

ECONOMIC AND BUDGETARY ISSUES WHICH WE SHOULD – BUT PROBABLY WON'T – BE TALKING ABOUT DURING THE ELECTION CAMPAIGN

ON-LINE PRESENTATION TO THE
JOHN CURTIN INSTITUTE OF PUBLIC POLICY

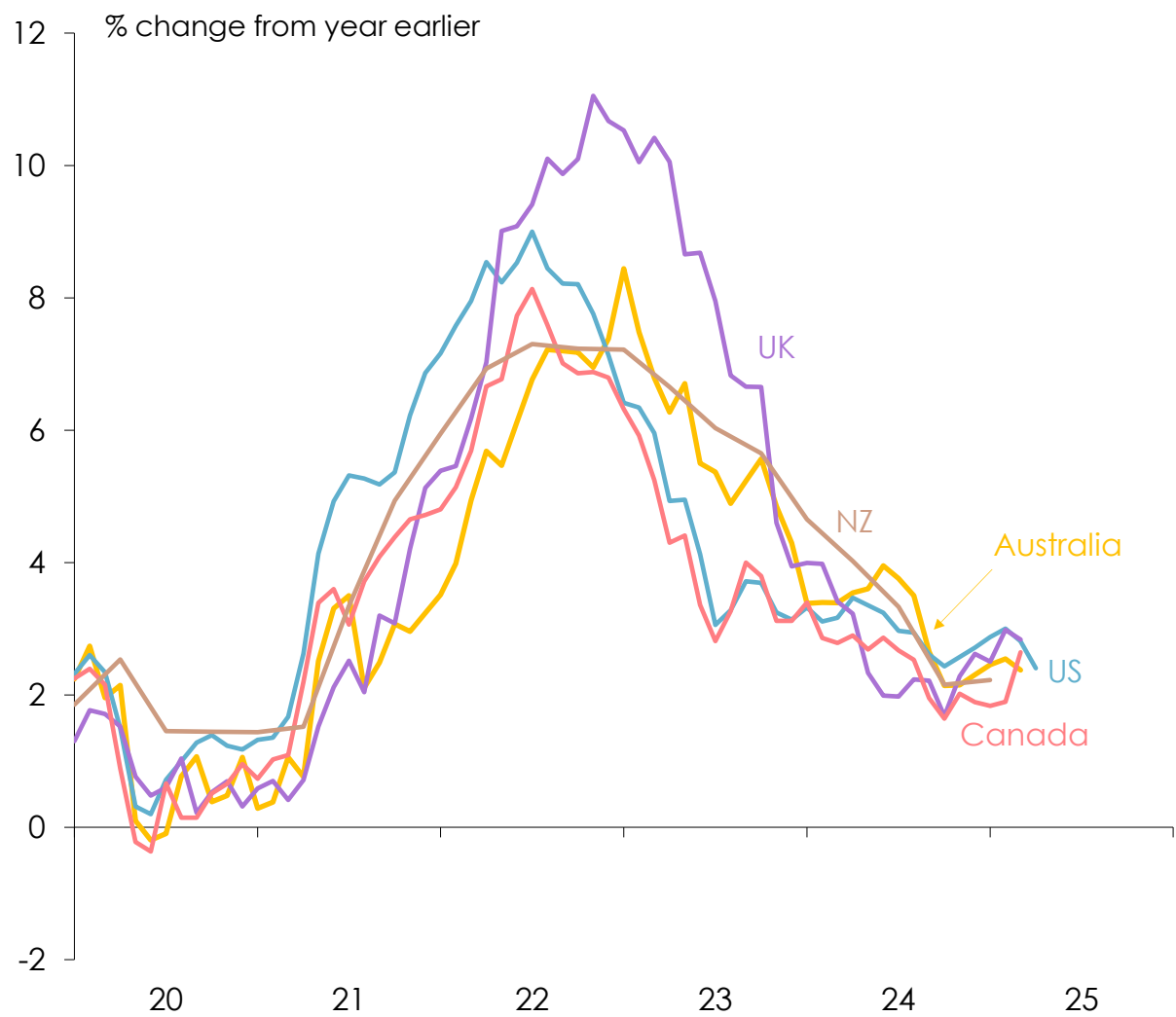
11TH APRIL 2025

SAUL ESLAKE

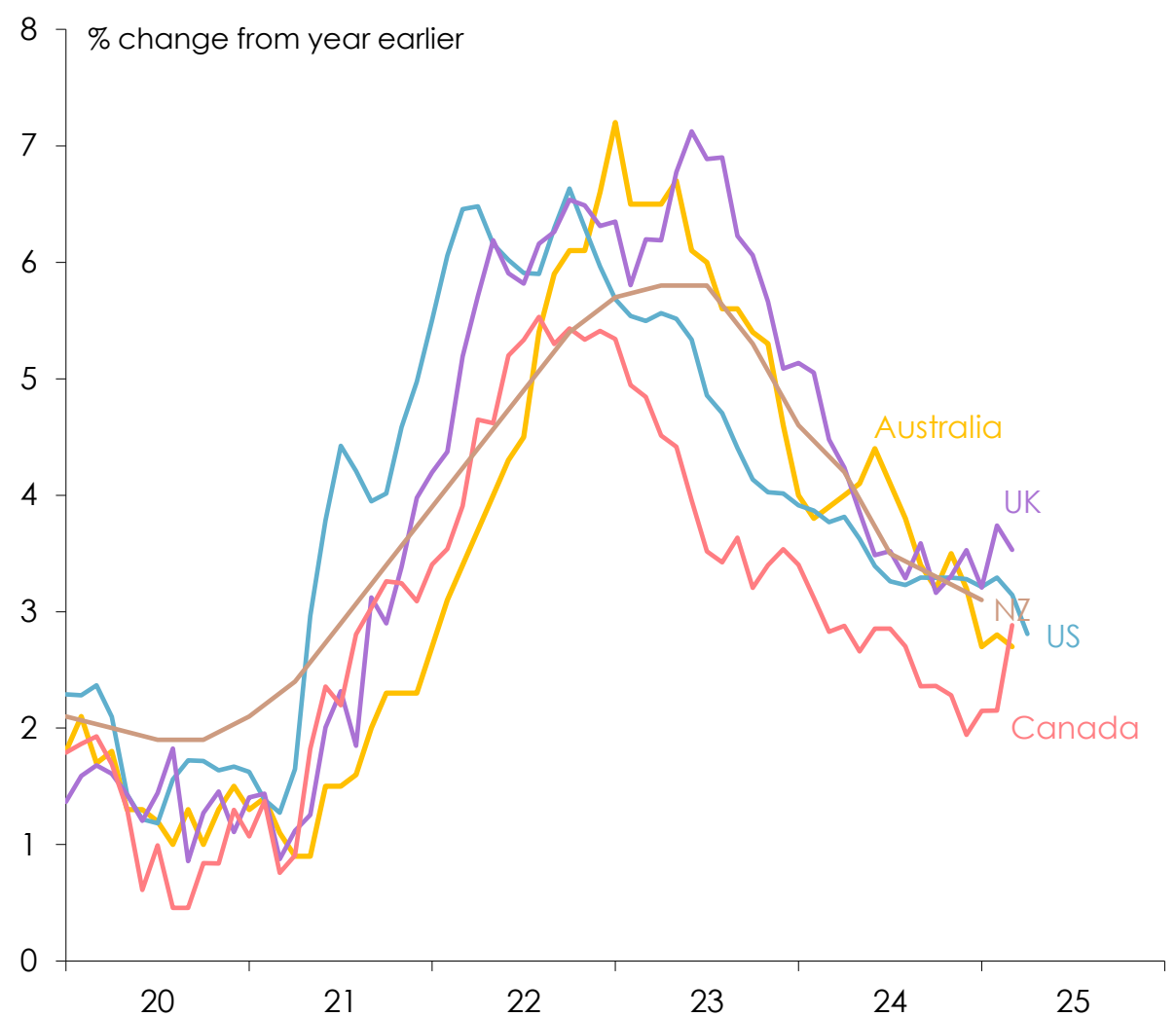
CORINNA ECONOMIC ADVISORY
INDEPENDENT ECONOMICS

'Underlying' inflation has now fallen more or less as much in Australia as it has done in most other comparable countries

'Headline' inflation



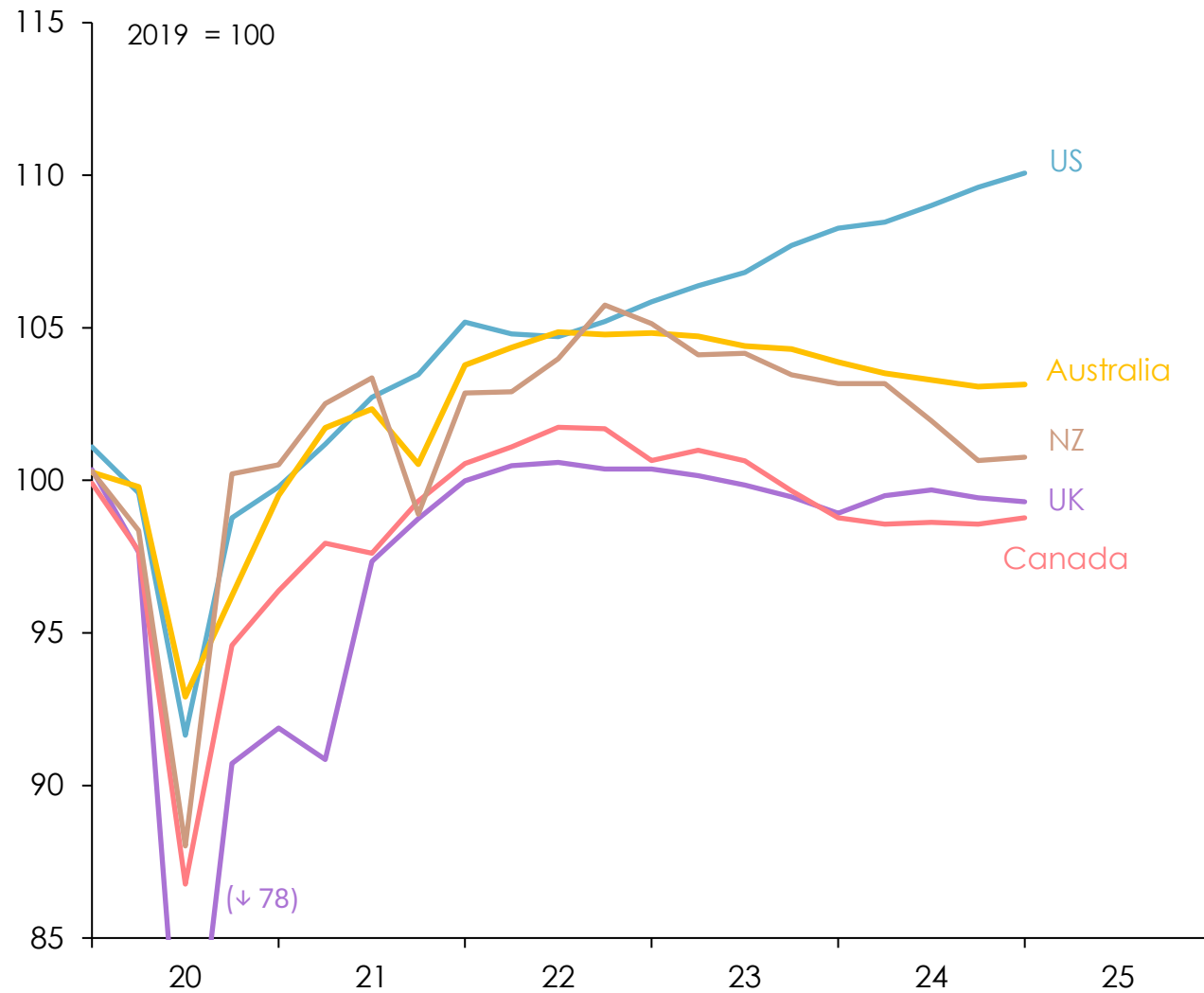
'Core' or 'underlying' inflation



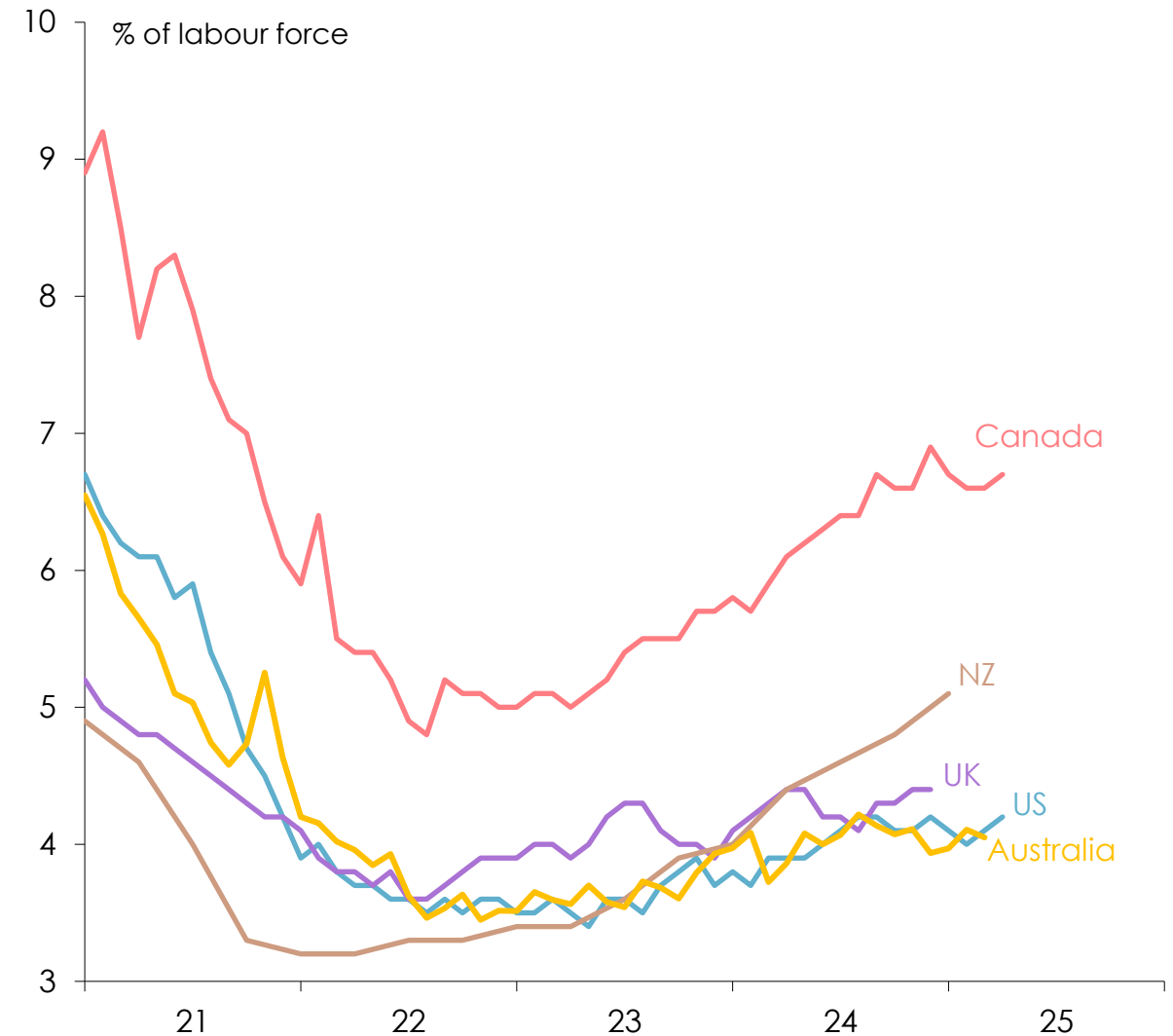
2 Note: 'Core' inflation in the US, UK and Canada is the annual change in the CPI excluding food & energy; 'underlying' inflation in Australia is the 'trimmed mean' and in NZ is derived from a statistical model. Sources: US [Bureau of Labor Statistics](#); [Statistics Canada](#); UK [Office for National Statistics](#); [ABS](#); [StatsNZ](#); [RBNZ](#).

