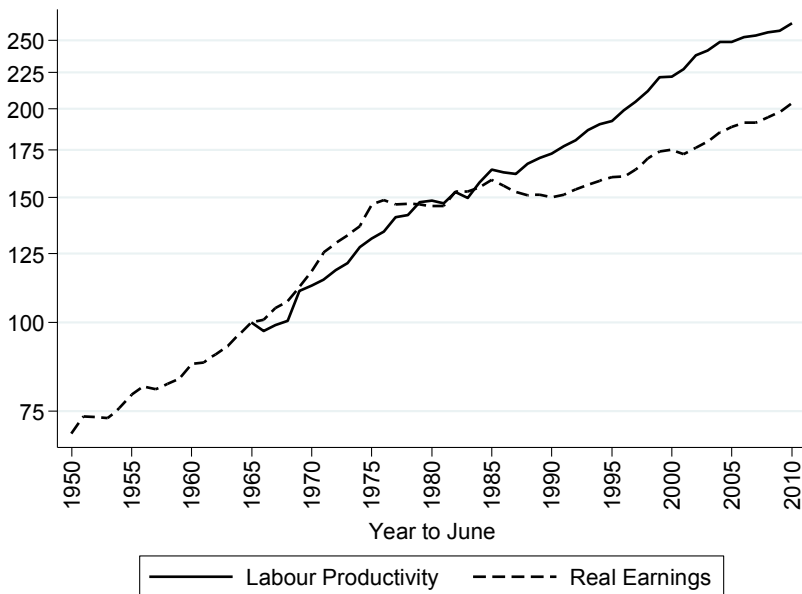


Source: ABS (2010) Experimental Estimates of Industry Multifactor Productivity, Australia: Detailed Productivity Estimates, cat. 5260.0.55.002_2009-10.

contention – and I lent some support to it – that real wages could and would rise *pari passu* with productivity and that money wage increases in excess of productivity growth would merely spill into inflation. Figure 3 bears on this issue. Unfortunately, the productivity numbers only begin in 1964-65. I have included earlier numbers for real wages to demonstrate the long period of strong growth in them; but I should acknowledge that I have had to construct this series by joining different sets of numbers and it has to be regarded as approximate. The earnings series represents, as best I can construct it, average total adult male earnings. The productivity numbers relate only to the market sector, whereas the earnings figures are economy-wide. I do not attach great importance to differences in trend between the two series. What I do find interesting is their different time patterns. Real earnings continued to rise strongly until 1974-75 and then stagnated for 15 years, despite the continuing growth of productivity. After 1989-90, they began to rise again; and the growth rate of real wages accelerated after 2000. I am not suggesting for a moment that productivity growth does not matter for real wages, but the relation between the two is clearly more complex than we used to suppose.

My second digression is to note that the ABS now publishes productivity estimates based on quality adjusted hours of work. The basic estimates, such as

