Australian rate cut warnings point to economic slump

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Major banks and finance houses are predicting further official interest rate cuts in Australia, taking rates to their lowest-ever recorded levels—perhaps even negative—by next year.

These forecasts point to a gathering economic slump, bringing with it deep cuts to working-class living standards, which are already being decimated by falling real wages. Financial commentators are writing of Australia being drawn into a deflationary "vortex" of falling prices, consumer spending and business investment.

This reality is being deliberately hidden from public view, as much as possible, in the campaign for the July 2 double-dissolution election for all members of both houses of federal parliament.

On May 3, just hours before the Liberal-National Coalition government delivered this year's budget, the Reserve Bank of Australia (RBA) cut its cash rate from 2 percent to 1.75—a record low. It was a desperate bid to stimulate borrowing and also drive down the value of the Australian dollar, giving the lie to the optimistic picture painted by the budget.

The financial markets have now made it plain that sharper rate cuts will be required because economic growth rates will fall far short of the projections offered in the budget.

Last week, the Commonwealth Bank of Australia became the first of the country's big four banks to predict another two RBA rate cuts in 2016, which would take the cash rate to 1.25 percent. The CBA's chief economist Michael Blythe said recent data showing price deflation had spread to Australia "shocked the RBA."

Other financial institutions issued even more dire forecasts. Vimal Gor, BT Financial Management's Sydney-based head of income and fixed interest, wrote in the group's April newsletter that "the RBA will be easing to 1 percent" with "a move to 0 percent or lower a distinct possibility."

Gor said the growth forecasts issued by the government and the RBA lacked "sustainability." Falling steel production in China would slash iron ore exports, which actually grew in volume and value in 2015 despite lower prices. This would be compounded by a "far from rosy" picture created by an over-construction of apartments, which had partly offset the collapse of the mining boom since 2012.

Gor warned that weak wages growth would add to the downward slide, as would governments' fear that any increased public spending and debt would risk losing the country's AAA credit rating on the global money markets.

David Murray, a former CBA chief executive and head of the government's financial system inquiry, warned of a downward spiral in consumer spending after the benchmark 10-year government bond yield crashed to 2.20 percent—its lowest level in at least 141 years. As well as hurting retirement savers, that plunge also demonstrates that investors foresee a trajectory of deflation and low growth.

These unprecedented trends are producing anxiety in the corporate elite and the financial markets. None of the traditional levers of capitalist economics—such as lowering interest rates—are preventing Australia, like other commodity export dependent economies, following Japan, Europe and North America into stagnation.

Writing in the *Australian* on May 7, economics correspondent Adam Creighton noted that for the past eight years, the Australian Treasury's revenue forecasts "optimistically have overshot reality, often significantly." A "stubborn assumption" that

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Australia's economy would "whirr back to 'normal'" had "proved continually misleading" since the 2008 global financial crisis.

The truth is that both the previous Labor government, in office from 2007 to 2013, and the current Coalition government have perpetrated this deception.

Creighton pointed to the fraud of the May 3 budget forecasts. According to the budget, the growth rate of the dollar value of the economy, known as nominal gross domestic product (GDP), would suddenly rise from 1.4 percent last financial year and 2.5 percent this financial year to 4.25 percent next year and then 5 percent. This generated unrealistic revenue calculations, such as that company tax, which fell 2.2 percent this year, would surge 19 percent across the next two years.

If the growth rate remained at 2.5 percent, Creighton calculated, the annual budget deficit would blow out to $56 billion by 2019, far from the $6 billion forecast by the government on May 3.

Workers' wages in Australia are already going the way of their counterparts in the US, Britain and Europe, where pay levels have been stagnating or sliding in real terms. In fact, because of the end of the resources boom, and wage-cutting throughout other basic industries, Australian workers have suffered one of the steepest falls in wage growth of any Organisation for Economic Cooperation and Development (OECD) country.

By RBA estimates, wage growth has dropped to an annual rate of just 0.4 percent, meaning a cut in real terms compared to household cost of living rises. The fall was greater than in any other OECD country, except for crisis-ridden Mediterranean and eastern European countries and The Netherlands.

This means that working people are already being made to pay for the worsening economic situation globally and in Australia. Alongside the mining collapse, the car industry is being shut down nationally, steel and other basic manufacturing plants are being wound down and several major retail chains have gone into liquidation, throwing thousands into unemployment or lower-paid and insecure employment.

Amid the fallout, the number of Australian companies entering voluntary administration increased by 18 percent to 10,299 in the 12 months ending March, according to an analysis of official data by FTI Consulting. Default payments have also risen by about 12 percent in value, hitting other businesses and throwing question marks over the bad debt provisions of the major banks.

Adding to the anxieties in ruling circles are mounting signs that a glut of speculative apartment construction, particularly in Sydney, Melbourne and Brisbane, could burst the housing bubble that has kept the economy from officially going into recession over the past four years.

CoreLogic research analysts last week released a New Settlement Risk Report, showing that 231,129 new units are due for completion in Australia's capital cities during the next two years, many more than the average number of sales over the past five years. Greville Pabst, executive chairman of WBP Property Group told *news.com.au*: "The figures paint an alarming picture for the new apartment market in the coming 12 to 24 months."

Many apartment complexes have been sold "off-the-plan" to investors, who usually pay 10 percent deposits. Because of rising debt risks, the banks have been forced to cut back lending to investors, who now may be unable to make settlements on the properties once construction is completed. As a result, prices have begun falling, compounding the alarm.

Once the July 2 election is out of the way, regardless of which party heads the next government, the fraudulent slogans of "jobs and growth" or "putting people first" will be quickly cast aside to bring forward drastic cuts to public spending and living standards.

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