But economic activity hasn't contracted as much in Australia as in NZ or Canada, and unemployment has risen by less than in the US or UK

Real per capita gross domestic product

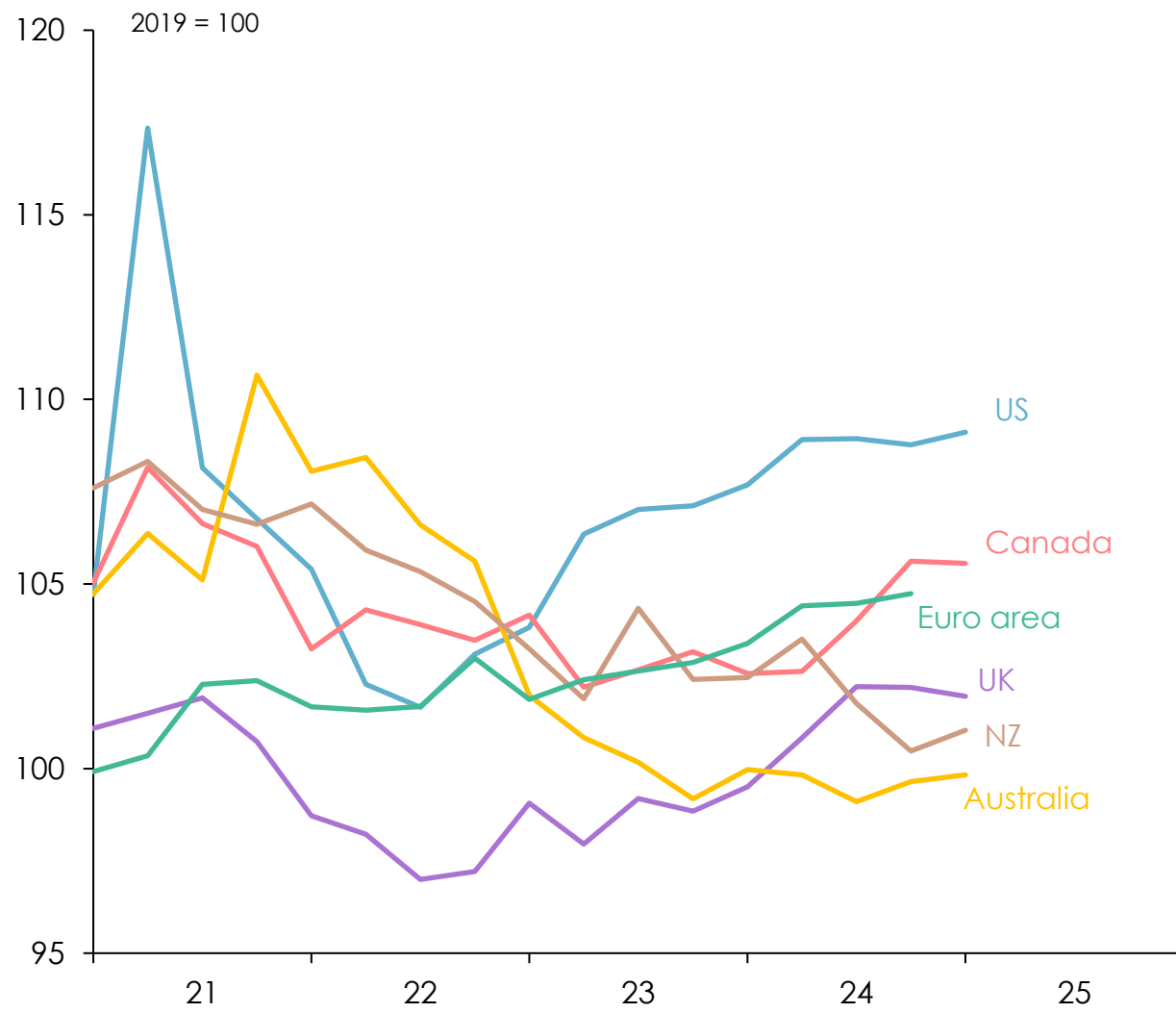


Unemployment rates

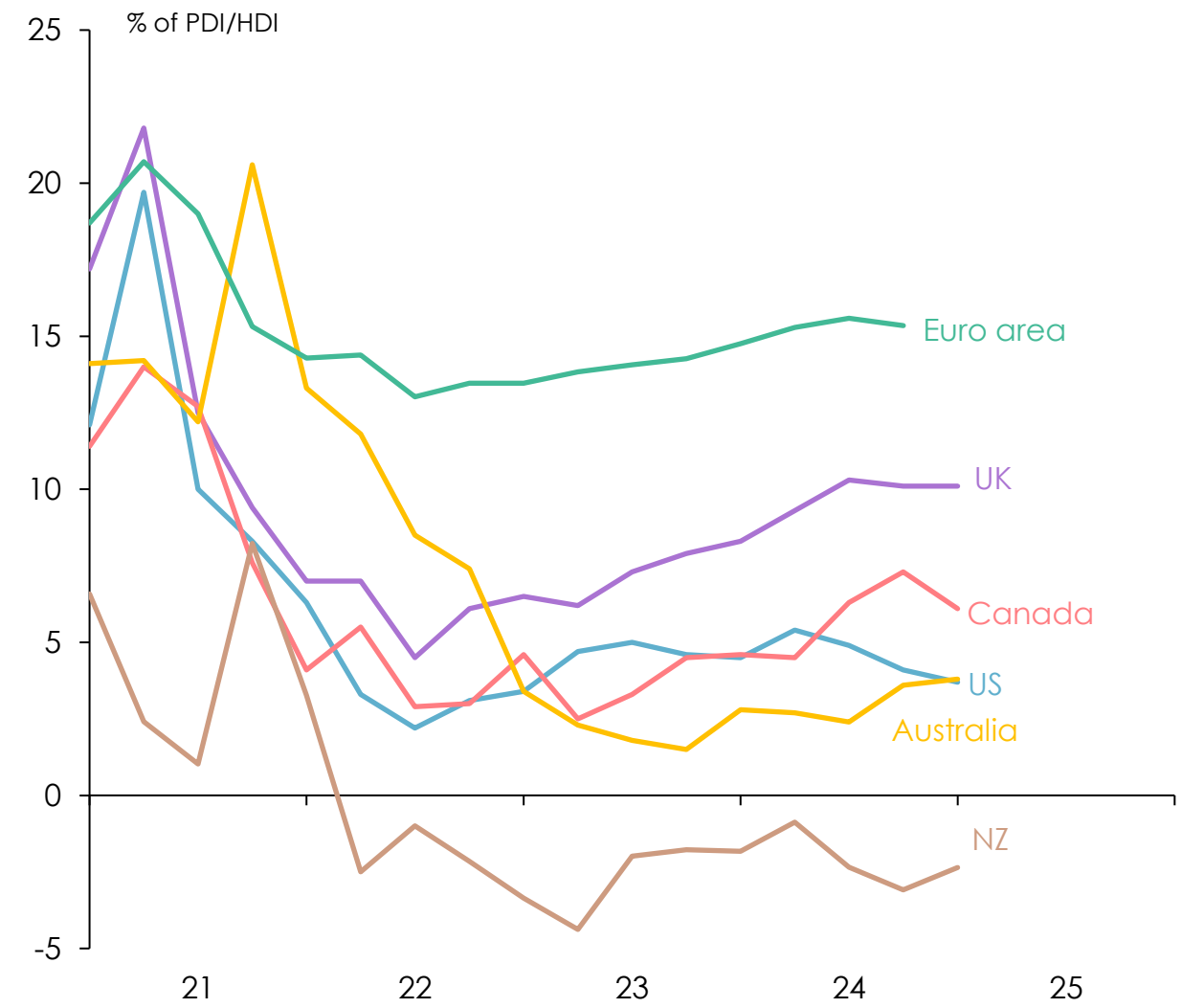


Although household finances have been squeezed more tightly in Australia than in other comparable countries

