Australian growth up but wages fall

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3 March 2017

Australia has avoided a technical recession—defined as two consecutive quarters of negative growth. National accounts figures issued on Wednesday for the December quarter showed that gross domestic product (GDP) rose by 1.1 percent, following a 0.5 percent contraction in the previous three months.

Media headlines declared that economic growth was "back on track" and even that the economy had "roared" back to life.

However, yesterday the Organisation for Economic Co-operation and Development (OECD) issued a report on the Australian economy, warning it was vulnerable to a recession if the housing price bubble collapsed, impacting on consumer spending and hitting the major banks.

There were three main reasons for the increase in GDP, each pointing to the fragility of the recovery. The biggest factor was increased household consumption spending. It contributed 0.5 percentage points, almost half the increase for the quarter. This was despite household incomes contracting by 0.5 percent.

The consumer spending rise was financed by a rundown of savings. Households put just 5.2 percent of their income into savings, the lowest level since before the global financial crisis of 2008–09.

A number of commentators attributed the apparent strength in consumer spending to the "wealth effect" produced by escalating house prices, which rose by 18.4 percent in Sydney over the past year, with an average rise for the six state capitals of almost 12 percent.

Rising export prices, particularly for iron ore and coal, also provided a boost to the GDP numbers. The terms of trade index, which measures the ratio of export to import prices, rose by 9.2 percent in the December quarter and is now 15 percent higher than in December 2015. This is largely due to an uptick in demand from China, which may not last.

Finally, the growth figure was also helped by an increase in non-mining investment, which showed its first increase for three years. But questions remain over its sustainability.

Capital Economics chief economist Paul Dales told the *Guardian* that, despite the December result, "economic growth will probably still disappoint" this year. "In the second half of last year the economy grew by just 0.6 percent and we know that the collapse in mining investment has further to go," he said. Dales noted that the boost to national income from higher commodity prices will mostly boost profits rather than activity.

In other words, the increase in export prices will not lead to further mining investment, simply greater output from already completed projects.

Moreover, with record low wage growth, the household spending increase cannot be sustained for an extended period.

The national accounts figures were eagerly seized upon by the somewhat beleaguered Turnbull government. Treasurer Scott Morrison claimed that Australia was "top of the pack" of major economies. He said the result "confirms the change that is taking place in our economy as we move from the largest investment boom in our history to broader-based growth."

In fact, other data reveal that economic growth is becoming more narrowly confined. According to SGS Economics and Planning, the two major cites of Sydney and Melbourne were responsible for two-thirds of Australia's economic growth in 2015–16. This compares to their share of 34 percent in the first decade of the 2000s. Many regional areas are experiencing stagnation or economic contraction, which is contributing to the growth of support for right-wing populist parties such as Pauline Hanson's One Nation.

The *Australian Financial Review*, which is waging a

campaign against what it calls Australia's "dysfunctional political culture" and its failure to deliver sweeping pro-business measures, weighed in with an editorial yesterday warning of the fragile nature of the economic upturn.

While the "surprise rebound" in coal and iron ore prices would boost profits, a "sustained return to the sort of income growth Australians enjoyed over the last couple of decades is nowhere in sight."

The editorial emphasised the need for a "growth and productivity agenda"—the code phrase in financial circles for sweeping attacks on social services, government spending and working conditions.

Large deficits, "leave the economy much more vulnerable to any negative shock, such as another financial crisis, a China downturn or a disorderly puncturing of the reinflated Sydney and Melbourne housing bubble."

The record low interest rate of 1.5 percent set by the Reserve Bank of Australia was yet to "cajole a pick-up in business investment" but was "injecting more speculative financial risk into the economy that could come back to bite the over-leveraged housing sector and the big banks."

The editorial's warnings were underscored by the OECD report. In its first major review of the Australian economy since 2014, it said the housing market may not "ease gently" but could develop into a "rout on prices and demand with significant macroeconomic implications."

A significant fall in house prices would produce a fall in household consumption and a rise in mortgage defaults that would impact on the rest of the economy. The OECD noted that households now account for about half of Australia's total debt, compared with around one-third in the mid-1990s. Australia is near the top of OECD rankings for household debt.

The OECD also said Australia, along with other developed economies, "now faces the risk of low growth and lacklustre private sector investment due to pessimistic expectations and weakening global trade."

The government insists it has a plan to ensure economic growth in the form of a cut in company tax rates from 30 percent to 25 percent, costing $50 billion, over the next 10 years.

This scenario was called into question by a report published this week by the Grattan Institute entitled "Stagnation Nation?" It said while a reduced tax rate would attract more foreign investment it would also "reduce national income for years."

Most of the short-term benefits would go to foreign investors. The report also cast doubt on whether tax cuts for small businesses would bring major benefits as they were "unlikely to lead to a substantial increase in investment." Mining investment was experiencing its biggest ever fall and non-mining investment was down to its lowest point in 50 years, with at least a third of the decline due to slow economic growth.

The report called for a "perspective, not panic" but warned there were only "tough choices." The main demand outlined by the OECD was an increase in the Goods and Services Tax (GST) from 10 to 15 percent. In other words, like all other corporate think tanks, the Grattan Institute is insisting that workers and their families must pay for the mounting problems gripping the Australian economy.