Australia: Banks warn of “painful” recession

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Australia is vulnerable to recession in 2012 according to bank economists, and thousands of job losses have already begun in the banking industry, further denting the claims of the Labor government that the country’s economy is shielded from the European-centred global credit crunch because of mineral exports to China.

The banks’ warnings this week, issued amid signs of slowing growth in China, falling commodity prices and World Bank predictions of a sharp global downturn, underscore the acute exposure of Australian capitalism to the worldwide impact of the worsening global financial crisis.

According to a research report by investment bank JP Morgan, Australia’s over-reliance on the slowing Chinese economy, the local banks’ vulnerability to funding shocks and high rates of household debt make the country even more recession-prone than at the commencement of the global breakdown in 2008.

In a clear reference to the austerity measures being imposed on the working class across Europe at the behest of the financial markets, JP Morgan chief economist Stephen Walter said Australia had not undergone the “adjustments observed elsewhere … abrupt or otherwise, voluntary or not,” and remained “vulnerable to shocks.”

Walter said the Gillard government’s pledge to return the budget to surplus by 2012-13 allowed no scope for the kind of pump-priming that in 2008-2009 rescued the Australian banks and big business. The government had “donned a fiscal straitjacket by unwisely and implausibly promising a budget surplus in the next fiscal year,” he said. “This requires an abrupt fiscal adjustment that officials are politically bound to deliver…The next recession, when it inevitably arrives, could be very painful.”

In a separate report, HSBC chief economic Paul Bloxham warned of a negative reaction by the international financial markets if the government failed to deliver the promised budget surplus, as was increasingly likely. “The quite ambitious plan for fiscal unwind has helped to protect Australia’s very strong sovereign debt position and is likely to be supporting the availability of international funds to local banks,” he said. “However, slippage in the plans to return to budget surplus is a key risk, particularly if global growth is weaker than currently expected.”

Another JP Morgan economist, Ben Jarman, told the *Sydney Morning Herald* that consumer spending patterns in Australia were following those in the US and Britain, both of which have suffered their deepest recessions since the 1930s. He said the drying-up of consumer demand was made even more dangerous in Australia by high levels of household debt, mostly in the form of mortgage borrowing. “It would be pretty amazing if we were the one economy in the world where there wouldn’t be a long period of deleveraging in recognition of the fact that asset prices aren’t growing how they grew in the prior decade.”

“Deleveraging” means the reduction of debt, including through asset sales—in this case houses. A “long period of deleveraging” will exacerbate already falling house prices. Australia’s prices remain among the most inflated in the world. Over the past decade, they have surged 147 percent, while incomes rose by only 57 percent. The rate of household debt (mostly mortgages) to income is 150 percent.

Mounting job losses could become the trigger for this debt ‘time bomb.’ According to a report by the international bank UBS, the banks themselves will shed an estimated 7,000 jobs in the next two years (1 in every 25 employees), on top of the thousands of job cuts being made by the federal and state governments, and mass sackings that have already occurred at Qantas, BlueScope Steel and other major businesses.

The ANZ bank this week announced that 700 jobs would be lost in Australia, mostly in Sydney. ANZ, which posted a $4.36 billion annual profit in November, already cut 2,150 jobs between March 2009 and September 2011. The Royal Bank of Scotland this week announced the closure of its Australian offices, meaning the loss of more than 200 jobs, and Westpac executives indicated that they would eliminate about 600 jobs this year.

The Australian Bureau of Statistics yesterday reported a loss of 29,300 jobs in December, although the official seasonally adjusted unemployment rate remained at 5.2 percent because of a decrease in the labour participation rate, indicating that more people had given up looking for work. For the first time since 1992, there was a net annual loss of jobs last year.

With European banks lurching further into crisis, the ‘big four’ Australian banks are already being forced to pay steeper interest rates as they start to refinance $96 billion worth of borrowings in 2012. Despite its debt still being rated AAA, the Commonwealth Bank of Australia had to pay 1.75 percentage points above the short-term bank bill rate in a “covered bonds” auction to raise $3.5 billion this week.

Finance market analysts told the *Australian Financial Review* that the deal marked a “step change” in the cost of funds for Australian markets, increasing the financial pressure on them not to pass on any future official interest rate cuts by the Reserve Bank of Australia. Rising bad debts—company liquidations rose by 9 percent in the third quarter of 2011—were also creating “key asset quality stress” for the banks, Credit Suisse warned.

Acting Treasurer Bill Shorten dismissed the gloomy forecasts and claimed that Australian banks were “rock solid.” But the banks only dodged a meltdown during the 2008-09 crisis because the Labor government guaranteed their offshore borrowings, the source of 40 percent of their capital. Even if the government reactivated that guarantee, borrowing costs would rise sharply.

Falling house prices are compounding the funding squeeze. Prices in Australian capital cities slid 3.7 percent in the first 11 months of 2011, following what was already the largest annual drop in 12 years. Brisbane, capital city of the resource-rich state of Queensland, suffered home price falls of 7 percent overall, with bigger falls in outlying working class suburbs. Average Melbourne prices fell by 5.7 percent. Prices in Sydney dropped by just 1.1 percent, but that city suffered the largest increase in home repossessions—22.5 percent—reflecting the destruction of jobs in the manufacturing and finance sectors.

Commenting on the ANZ jobs announcement, Acting Treasurer Shorten feigned sympathy for bank workers, saying the retrenchments were “unfortunate,” but added: “I can’t stick my head in the sand and pretend that there is no upheaval going on in banking around the world, because there is.”

Earlier, responding to the recession warnings, Shorten had insisted there was “a stark contrast between Australia’s rock solid economic fundamentals and the fiscal challenges facing Europe and other parts of the world.” He declared: “By global comparison, Australia walks tall because of the relative strength of our economy under the Gillard government’s strong economic management.”

Far from being rock solid, the Australian banks and the entire economy are highly exposed to the deepening global crisis. As job losses mount, causing further social misery, the Gillard government’s claims of “walking tall” will be increasingly discredited, fuelling mounting discontent among working people.