Real per capita household disposable income

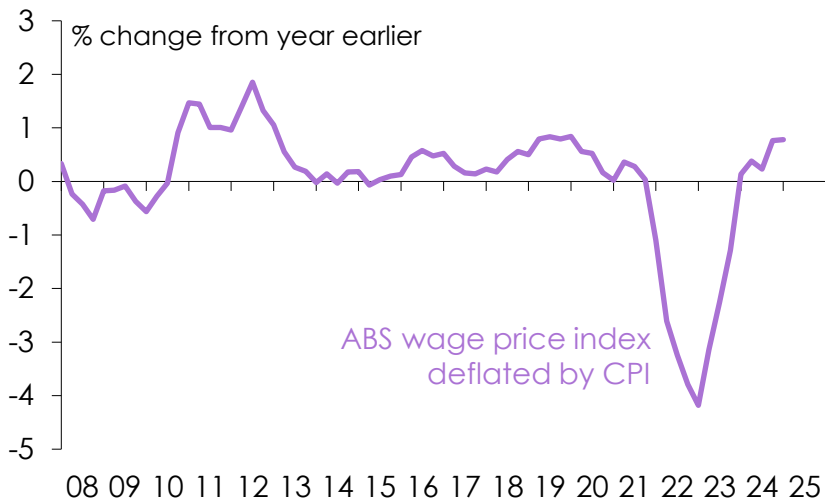


Household saving rates

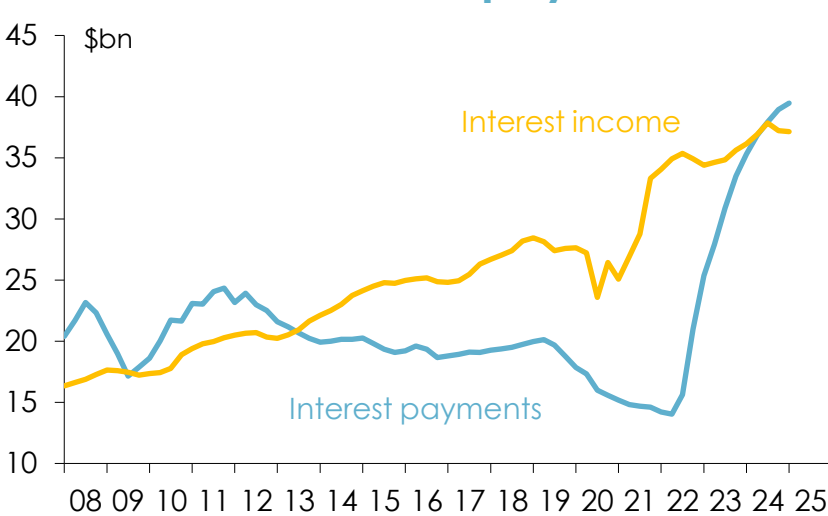


The squeeze on household finances is starting to ease

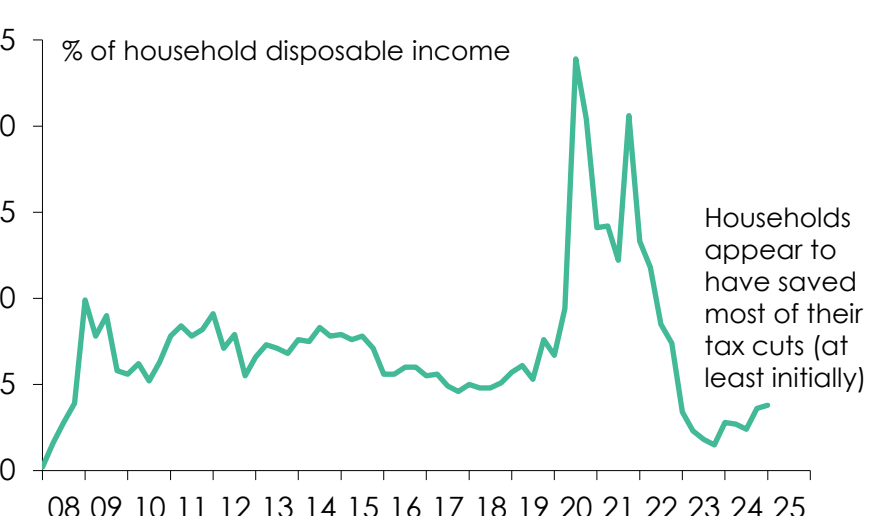
Real wages



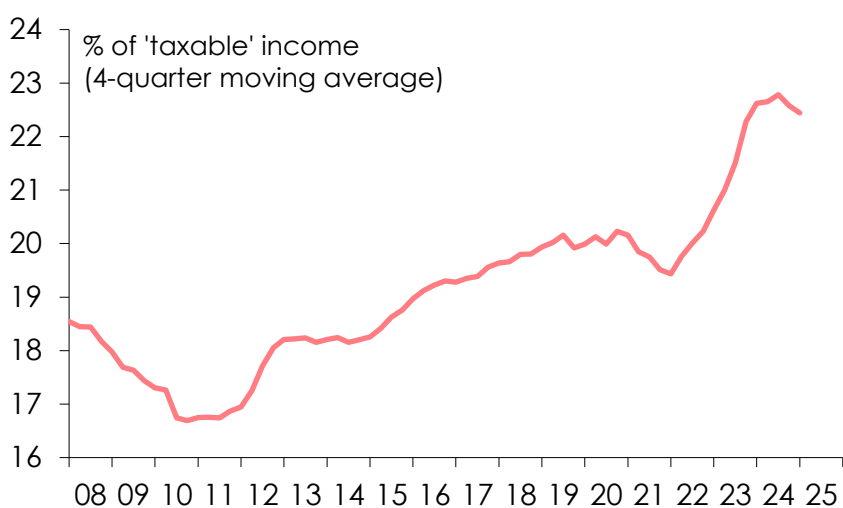
Interest income and payments



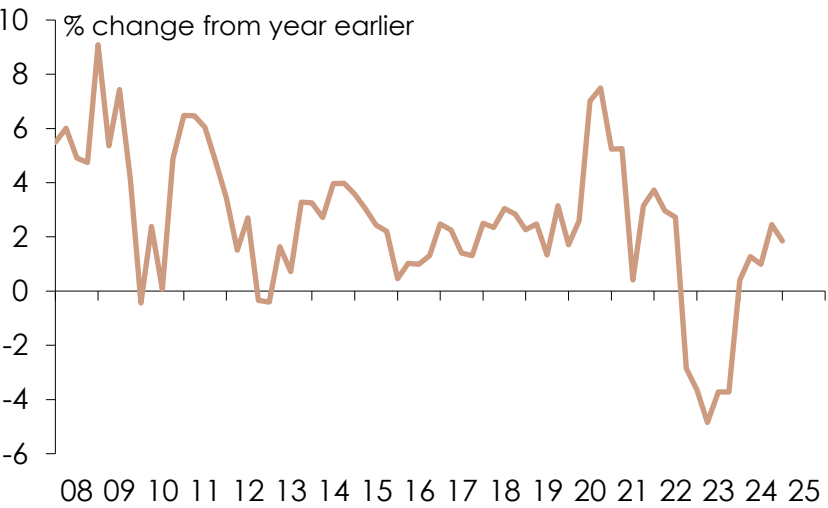
Household saving



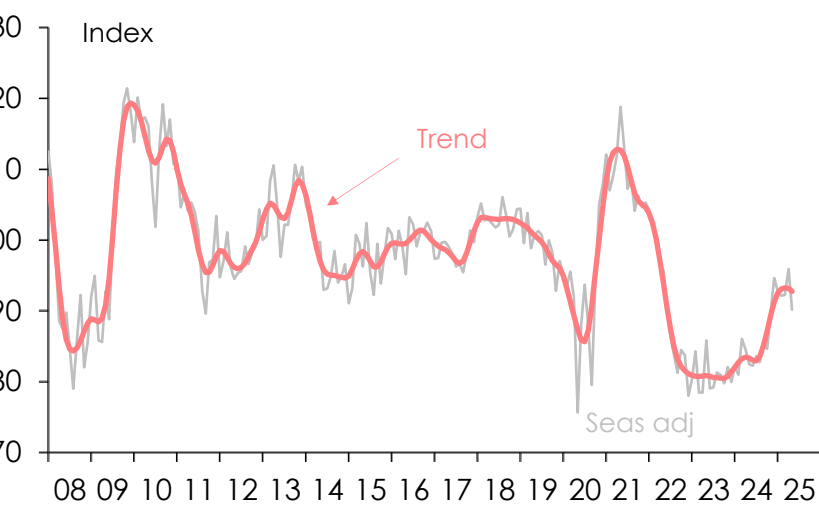
Personal income tax payments



Real household disposable income



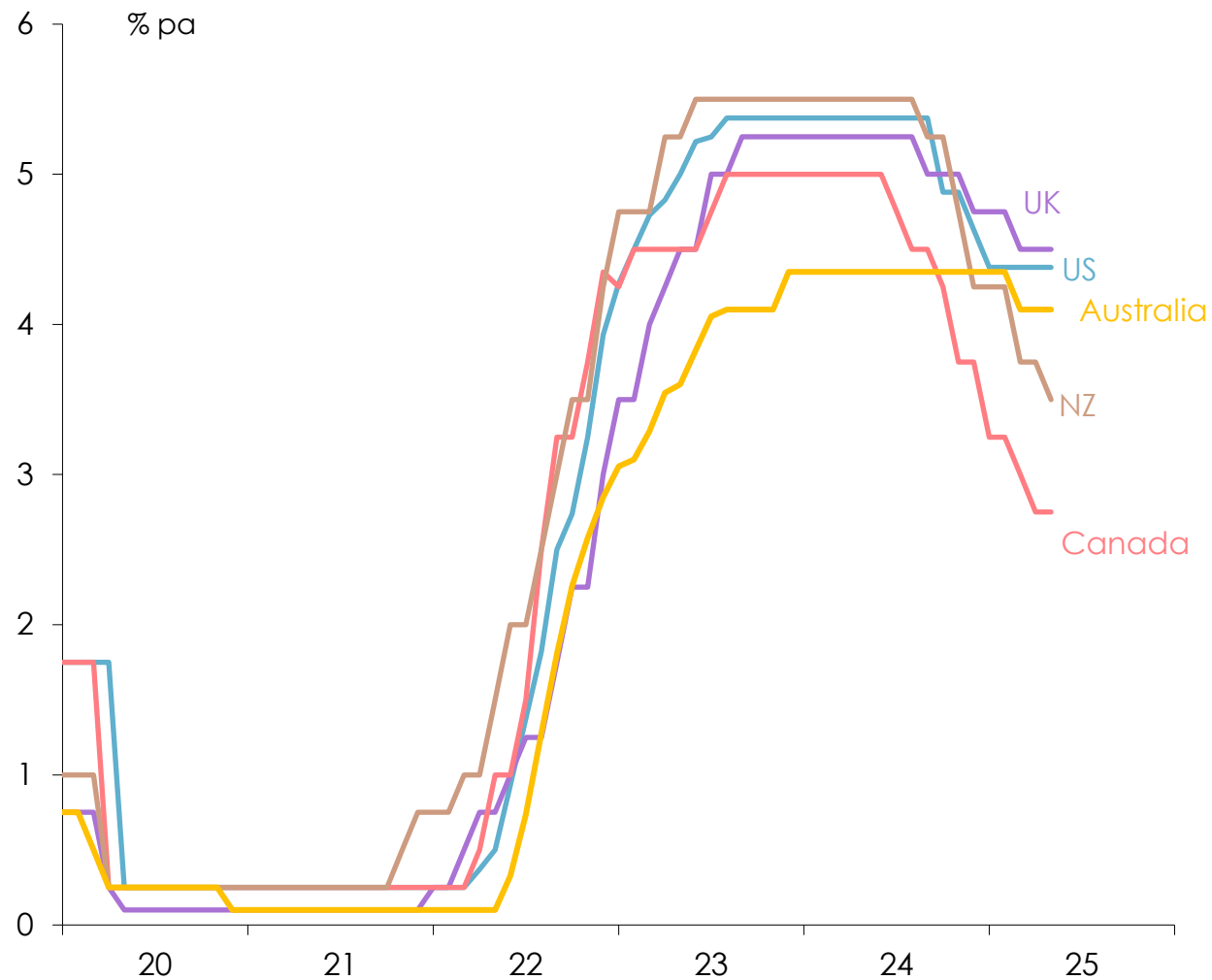
Consumer confidence



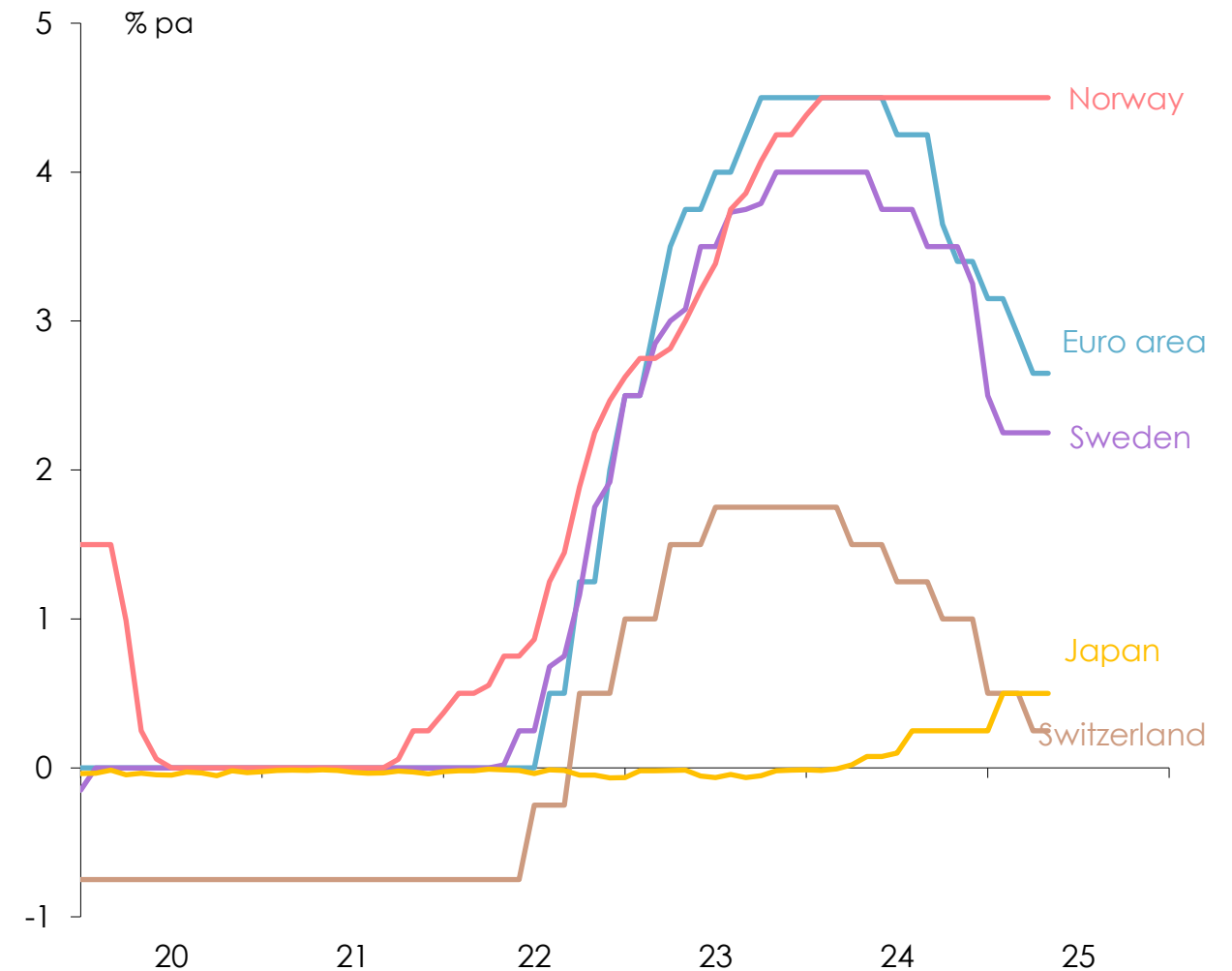
Sources: ABS, [Wage Price Index](#), December quarter 2024, [Consumer Price Index](#), December quarter 2024 and [Australian National Accounts: National Income, Expenditure and Product](#), December quarter 2024; Westpac, [Westpac-MI Consumer Sentiment](#), April 2025.

The RBA was later to start lifting rates, and lifted them by less, than its peers – so it has been slower to start cutting rates, and will cut them by less

Monetary policy interest rates – Australia and comparable countries



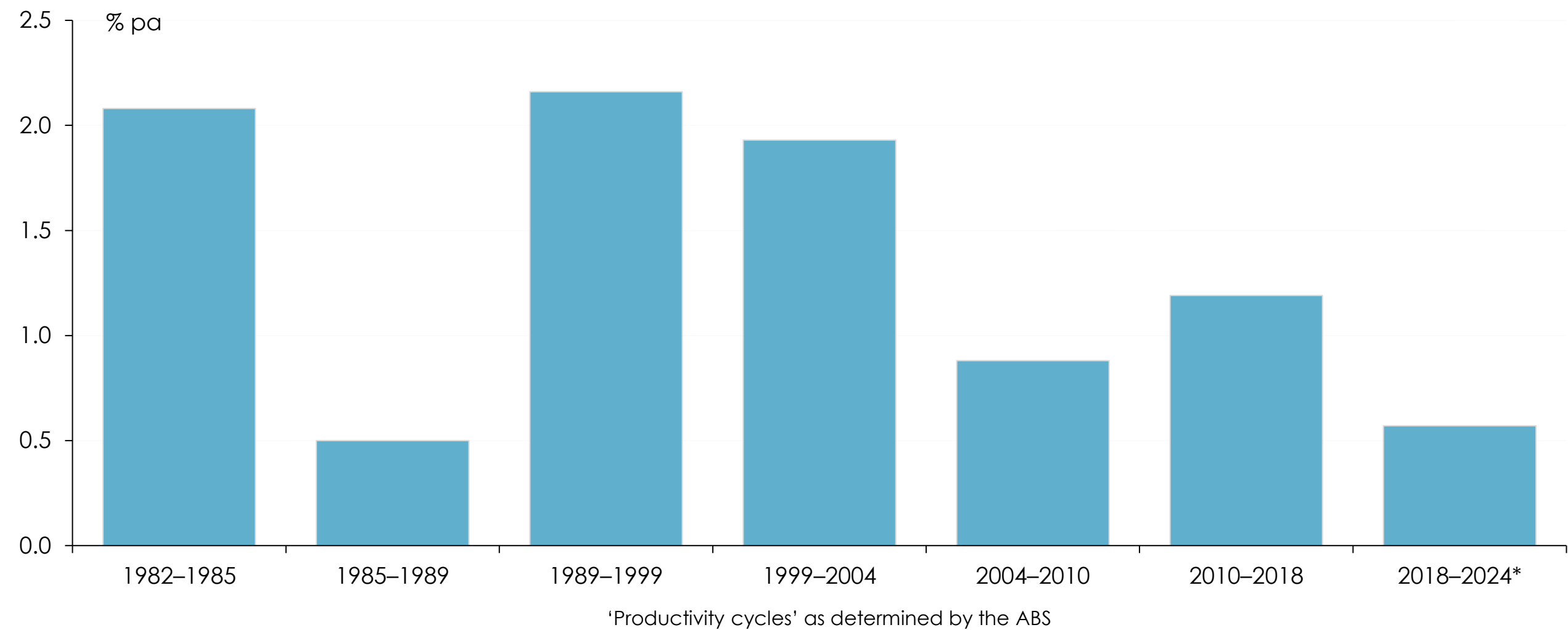
Monetary policy interest rates – Europe and Japan



Sources: US [Federal Reserve](#); [Bank of Canada](#); [European Central Bank](#); [Bank of England](#); [Reserve Bank of Australia](#); [Reserve Bank of New Zealand](#); [European Central Bank](#); [Sveriges Riksbank](#); [Norges Bank](#); [Schweizerische Nationalbank](#); [Bank of Japan](#).

Australian labour productivity growth has slowed significantly over the past two decades

Australian 'market sector' labour productivity growth, 1981-82 to 2023-24

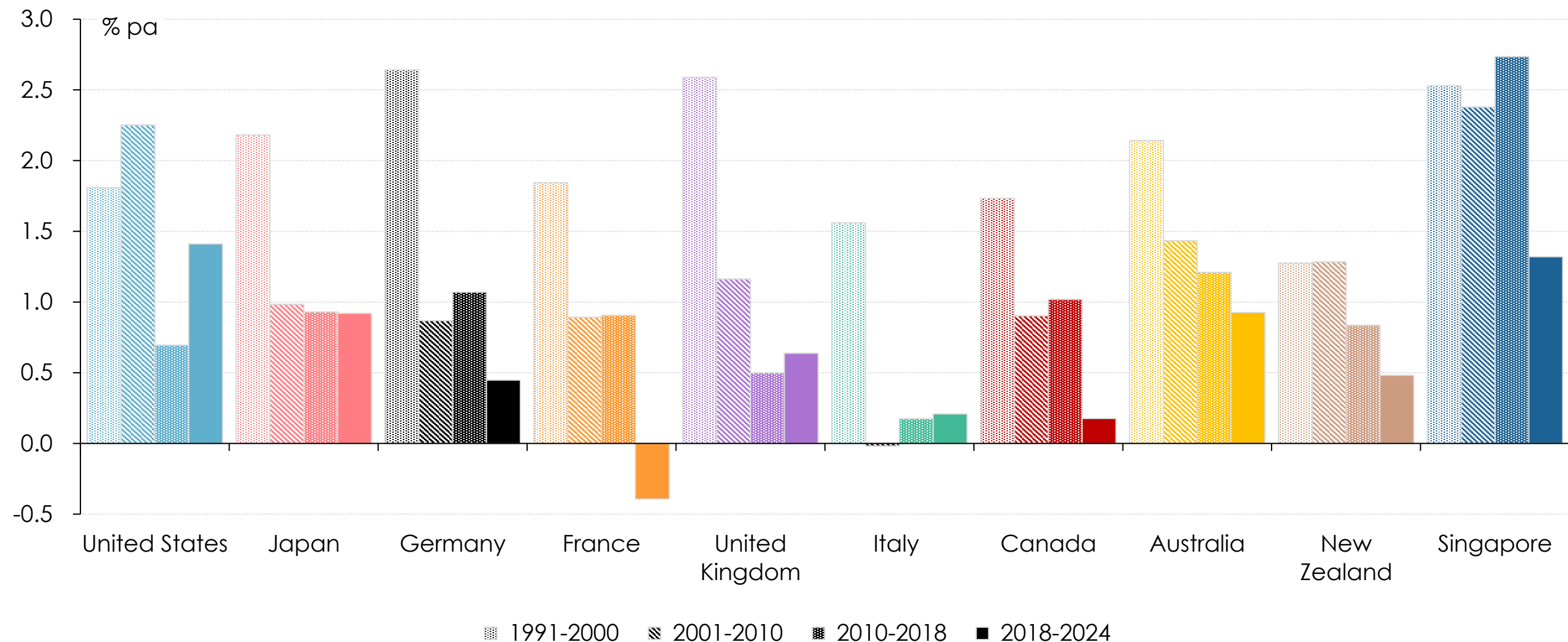


Note: The 'market sector' excludes public administration & defence, education & training, health care & social assistance and ownership of dwellings. 2018-2024 is an incomplete productivity cycle.