Figure 3. Real earnings and labour productivity

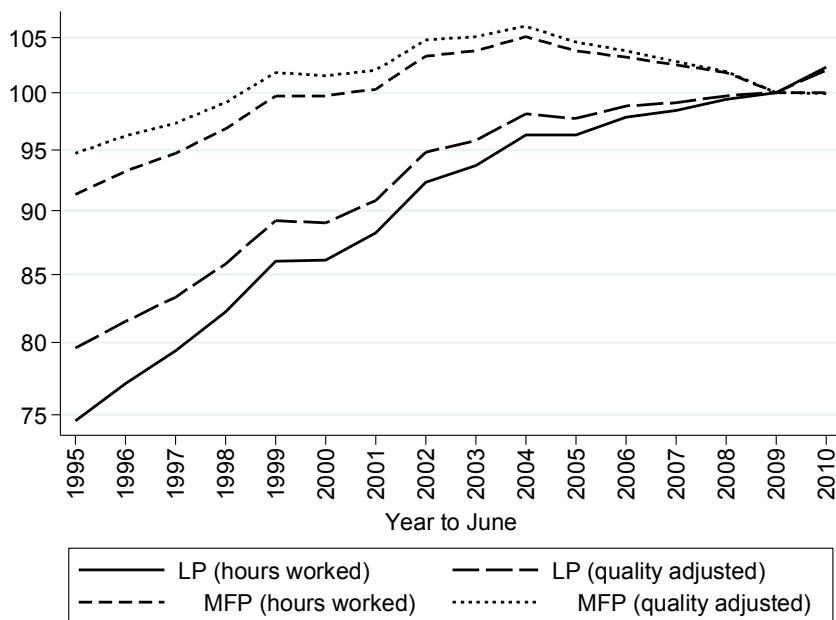


Source: Real earnings data are for the period 1950 to 2010 and are constructed from various sources. Productivity data are for the period 1965 to 2010 and are taken from ABS (2010) Experimental Estimates of Industry Multifactor Productivity, Australia: Detailed Productivity Estimates, cat. 5260.0.55.002_2009-10.

are used in my previous figures, simply assume that an hour is an hour, no matter what the work is. For some purposes, that is an appropriate assumption. But if the question is how well the economy has been using its resources, we should take into account changes in the quality of labour. The ABS measures ‘quality’ by relative wages, and quality adjustment allows for shifts in the composition of hours to more expensive or less expensive ones. What would we expect to find? We are all familiar with the story of the disappearing middle. This implies that there have been shifts toward both high-quality and low-quality hours and away from medium-quality hours. Which shift predominates? Figure 4 shows what has happened, though only since 1994-95. Quality adjustment, in fact, reduces the measured growth of productivity. This means that, on balance, the shift has been toward higher-quality hours.

I return to Figure 2. The recent experience, where multifactor productivity has actually declined and labour productivity has fallen relative to trend, is somewhat outside my terms of reference – except for two things. First, it is not plausible to ascribe this experience to changes in industrial relations. The suggestion that it was caused by *Work Choices* is too far-fetched to be taken seriously. So too is the suggestion that it is due to re-empowerment of unions by the Rudd and Gillard governments: the timing is against that. It follows that some other powerful

Figure 4. Productivity, 1994/95 – 2009/10 (quality adjusted hours)



Source: ABS (2010) Experimental Estimates of Industry Multifactor Productivity, Australia: Detailed Productivity Estimates, cat. 5260.0.55.002_2009-10.

factor or factors must have been at work. If that is true of the recent experience, it must at least raise a question as to whether any focus on industrial relations in the 1990s is misplaced. Second, it has been argued that the less favourable productivity experience of the past decade, by comparison with the 1990s, is due to the effects of policy changes (including the shift to enterprise bargaining) having exhausted themselves. The implication is that there was some low-hanging fruit that was picked in the nineties. Once it was gone, that was that. The Productivity Commission (2009) and Eslake (2011) have lent a degree of support for this interpretation, though insisting (at least in the Productivity Commission's case) that there is more fruit available if we only try hard enough. As of 2004-05, that understanding of the world had some resonance with the evidence and it is not to be disregarded. But something more seems to be necessary to explain the stark decline of the growth rate in the next five years.

It is useful, I think, to look at the ABS's analysis of productivity at the industry level. To save time and to minimise tedium, I shall confine myself to labour productivity. There are data for 16 industry groups. For 12 of these, the data cover the years from 1985-86 to 2009-10; for the other 4 they are available only since 1994-95. Sixteen industries are too many for one graph; hence I shall show them in three.² Beginning with Panel A in Figure 5, I draw your attention first to manufacturing. If there were a productivity surge triggered by enterprise bargaining, we might surely have expected to see evidence of it in manufacturing; but there is none. Next consider mining. Here we see a strong rise in productivity from 1985-86 or earlier and continuing to 2001-02. This has been followed by a stark decline. The important point for my paper is that the rise began well before the shift to enterprise bargaining and was not obviously boosted by it. Much the same story can be told of electricity, gas and water, except that the peak came earlier – in 1997-98. Construction does show some modest signs of additional productivity growth in the late 1990s, although most of the gain was lost in the next few years. In agriculture, there has been a continuing growth of productivity, not obviously affected by time-specific developments such as enterprise bargaining.

