

# Australian economic "boom": a widening gap between hype and reality

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For Prime Minister John Howard and Treasurer Peter Costello, the latest national accounts figures, showing the Australian economy had grown 1.3 percent in the December quarter and 4.2 percent for the year, were something of a political godsend.

Howard has spent the last month embroiled in two scandals: the exposure of the government's claim that refugee children were "thrown overboard" when their boat was intercepted by the Navy last October, and accusations that Governor-General Peter Hollingworth, Howard's appointment to the post, covered up sexual abuse in the Anglican Church when he was archbishop of Brisbane.

Prime Ministerial aspirant Costello has kept himself well clear of both the "children overboard" events and the controversy surrounding the governor-general. But he has had some problems of his own. They centre on revelations that the government has lost up to \$5 billion in foreign currency markets as the result of a system that saw a portion of the Australian debt denominated in US dollars to take advantage of lower US interest rates. The losses were incurred when the Australian dollar fell sharply against the US currency.

So when the economic numbers were released last Thursday both of them had good reason to seize upon them and begin trumpeting the Australian economic "success story".

Howard told a radio interviewer that the Australian economy was "going gangbusters." But then added an immediate rider that this should not lead to a lift in interest rates by the Reserve Bank.

Costello was no less effusive. "It looks to me as if the worst in the international environment is over, and Australia survived the worst in the international environment. I don't like tempting fate, because there could be another shock around the corner, but I think

this is a remarkable run.

"The fact that Australia grew in 2001 at 4 percent when Japan was in recession and America was in recession and a good deal of Europe was in recession, that the growth rate was 10 times the average of the OECD and the G7 [major industrial economies], I think is truly remarkable."

The media chimed in with headlines such as "Australia booming amid the gloom" and "Australia has fastest-growing economy in developed world." According to one *Sydney Morning Herald* columnist, the unexpected surge in growth had "cemented Australia's place as the stellar performer of the developed world."

One of the reasons for this overblown reaction to the upturn in the business cycle seems to be relief in government and financial circles that the downturn that loomed little more than 12 months ago proved to be less serious than first thought. Twelve months ago, the national accounts figures showed that growth in the December quarter of 2000 had contracted by 0.4 percent. There were fears that with the US economy entering a slowdown and the Japanese economy already in recession, Australia would follow suit.

In the event, growth rates turned positive resulting in a 4.1 percent expansion for the year. But this upturn by no means signifies that Australia has either escaped the impact of global economic trends or found some high road to economic success. Rather, examination of the growth components show that the unexpected rise resulted from factors that will not be repeated.

Over the course of the year consumer spending rose by 4.2 percent and played a central role in lifting the economy as a whole. But it outstripped the growth in income to the tune of 1.9 percentage points, meaning that households saved less and borrowed more to

increase spending.

One of the factors behind the increased spending and indebtedness is the real estate bubble. Figures released along with the national accounts data show that established house prices in the capital cities rose by 15.5 percent in 2001. But, as a comment in the *Australian Financial Review* pointed out, while this boom is a source of increased purchasing power it can be a “potential source of distress” if interest rates increase.

With household debt now at more than 100 percent of annual disposable income it will not take a large increase in rates for that “distress” to increase. Moreover, figures calculated by the ANZ Bank show that after basic costs such as rent, gas, electricity, health, insurance and vehicle operating costs are taken out, debt-servicing costs are around 10 percent of remaining income.

An examination of the components of expenditure is also revealing. In the December quarter, spending on housing investment rose by 7.9 percent along with increases in house-related items.

According to Michael Blyth, chief research economist for the Commonwealth Bank: “If you take the September and December quarters together it was the biggest increase in dwelling investment since 1975. And that has big knock-on effects to other parts of the economy.”

The housing boom has been pushed along by two factors: the two percentage point cut in interest rates during 2001, which sent mortgage rates to their lowest levels in more than three decades, and the government’s \$14,000 grant to first-home buyers. Both these stimuli will taper off. Interest rates are expected to rise and the grants scheme is to be phased out, starting in July.

While Howard and Costello, supported by the mass media, waxed enthusiastic about the Australian economic performance, there were some significant figures they chose not to highlight.

The value of transport services, for example, fell 10 percent in the December quarter, reflecting the collapse of Ansett, the country’s second biggest airline, last September with the loss of 26,000 jobs. The communications industry, once hailed as the heart of the “new economy,” suffered a 4.4 percent drop for the December quarter and a 3.4 percent decline for the

year. This was the first contraction in this industry since 1976.

Despite the fact that the Australian dollar fell to record lows in international currency markets, exports declined 3.2 percent in the December quarter.

The most significant figures of all concern employment levels. The trend level in the total number of hours worked dropped by another 0.5 percent in the December quarter, taking the fall in the past year to 1.2 percent. Official unemployment levels are still more than 7 percent, with most estimates putting the real jobless level at above 10 percent. The number of long-term unemployed—those who have been out of work for more than a year—total around 385,000, the same as in 1995.

The gap between the media hype surrounding the official statistics and the experiences of working people was highlighted in some of the letters to the *Sydney Morning Herald* following the release of the national accounts data.

One correspondent warned Treasurer Costello there was “little healthy growth in this performance.” “When interest rates rise and the dollar drops further, I’d like to see which levers you pull.”

Another commented that while the housing boom had been a bonus in the short term, “we must hope that the Treasurer has another rabbit in the hat as the boom comes off and the personal debt begins to bite, given that our personal bankruptcy rate is already at record levels.”

A third letter-writer summed up the situation as follows: “We are experiencing record personal debts, longstanding companies have been going bust and leaving thousands of people unemployed, house prices are soaring, our government has lost billions of dollars playing the foreign exchange market—yet it has the cheek to tell us we are going through a major economic boom.”



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