Sources: Australian Treasury, [2023 Intergenerational Report](#), August 2023; ABS, [Australian System of National Accounts](#), 2023-24, October 2024, Table 13.

Australia's productivity experience is by no means unique – most 'advanced' economies except the US have had a similar slowdown

Labour productivity growth, selected 'advanced' economies, 1990-2024

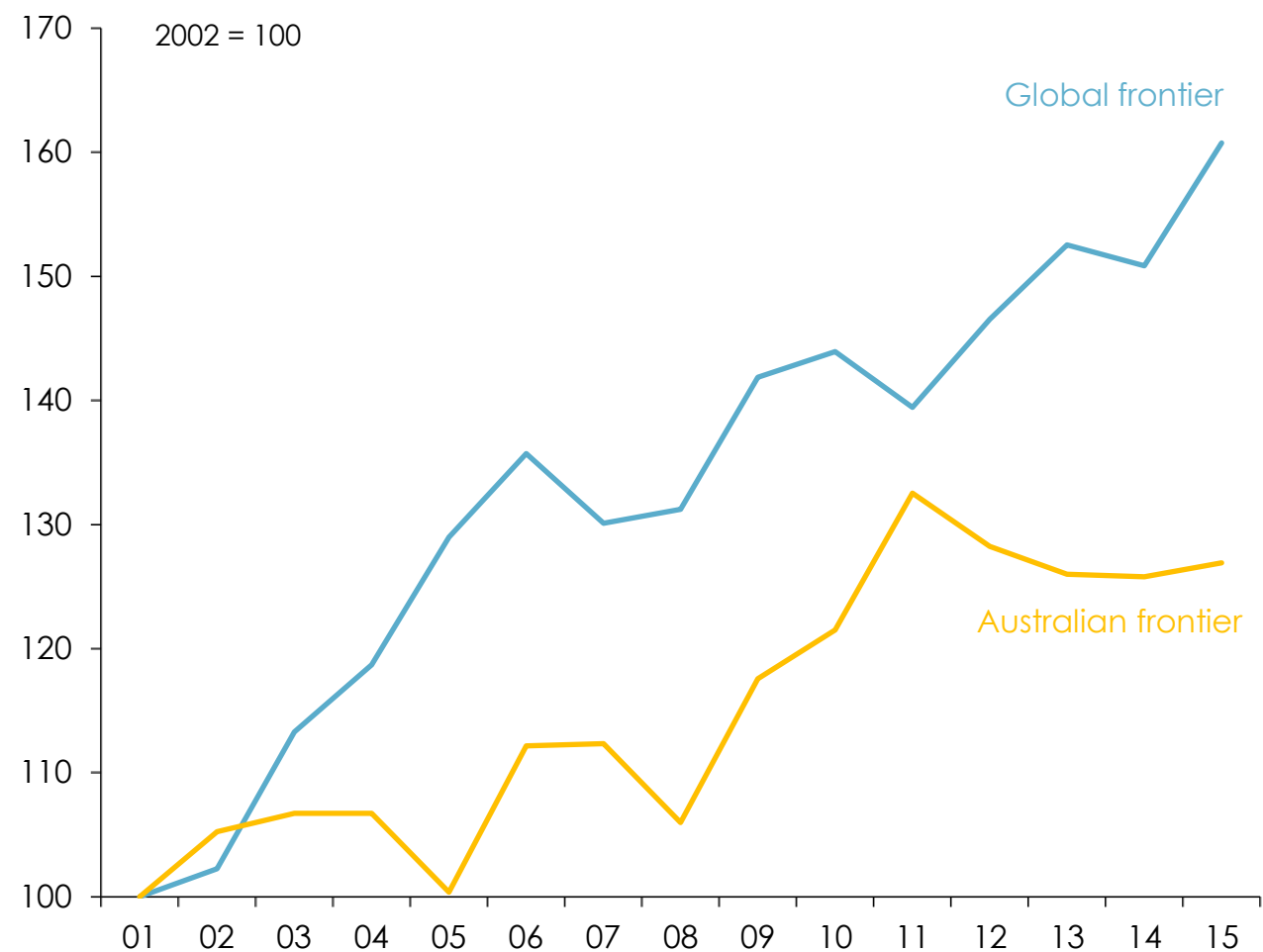


Note: 'Labour productivity' here is GDP (in 2022 US dollars at purchasing power parity exchange rates) per hour worked.
Sources: The Conference Board, [Total Economy Database](#), May 2024; Corinna.

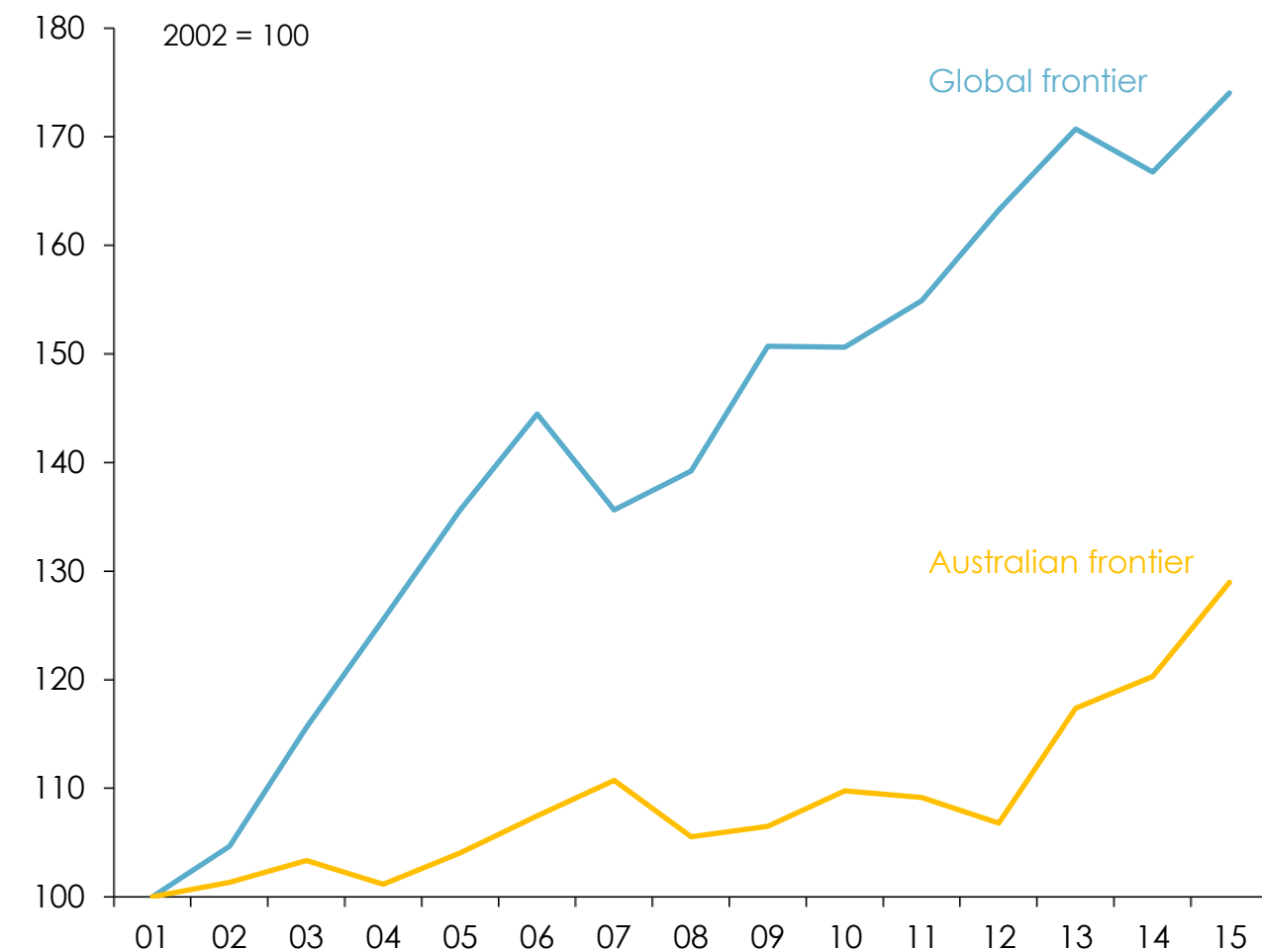
Australian firms have been slower than world-leading firms in adopting innovative technology or organizational methods

Cumulative growth in labour productivity at Australian and global 'frontier' firms

Manufacturing



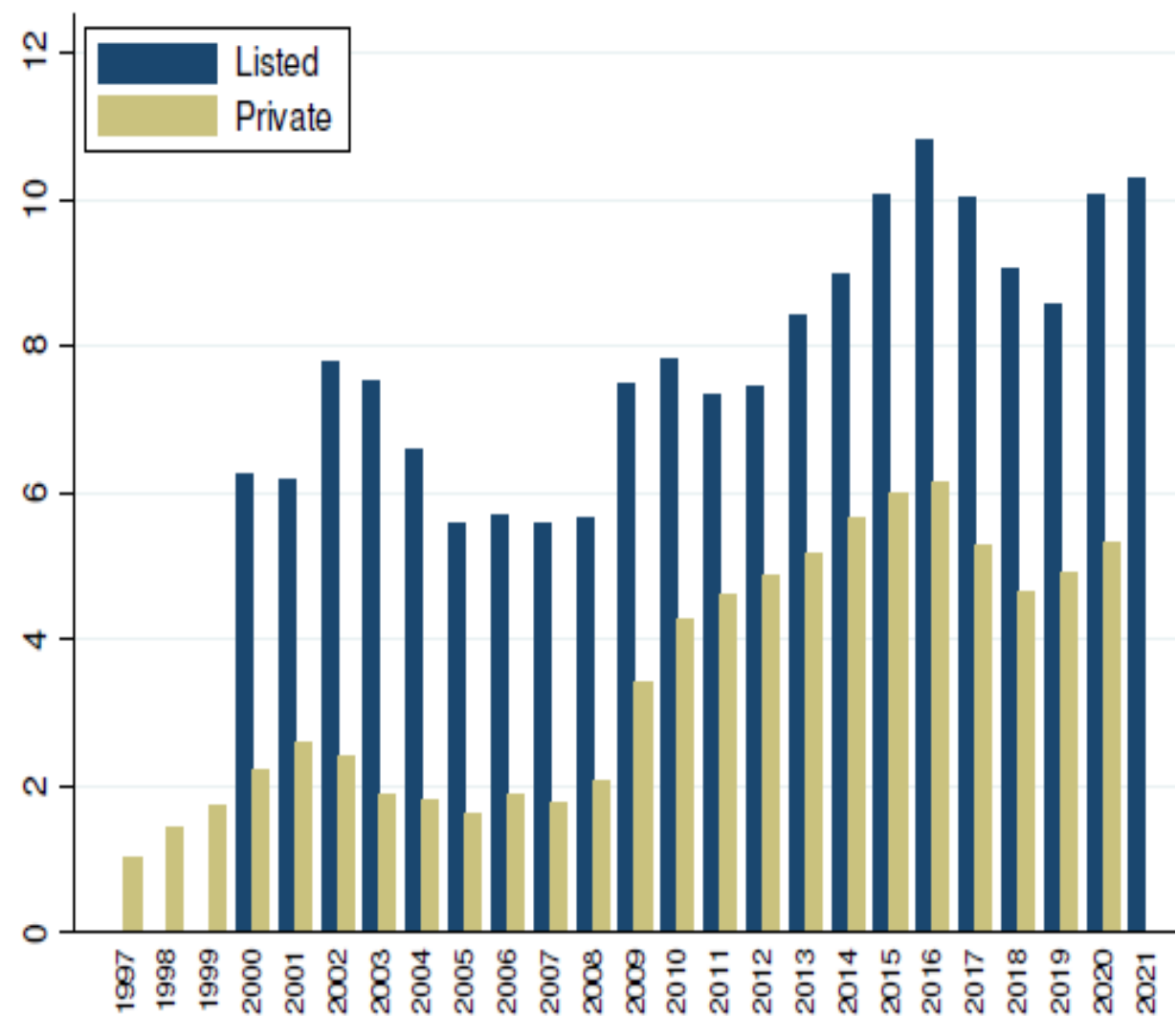
Services



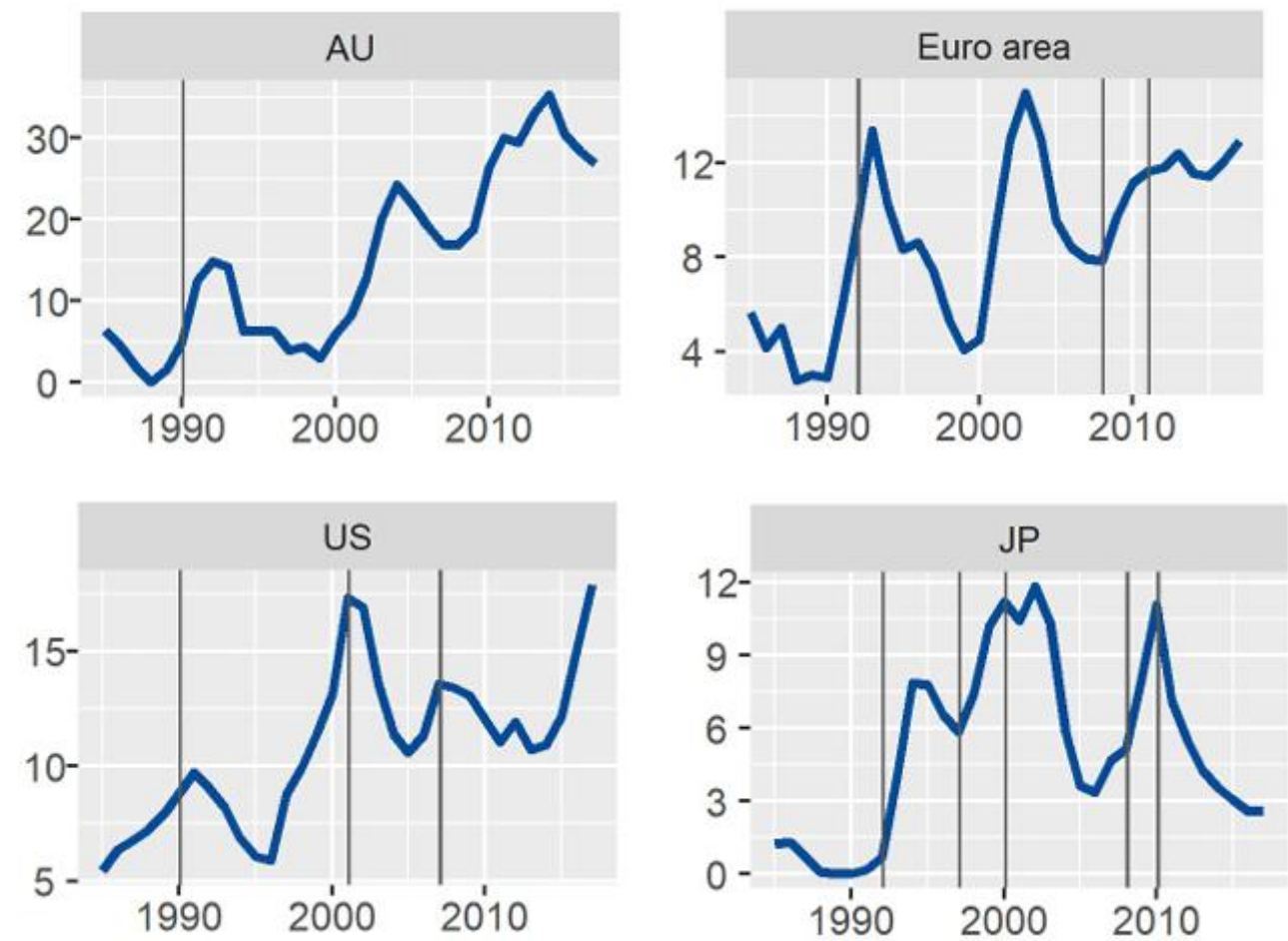
Sources: Dan Andrews, Jonathan Hambur, David Hansell and Angus Wheeler, [Reaching for the Stars: Australian Firms and the Global Productivity Frontier](#), Australian Treasury Working Paper No. 2022-01, January 2022; Aruna Sathanapally, Sam Bennett, Peter Breadon, Brendan Coates, Jordana Hunter, Tony Wood and Kate Griffiths, [Orange Book 2025: Policy priorities for the federal government](#), Grattan Institute, March 2025.