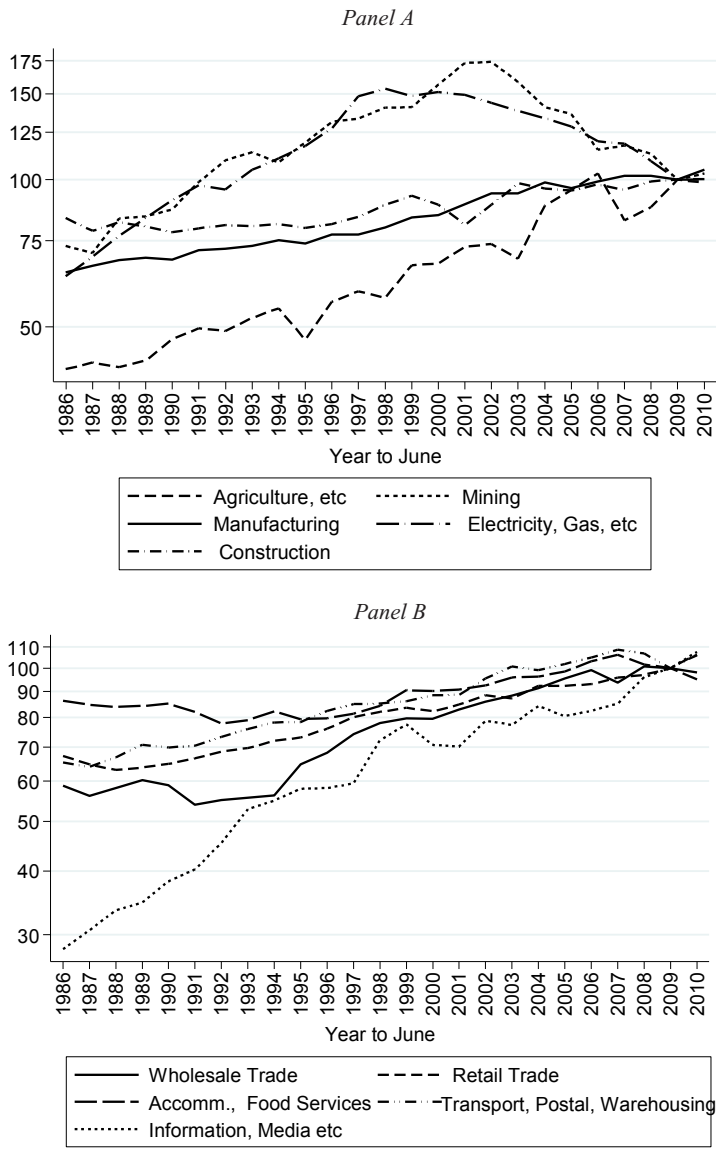
Panel B in Figure 5 covers wholesale trade; retail trade; accommodation and food services; transport, postal and warehousing; and information, media and telecommunications. Notice first the line for information, media and telecommunications. Here we see that there was strong growth in productivity beginning in or before 1985-86, and that the growth rate actually fell away at around the time of the shift to enterprise bargaining. There was an improvement between 1996-97 and 1998-99, which may or may not have been due to enterprise bargaining. Next look at wholesale trade: this, in terms of timing, is probably the best exhibit for enterprise bargaining, for there was a definite boost to productivity

2. The source for all three figures is ABS (2010) *Experimental Estimates of Industry Multifactor Productivity, Australia: Detailed Productivity Estimates*, cat. 5260.0.55.002_2009-10.

