

Seven economic problems bigger than budget 'black holes'.

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By focusing on phoney debates about deficits and costings, the major parties and the media are obscuring a big picture. Instead of playing political games, these are the issues we should be talking about, writes Ian McAuley.

The ABC's Vote Compass reveals that "the economy" rates as voters' most important issue in the coming election.

There is always a lag between the end of a boom and people's experience of economic hardship, but by now we are surrounded by signs of economic weaknesses.

Official statistics reveal a sluggish economy. Incomes have been stagnant for the last three years, wages are no longer growing, business investment is low, levels of personal debt are rising, and over the first four months of this year employment growth has virtually stalled.

In spite of a substantial devaluation of our currency, which should in theory result in higher prices, we have had negative CPI inflation, as importers and retailers find they have to absorb cost increases in a weak market. Companies dependent on discretionary expenditure, such as airlines and department stores, are finding it particularly tough.

The boom had covered over many of our economic weaknesses, but as the saying goes, when the tide goes out you can see who has been swimming naked. Those weaknesses, most of which are interrelated, include:

Growing income and wealth disparities

The inability of our economy to provide well-paid employment for all has required public budgets to be directed away from expenditure on economically important services – education, health and infrastructure – and towards personal transfer payments. Also worsening inequality, in undermining the belief that there is a connection between contribution and reward, threatens the legitimacy of our whole economic and political system.

An inadequate response to climate change

On a per capita basis Australia is among the very highest emitters of greenhouse gases. Unless we adopt a strong response in decarbonising our industries (particularly power generation) we face the risk of countervailing duties and trade sanctions. We cannot go on subsidising our coal industry by failing to charge for environmental externalities. Also, we have to cope with the local consequences of global warming – more destructive storms, bushfires and worsening conditions for our rural industries.

Declining education standards

Our scores on the Program for International Student Assessment (PISA) reveal that we are slipping – not only relative to our competitors, but also in absolute terms. Our decline in science and mathematics has attracted most attention, but we should also remember that humanities – history, foreign languages, philosophy – contribute to a society's openness to ideas and acceptance of change.

Inadequate physical infrastructure

Our urban infrastructure – public transport, roads, water supply, sewerage – is barely keeping up with population growth. Our interstate roads and railroads are inadequate. And our internet connectivity standards relative to our competitors are falling.

High house prices and high levels of household debt

In our largest cities house prices relative to income are among the highest in the world – five to seven times median earnings. And our household debt has steadily risen from 63 per cent of disposable income in 1988 to 186 per cent this year. These are similar to the conditions that prevailed in the USA before the 2008 crash.

Dependence on a narrow range of exports to a narrow range of markets

Almost 60 per cent of our exports are of low value-added commodities. Rural products account for 14 per cent of our exports and minerals and fuels account for 45 per cent, the latter being dominated by thermal coal and iron ore. This means we are subject to the swings of the commodity cycle, which plays havoc with our exchange rate. Half of our exports are to three Asian countries (China, Japan and South Korea). By contrast most developed countries base their export competitiveness on high value-added goods and services serving worldwide markets.

A chronic deficit on our current account

Even during the mining boom, we were importing more than we were exporting, the balance being met with foreign capital inflows. As a consequence we have a very high and probably unsustainable level of foreign debt, as I pointed out in a recent New Matilda article.

We might expect these to be the issues discussed in an election campaign in which the economy is people's main concern. How will we develop an economic structure that pays good wages? How will we decarbonise our economy? How will we improve our education standards? And so on.

While these issues get the occasional mention, what passes for an economic debate has been largely about the narrow issue of fiscal management, particularly the Coalition's claims about Labor's election costings, with alarmist talk about Labor's "black holes".

This is largely a meaningless issue. As Peter Martin points out, at the end of the campaign we will find both Labor's and the Coalition's costings fit neatly within the present budget's four year estimates of the budget deficit. Both sides know the game, and using every accounting legerdemain available they play by the rules, trying to show that they are better guardians of the public purse than the other side.

Fiscal management – the control of aggregate levels of revenue and expenditure and the net budget outcome – is important, but there is much more to economic management than keeping control of the bank account.

Unfortunately, in the last three elections fiscal management has come to displace all other aspects of economic policy.

One reason is that arguments over fiscal costs provide neat numbers with an air of precision, and an impression of objectivity. As the Australian economist Peter Reuter pointed out in a seminal article in 1986, policy debates steer themselves to areas where there are numbers, no matter how flaky or inaccurate those numbers may be. In the case of budgets and election costings the numbers commentators fasten on are the estimated four-year cash outlays on programs and proposals – measures that make little distinction between once-off and ongoing outlays, and that ignore costs beyond five years.

These four-year budget "forward estimates" as they are called are simply a planning tool for cash management purposes. They are not a tool for economic assessment, which should be based on the more thorough discipline of cost-benefit analysis and studies such as those conducted by the Productivity Commission.

But in the mainstream media there is only a handful of journalists of Peter Martin's calibre who understand public economics. Most election commentary, including in the ABC, is by political journalists who are abreast of every political scandal, but who don't know the difference between fiscal and economic analysis and who easily get sucked in to the election costing debate, as if there is no other important economic issue at stake.

Also, this fiscal focus has suited the Coalition because it aligns with the narrative that Labor, in its time in office, left the Coalition to deal with a "budget mess". It's a simple message that plays on a public perception that a deficit is "bad", while a surplus is "good".

The economic reality is far more complex – a deficit is a very appropriate response to an event such as the 2008 financial crisis, and public debt is generally a responsible way to finance productive public investment. But this dumbed-down presentation of economic policy, as if economics is all about the size of the budget deficit, has undoubtedly contributed to the public perception that the Coalition is better than Labor at economic management.

The Coalition's fiscal focus goes back to 1988, when the newly-elected Howard-Costello Government legislated a "Charter of budget honesty", an initiative that looked innocuous at first sight, but which was actually cover for pushing economic policy to the sidelines and pursuing a "small government agenda. (At the time I suggested that we really needed a charter of economic honesty.)

There is still time for the electorate to turn its attention to the broad issues of economic policy, but will journalists in the mainstream media continue to be distracted by the Coalition's agenda of reducing economic policy to the accountant's craft of bookkeeping?