Another global factor has been the proliferation of ‘zombie firms’

Global share of ‘zombie firms’



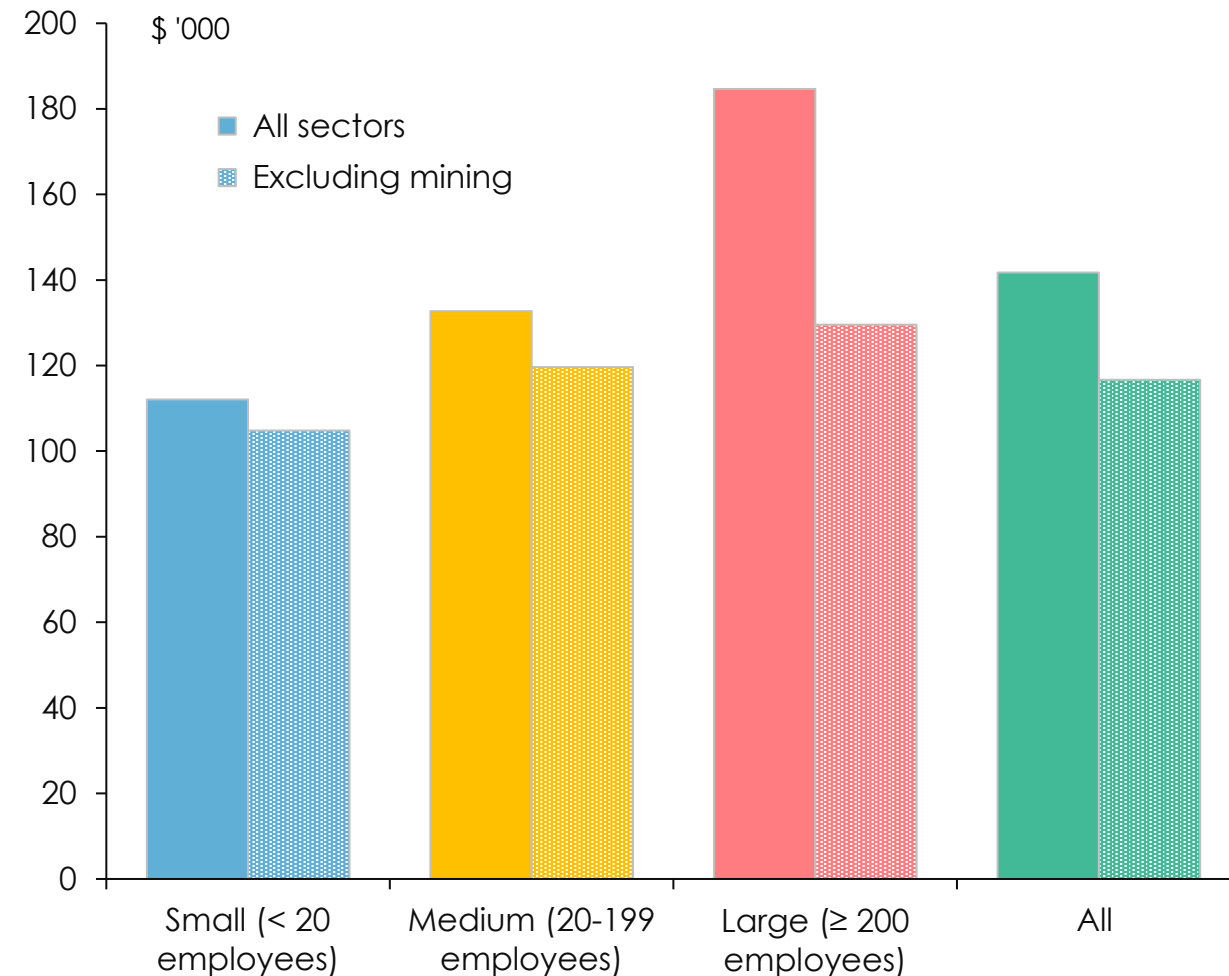
‘Zombie firms’ share in selected economies



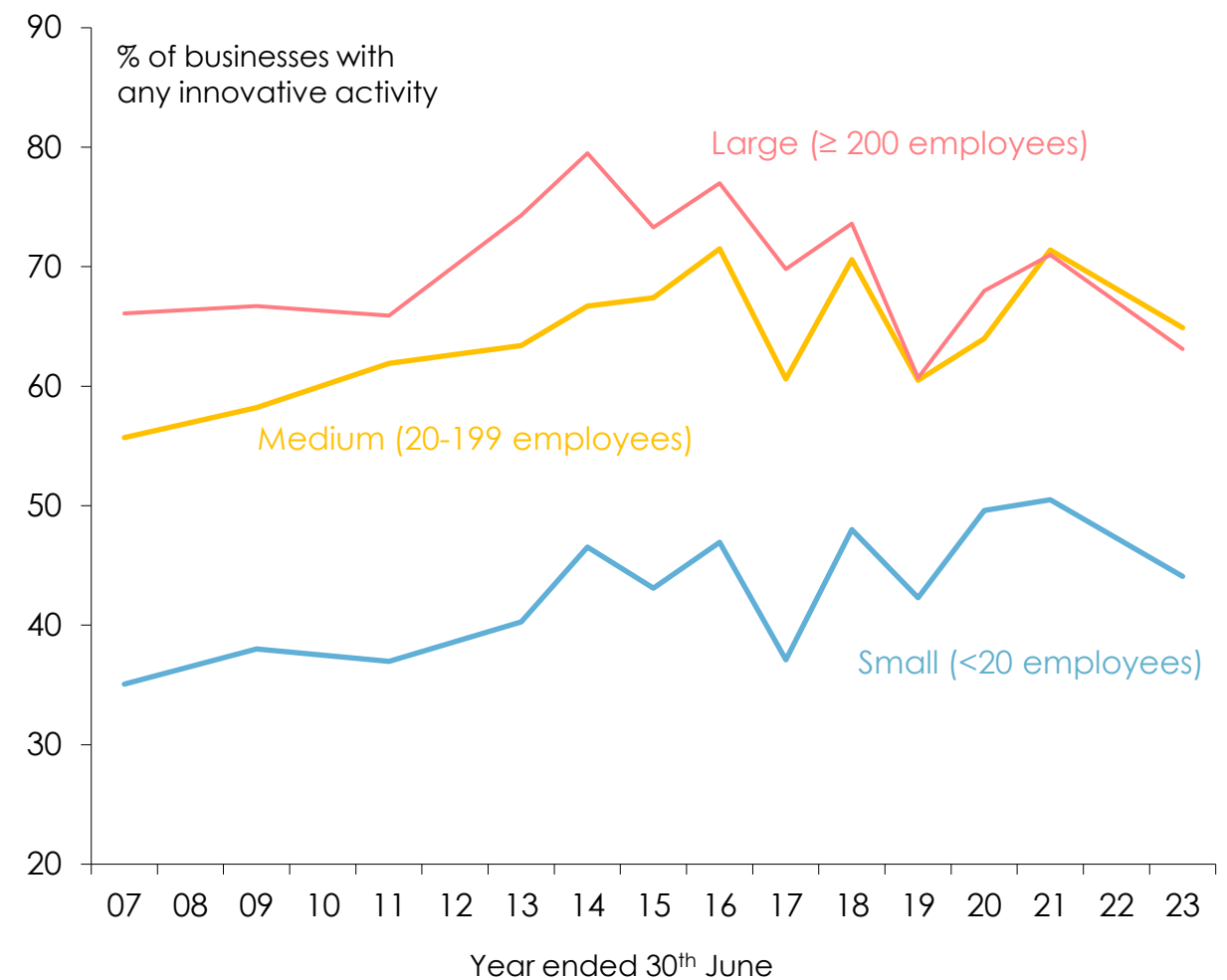
Note: ‘zombie’ firms are those with an interest coverage ratio of less than 1, and a leverage ratio above the median for the firm’s industry. Data sourced from S&P Compustat (for listed firms) and ORBIS for private firms. Sources: Bruno Albuquerque and Roshan Iyer, *The Rise of the Walking Dead: Zombie Firms Around the World*, IMF Working Paper No. 125, November 2023; and Ryan Banerjee and Boris Hofmann, *Corporate zombies: Anatomy and life cycle*, BIS Working Paper No. 882, January 2022.

Australian 'small business fetishism' is bad for productivity, because productivity in small business is 21% below the average for all businesses

Gross value added per person employed, by business size, 2022-23



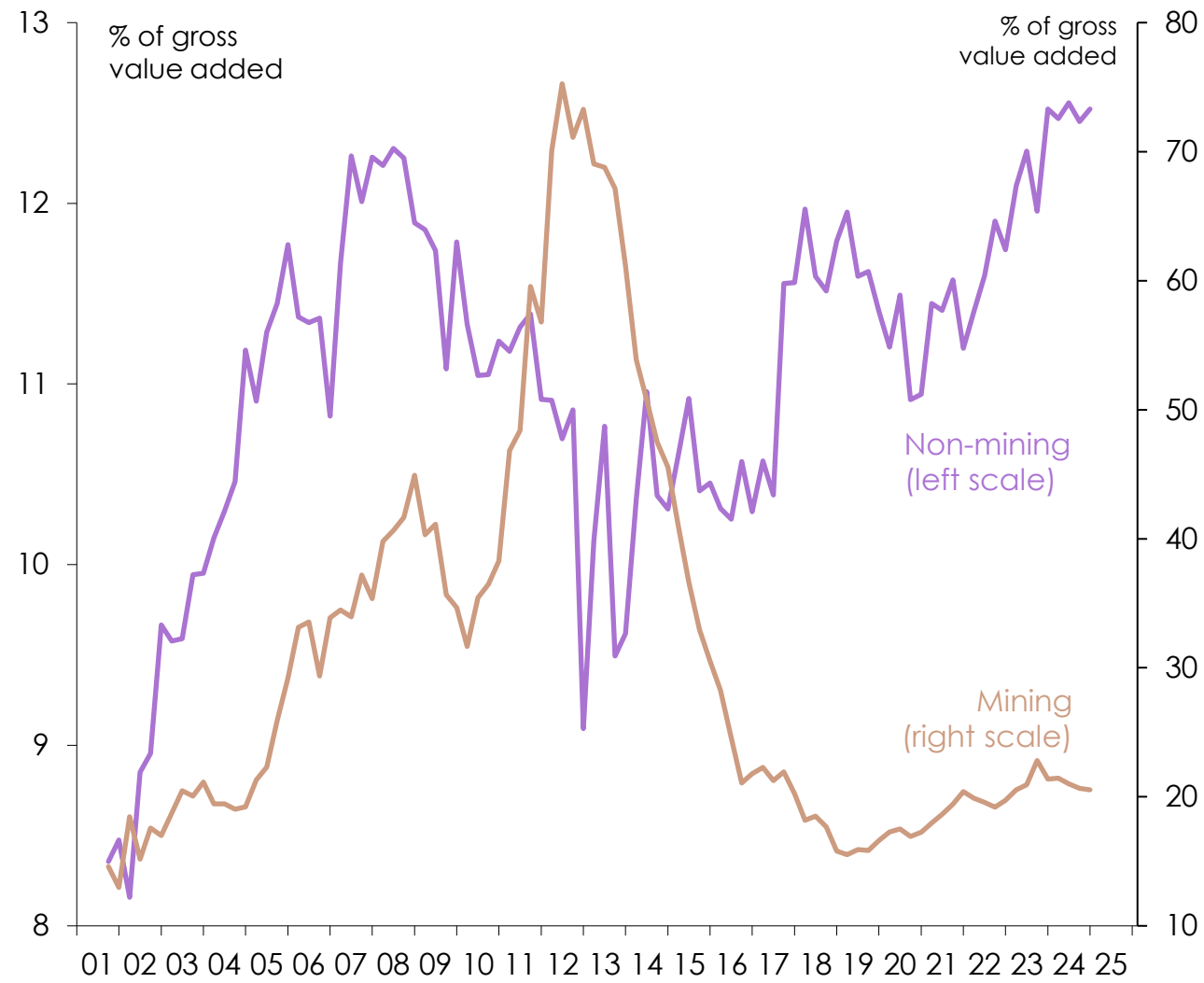
Business innovation, by business size, 2006-07 through 2022-23