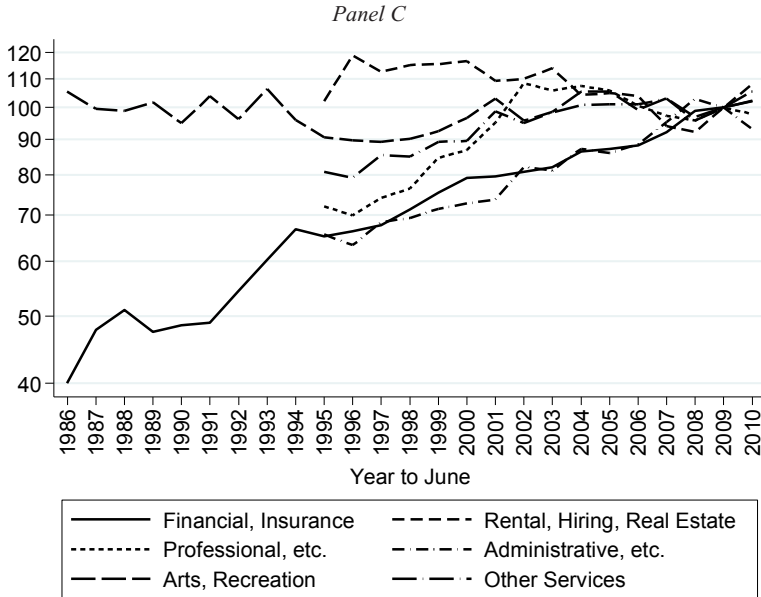
in the later 1990s. There is perhaps a faint echo of this in retail trade. In the other two industry groups, it is hard to discern anything special to the post-enterprise bargaining era. These are accommodation and food services and transport, etc.

I shall not list all six industry groups covered in Panel C of Figure 5. Financial and insurance services underwent a productivity surge in the early 1990s. My guess is that this had more to do with the spread and improvement

Figure 5. Labour productivity, Australia, by industry, 1986-2010



contd.

Figure 5. *contd.*

of IT than with bargaining arrangements. In the professions, where we probably would not look for the clearest shift to enterprise bargaining, productivity leapt dramatically between 1995-96 and 2001-02. Since then, it has declined.

What seems to emerge from this industry-level dissection is that the short-lived productivity surge of the 1990s was an aggregate outcome of different patterns in different industries. The supposition that it was due to enterprise bargaining is hard to sustain. Insofar as there was a surge, it seems either to have occurred in the wrong industries or, if it was in the right industries, to have been a continuation of a process that pre-dated enterprise bargaining.

Altering the trends

During the 1990s, and especially in the enterprise-bargaining debates, there were predictions that the changes introduced would provide, not only a one-off shift in the level of productivity, but also an increase in the growth rate. The idea was, I think, that policy reform would release a brake on experimentation and innovation that generate continuous improvement. This would mean that the long-term trend of productivity would be higher than previously. The more pessimistic view is the 'low-hanging fruit' one to which I have already alluded. In the industrial relations context, there were various productivity-reducing work practices which might be abolished. The Arbitration Commissions had, indeed, sought this effect through Restructuring and Efficiency and Structural Efficiency;

and it might have been hoped that collective bargaining at the enterprise level would allow employers to buy out some or all of the remaining restrictions.

Unless we identify some temporary cause which has affected the productivity performance since 1998-99, we can hardly now think that policy reforms have caused an upward tilt in the productivity trend lines. Whatever was gained, in terms of moving above the trend, seems to have been forfeited. If we divide the period covered by Figure 1 into the pre-1991-92 years and the post-1991-92 years, we find that the trend growth rates have actually diminished:

	<i>Labour Productivity</i>	<i>MFP</i>
<i>Pre-1991-92</i>	2.34	1.18
<i>Post-1991-92</i>	2.20	0.88

In the early 2000s, when the first signs of the deterioration had appeared, proponents of the more optimistic view, such as the Productivity Commission, attributed it to temporary factors. One favourite was the millennium bug which, it was said, had led to a diversion of resources to relatively unproductive purposes. By now, it must surely be plain that there is more to it than short-term and one-off causes.