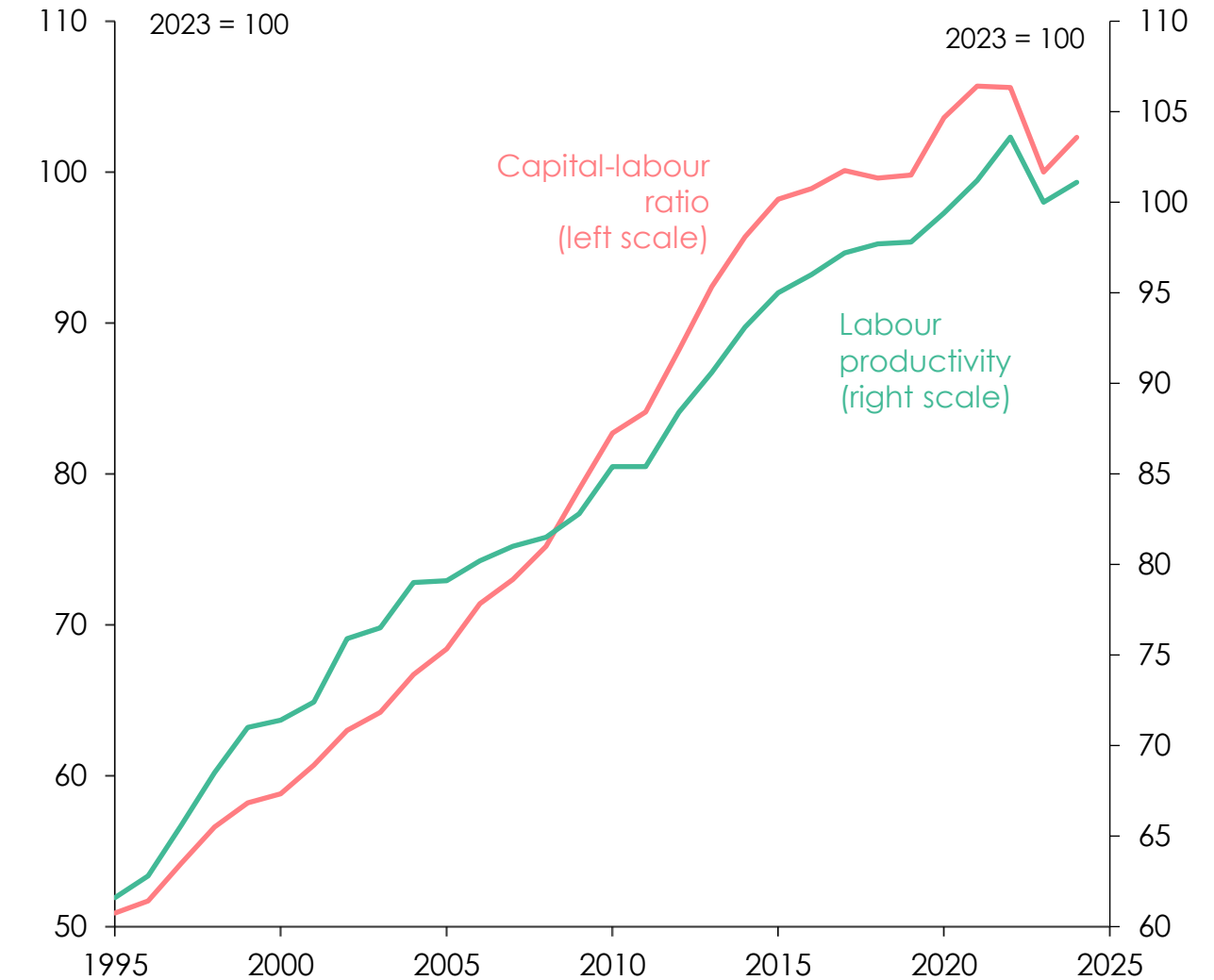
Sources: ABS, [Australian Industry](#), 2022-23 financial year, and [Innovation in Australian Business](#), 2022-23 financial year.

A decline in business investment after the GFC has almost certainly contributed to the slowdown in Australian productivity growth

Business investment

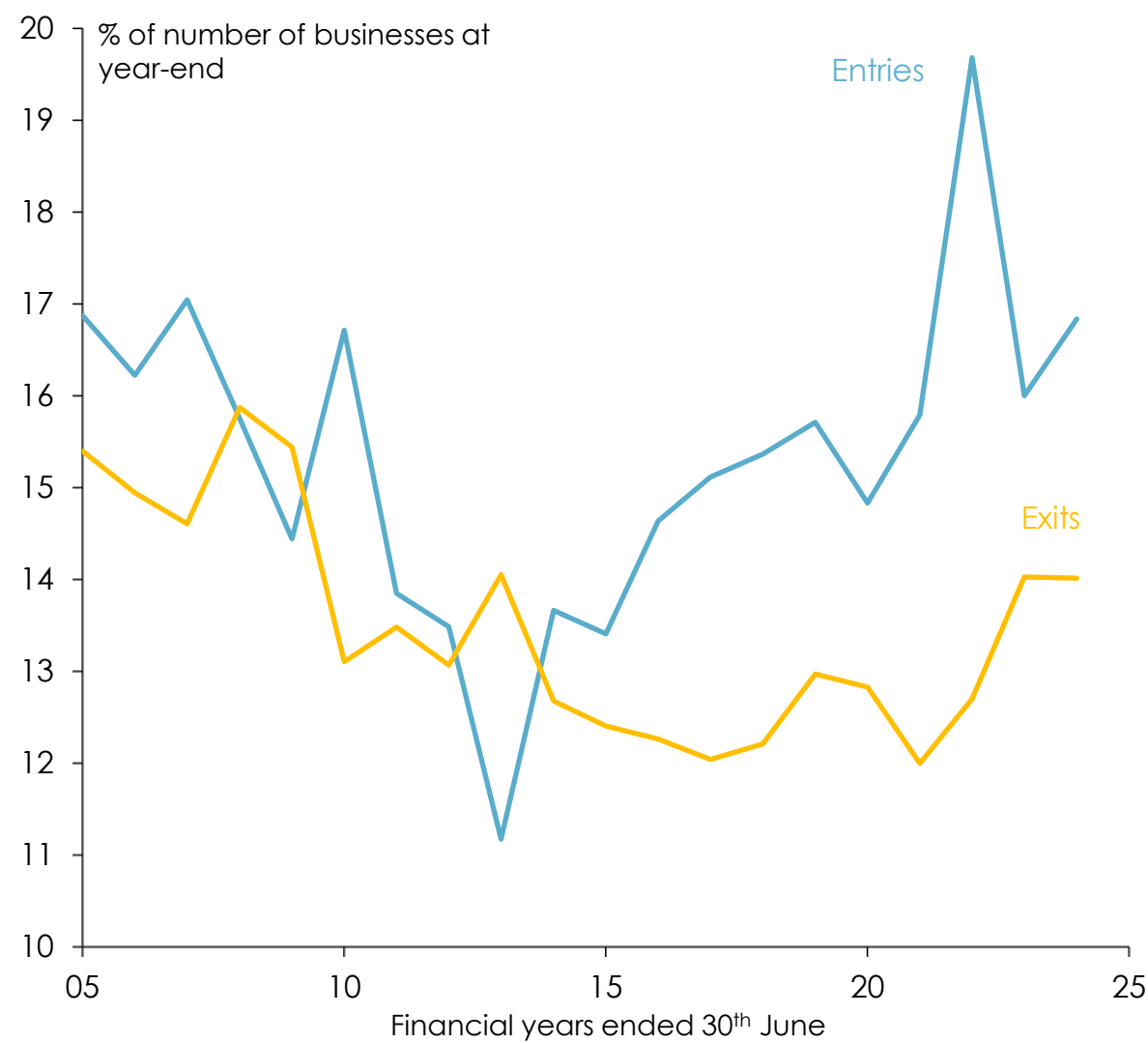


Capital-labour ratio and labour productivity

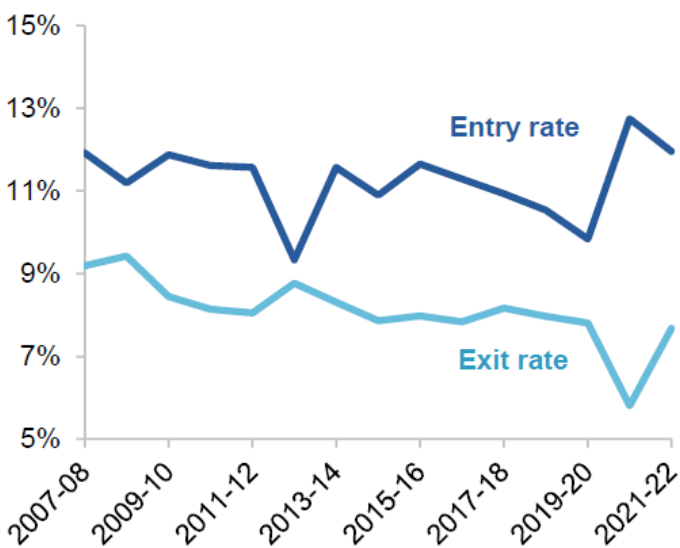


A decline in ‘business dynamism’ has also likely contributed to the slowdown in Australian productivity growth

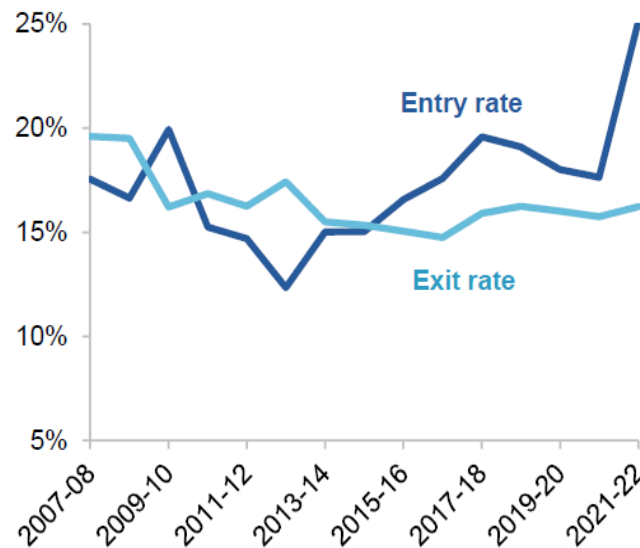
Business entries and exits



Employing businesses



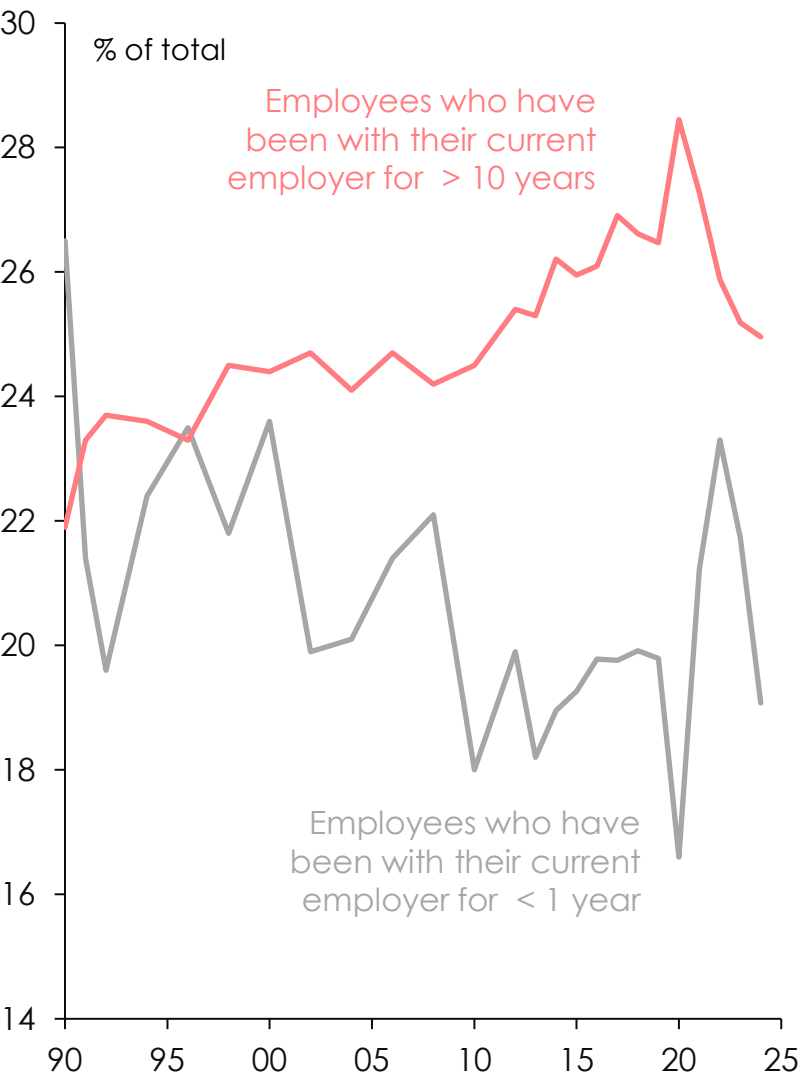
Non-employing businesses



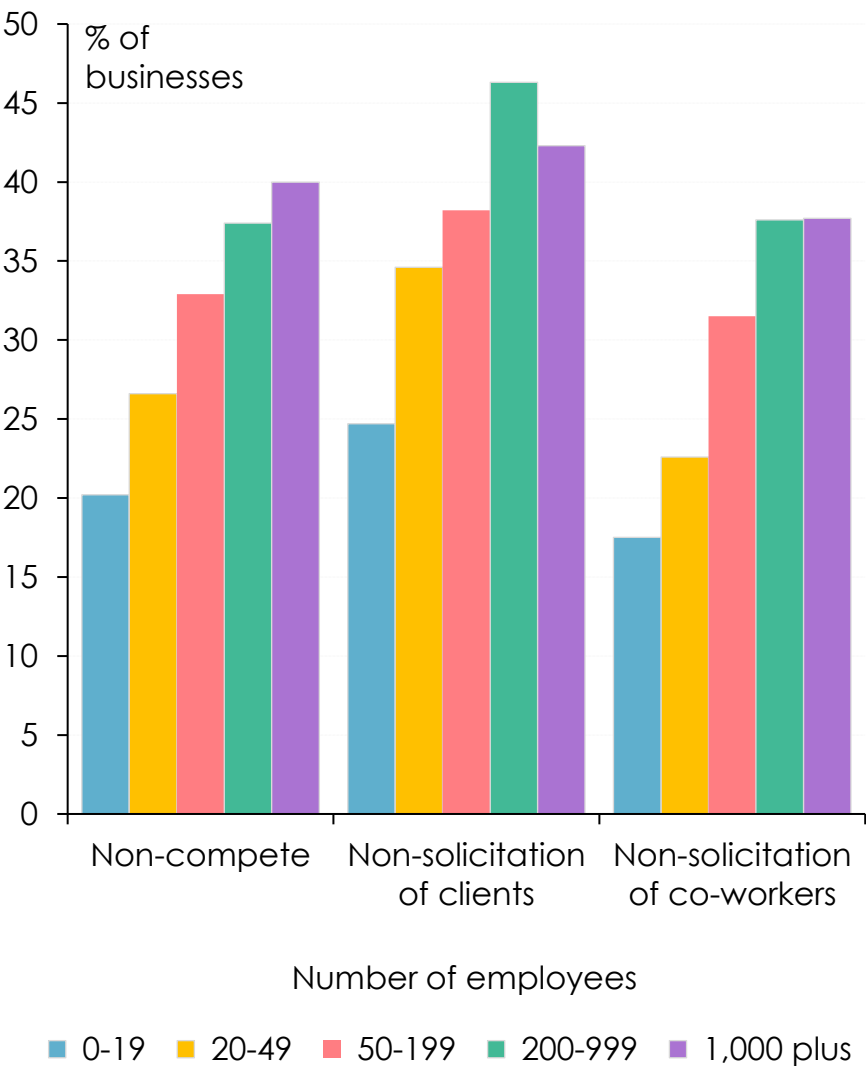
Sources: ABS, [Counts of Australian Businesses, including Entries and Exits](#), July 2020-June 2024; Productivity Commission, [Submission to the Inquiry into Promoting Economic Dynamism, Competition and Business Formation](#), House of Representatives Standing Committee on Economics, March 2023.

'Job-switching' in Australia has declined – possibly as a result of the proliferation of non-compete clauses in employment contracts

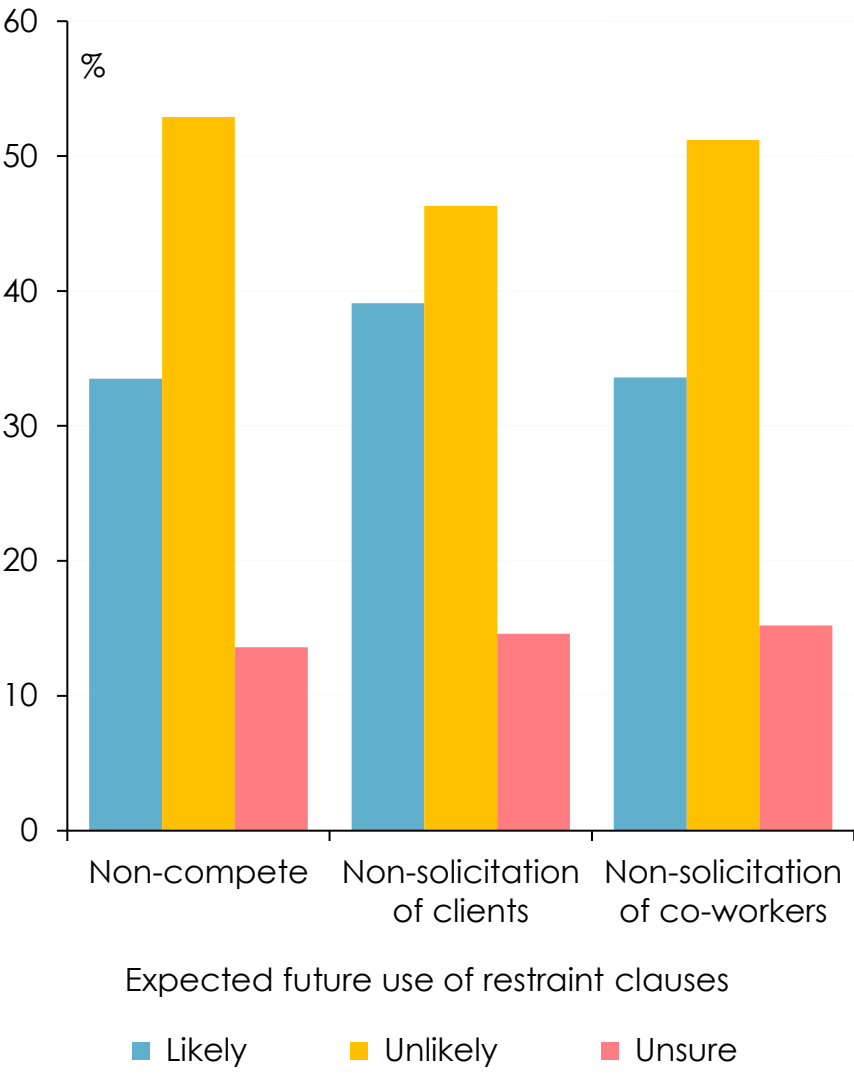
Employee tenure



Use of 'restraint clauses'



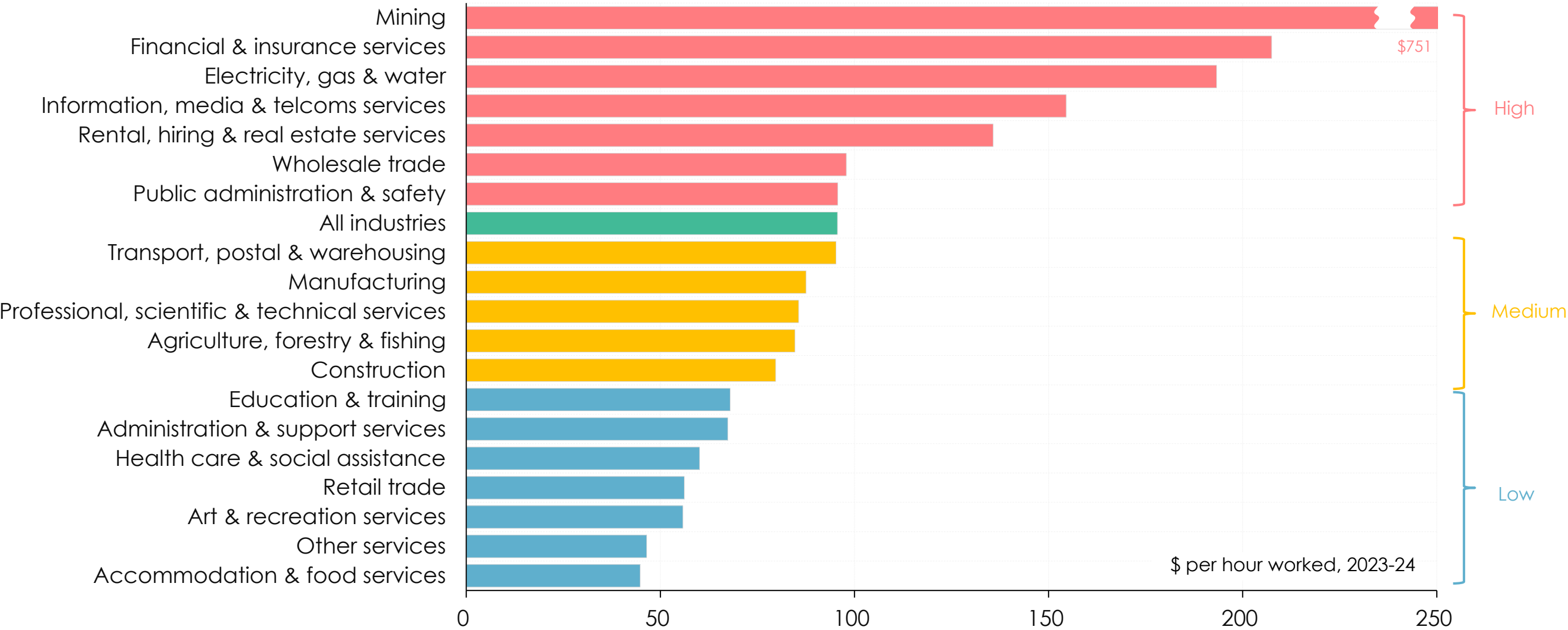
Future use of 'restraint clauses'



Sources: ABS, [Labour Force, Australia, Detailed](#), January 2024; and [Restraint Clauses](#), 2023 (note data shown here excludes 'non-disclosure' restraint clauses).

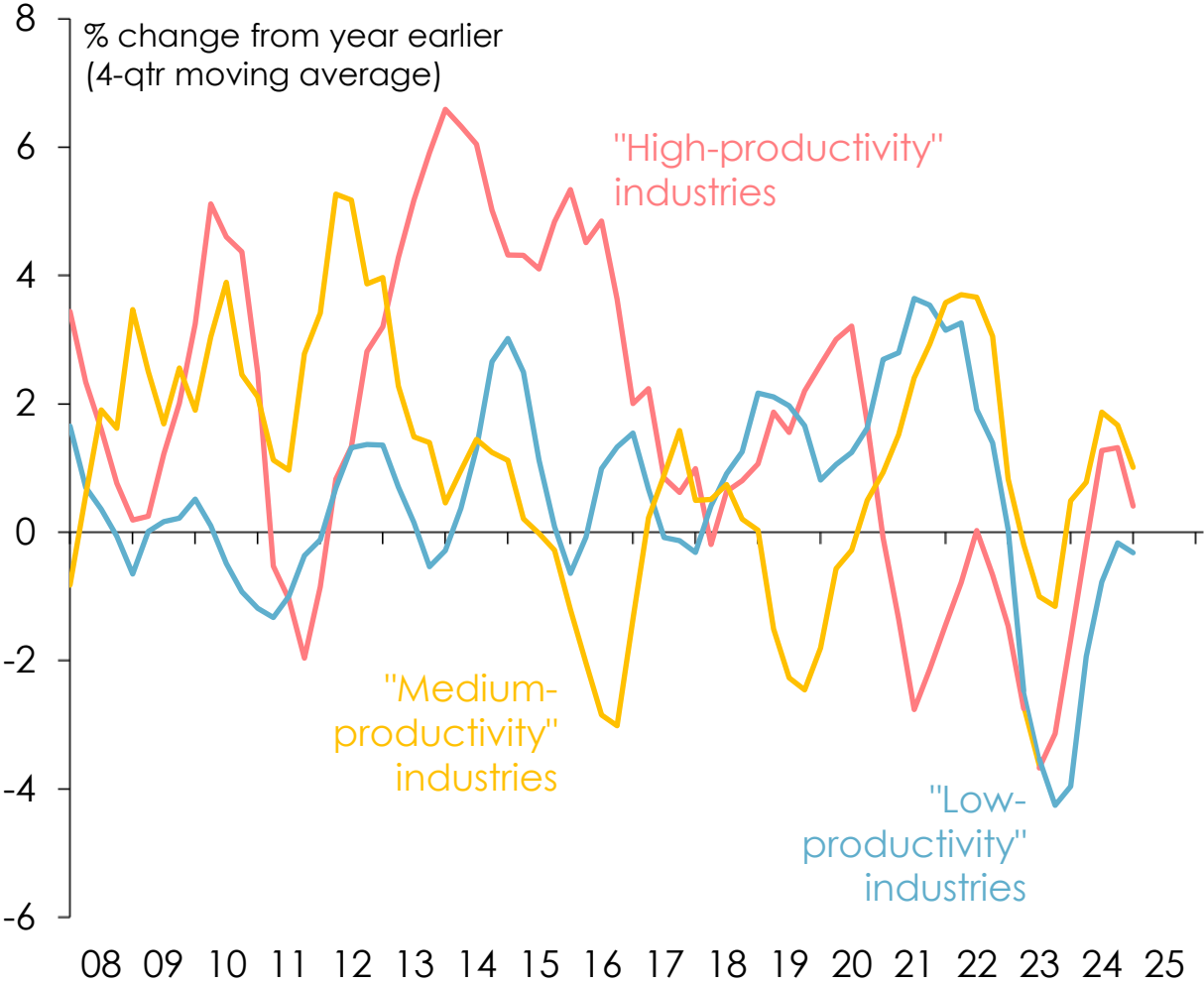
Some industries have much higher labour productivity than others

Australian labour productivity (gross value added per hour worked) by industry, 2023-24

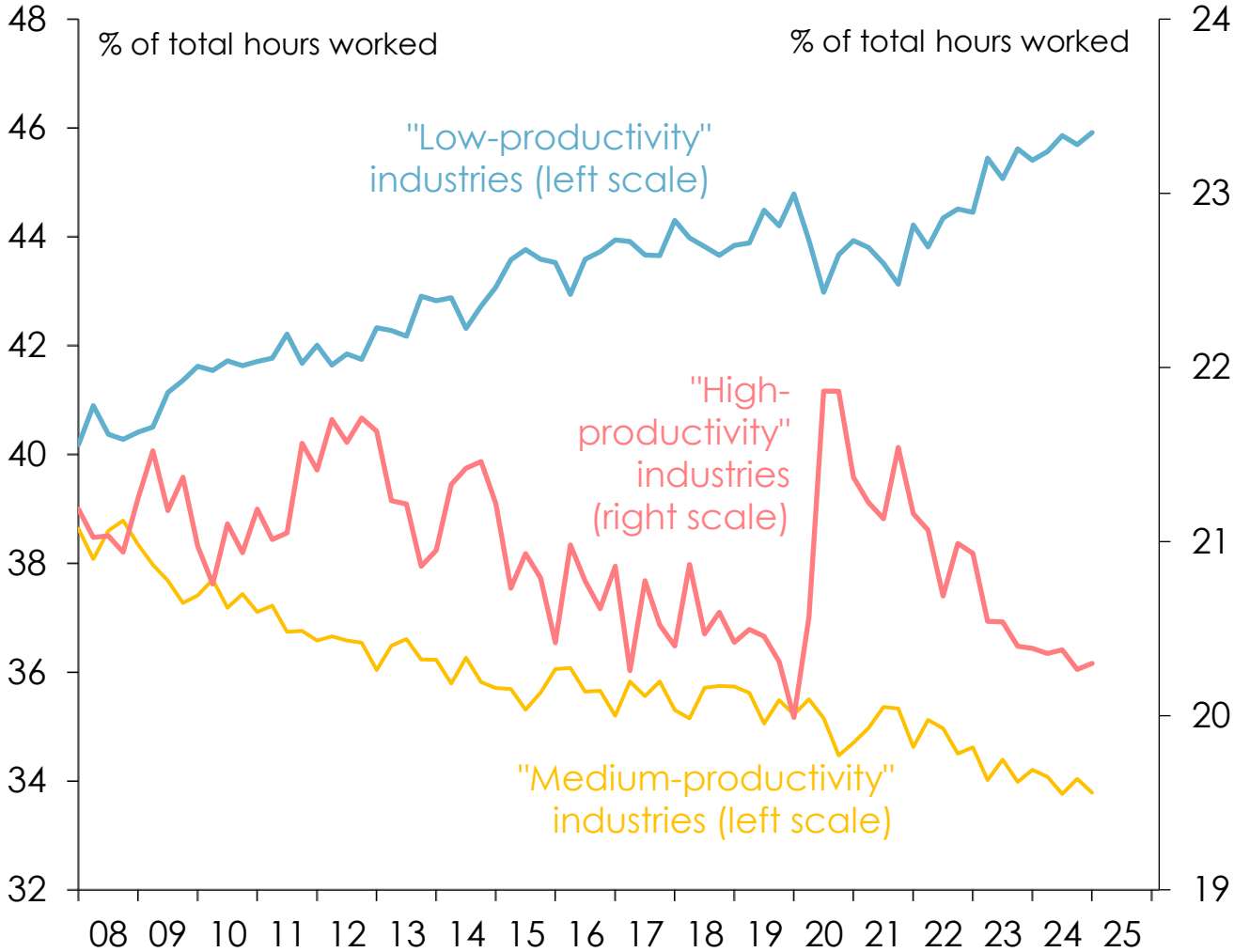


The slide in Australia's overall productivity growth rate is partly due to a shift towards intrinsically low labour productivity industries ...