Explaining the ‘surge’

The Productivity Commission has characterised what happened in the 4-6 years before 1998-99 as a ‘productivity surge’. It attributes the surge to microeconomic reform, and it arrives at this conclusion by a process of elimination. That is, it rejects or ascribes small importance to a range of other explanations that might conceivably be put forward. The downplayed explanations include:

- That Australia was ‘carried along by an international productivity boom’. Australia, says the Productivity Commission, led the field rather than followed along.
- That the surge was a normal result of recovery from the recession of the early nineties. The improved performance was ‘longer and stronger than in previous recoveries’.
- That the surge was due to an increase in the level of skills in the workforce. ‘Analysis by Barnes and Kennard (2002) of ABS estimates of MFP adjusted for labour quality shows that there was in fact a decline in the contribution of labour quality improvement between the 1988-89 to 1993-94 cycle and the period of the surge.’
- That there was some special technological leap-forward. ‘While some other countries, including the United States, derived some productivity benefit from rapid advances in the production of information and communication

technologies (ICTs) in the 1990s, Australia produced little in the way of ICTs and so did not access that source of productivity gain.'

The Productivity Commission continues:

The removal of these possible explanations as likely causes of the surge in productivity leaves the reforms of the latter part of the 1980s and the 1990s as the prime candidate. This should not have been surprising, as the reforms were predicated on the need to remove policy-related sources of inefficiency that were seen as holding back relative living standards. One of the central economic problems that had faced Australia up to the mid-1980s was that large parts of the economy were inefficient, inward looking and inflexible. In particular, protection policy had allowed small scale production to proliferate, distorted the flow of economic resources away from industries with the best potential to add value and prospects for growth, encouraged manufacturing to focus on import replacement, and fostered a culture that allowed poor management and work practices to develop and become entrenched. This meant Australia was not well placed to respond to the changes and challenges arising from rapid technological change, global integration and fiercer competition from abroad.

The reforms of the 1980s and 1990s encompassed changes in monetary and fiscal policies, capital markets, industry assistance, taxation, government enterprises, regulation, labour markets and industrial relations, and innovation and training. These changes were linked with greater economic flexibility, improved efficiency and international competitiveness, and a more outward looking, opportunity focused business culture.

The Productivity Commission's reliance on the process of elimination entails a risk of overlooking something and also requires you to be sure that your grounds for rejecting each alternative and all of them together are cogent. The Productivity Commission may dismiss too readily the possible effects of developments in IT. It seems to argue that because Australia is not a producer of IT equipment, it does not benefit, in terms of productivity, from advances in this kind of technology. That, in my judgment, does not allow sufficiently for the benefits of *adopting* technologies developed elsewhere. I am not much impressed by the Productivity Commission argument that in the 1990s Australia was the productivity leader rather than the beneficiary of international forces. There is no reason why productivity gains due (say) to adoption of IT should be simultaneous in different countries. Australia in the 1990s may have enjoyed gains that, in other countries, occurred at different times.

When it comes to the policy reforms, the Productivity Commission itemises those going to monetary and fiscal policies, capital markets, industry assistance, taxation, government enterprises, regulation, labour markets and industrial relations, and innovation and training. That is, labour markets and industrial relations are but one of a range of reforms to which the Productivity Commission

attaches importance. There is no attempt to quantify the role of any of the factors in the list. This is not to be critical of the Productivity Commission, for I do not think that there is any way of disentangling their effects. But it is pertinent to the issue of enterprise bargaining and productivity that the endorsement of enterprise bargaining was merely one of a set of policy changes that occurred around the same time.

Conclusion

Let me summarise. There can be no certainty about the productivity effects of enterprise bargaining, because the counterfactual situation is and will remain unknown. That said, I contend that there are good grounds for doubting that enterprise bargaining contributed much, if anything, to productivity – still less to ongoing productivity growth. These grounds are:

1. At most, there was a four-year boost in productivity whose timing does conceivably match the introduction and spread of enterprise bargaining. The boost has not endured.
2. If the four-year boost was policy-induced, there were other changes of policy in the late 1980s and early 1990s that may have been more important than the shift to enterprise bargaining.
3. When the productivity data are dissected to the industry level, it is hard to identify any large movements in productivity that could reasonably be ascribed to enterprise bargaining. Wholesale trade is a possible exception. The records of some major industries, notably mining and electricity, gas and water, suggest that much stronger influences have been at work.

The AIRC's scepticism has, I think, been vindicated.

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