Labour productivity growth in “high-”, “medium-” and “low-productivity” industries



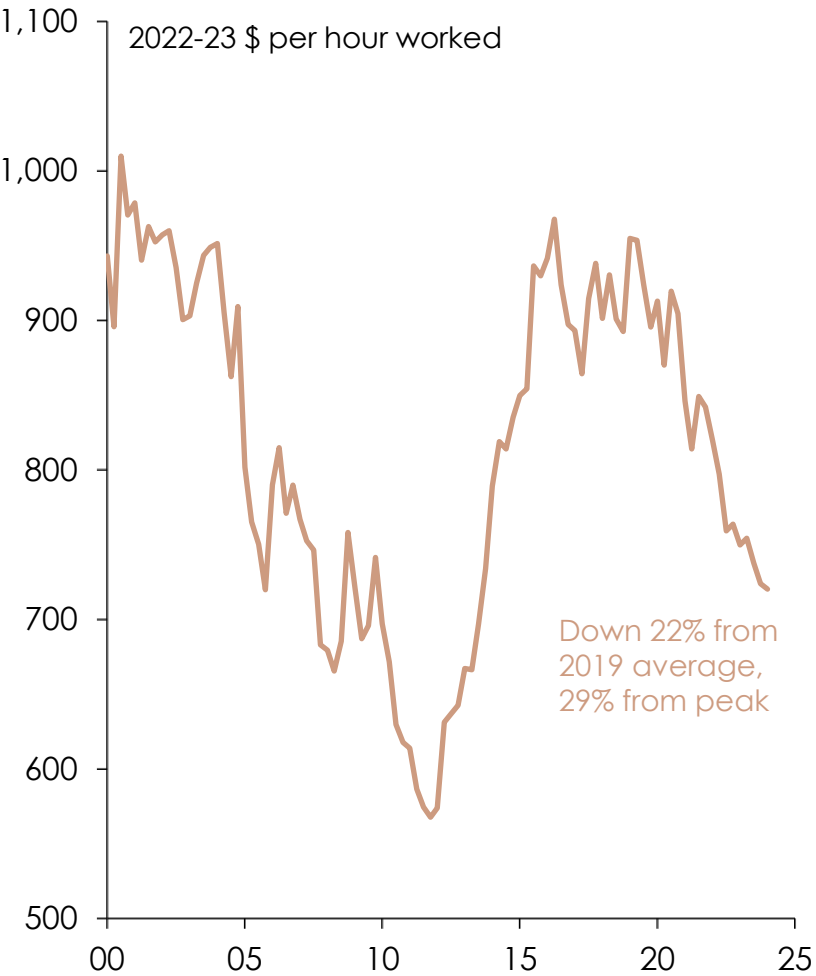
Shares of total hours worked in “high-”, “medium-” and “low-productivity” industries



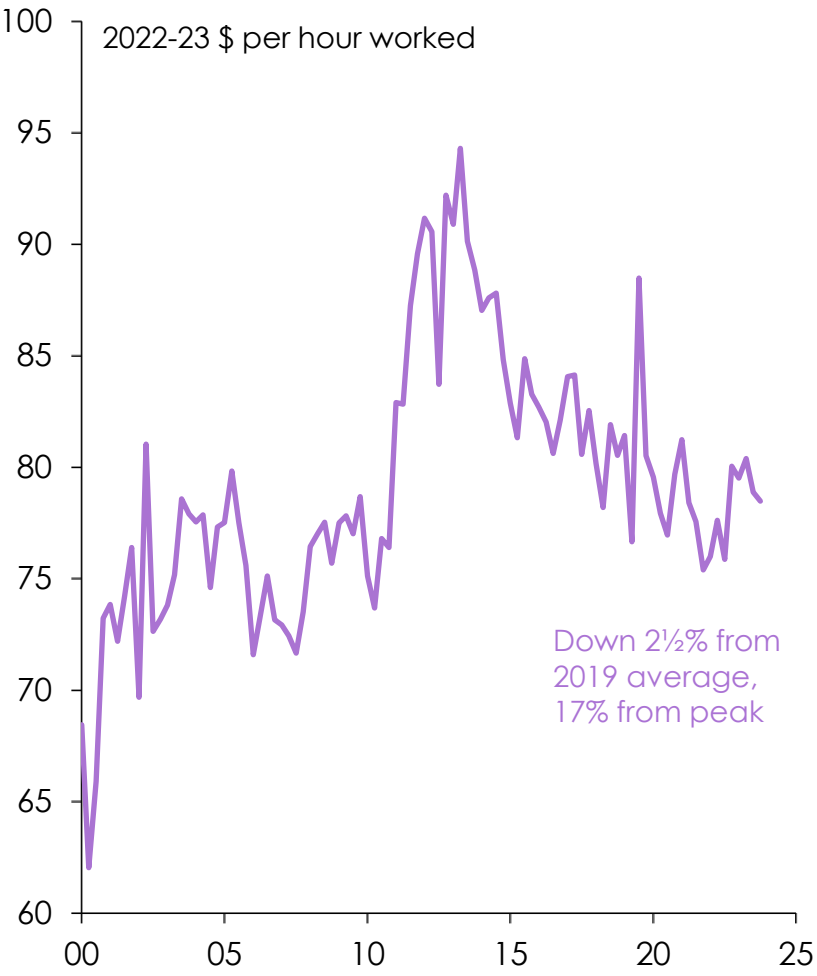
Note: “High-”, “medium-” and “low-productivity” industries are as classified in the previous slide.
Sources: ABS, [Australian National Accounts: National Income, Expenditure and Product](#), December quarter 2024, and [Labour Account, Australia](#), December quarter 2024.

... but also because productivity growth in three of Australia's more important industries has actually been negative over long periods of time

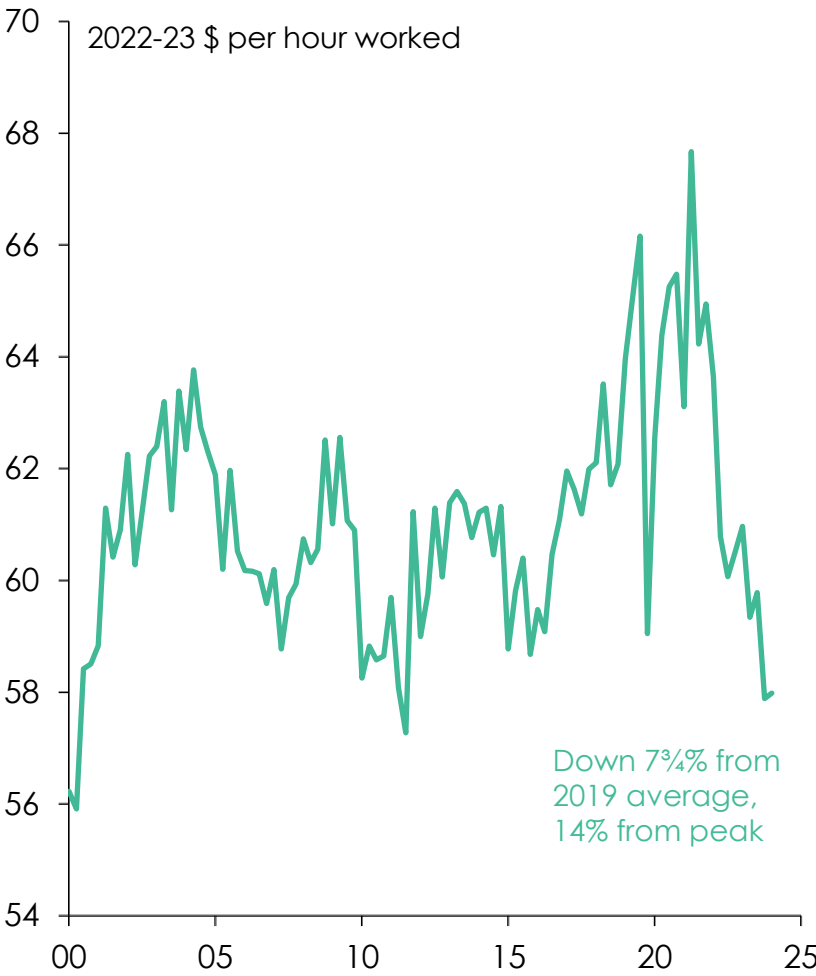
Labour productivity in mining



Labour productivity in construction



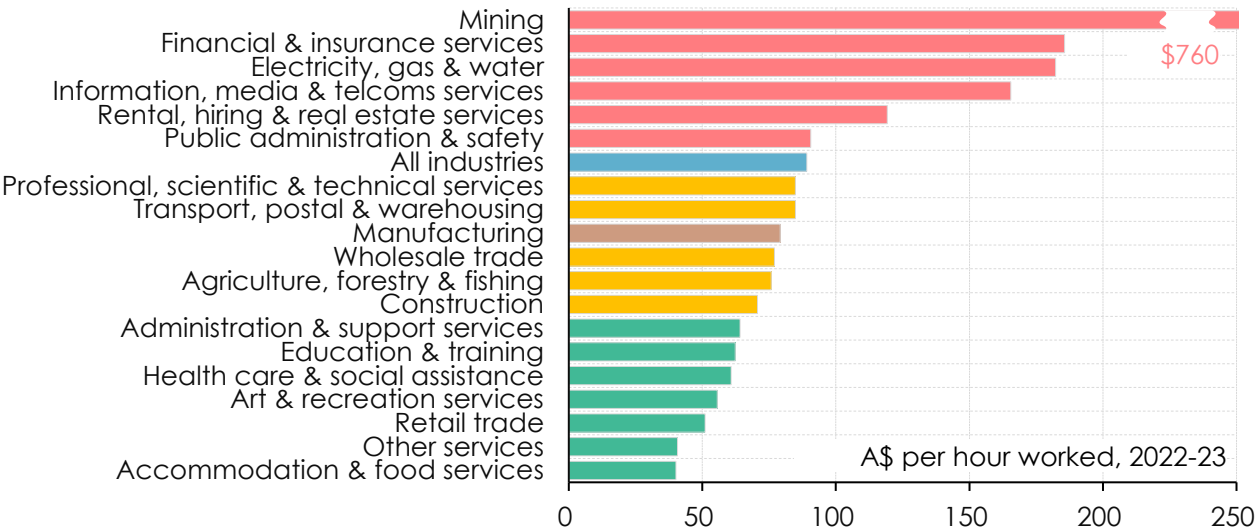
Labour productivity in health care and social assistance



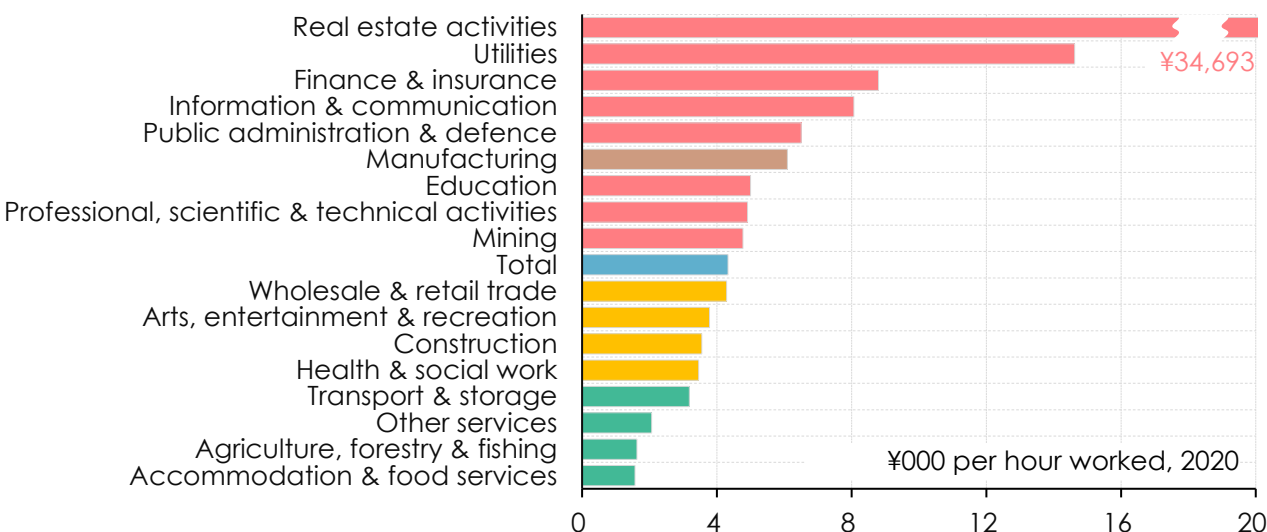
Sources: ABS, [Australian National Accounts: National Income, Expenditure and Product](#), December quarter 2024, and [Labour Account, Australia](#), December quarter 2024.

‘Manufacturing fetishism’ is bad for productivity in Australia, because in Australia manufacturing has below-average productivity

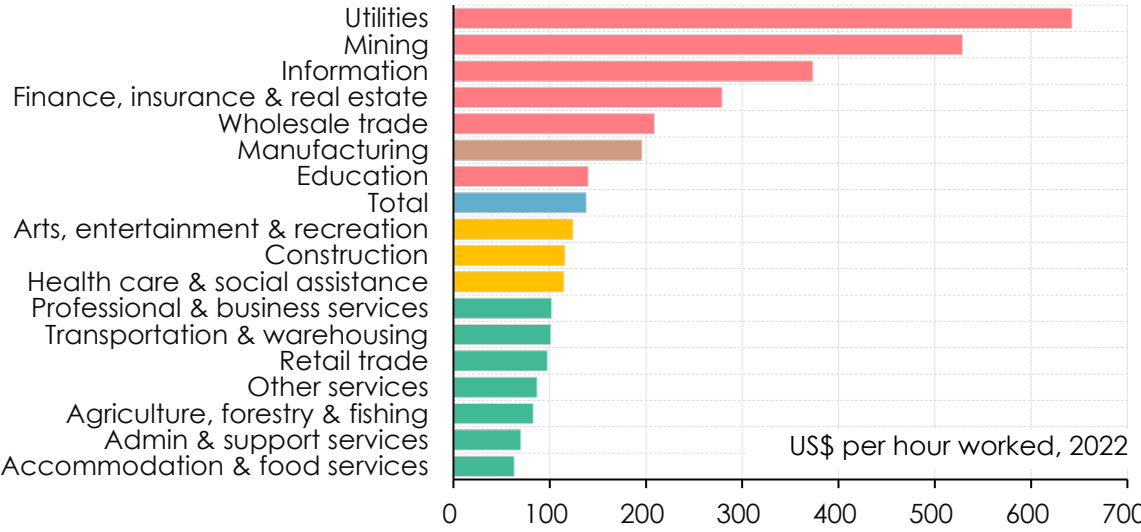
Labour productivity by industry - Australia



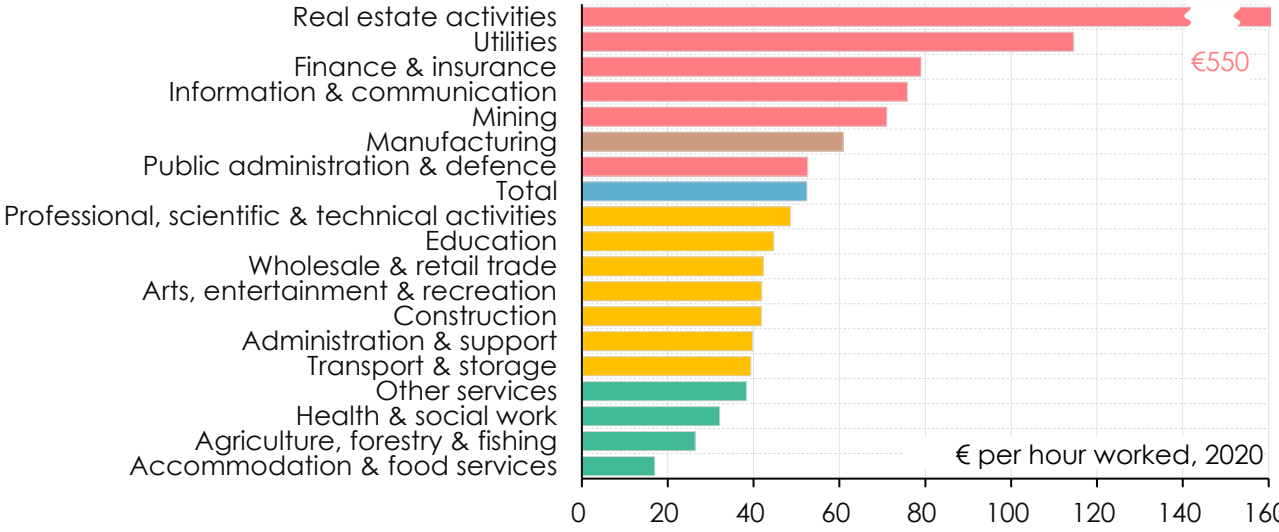
Labour productivity by industry - Japan



Labour productivity by industry – United States



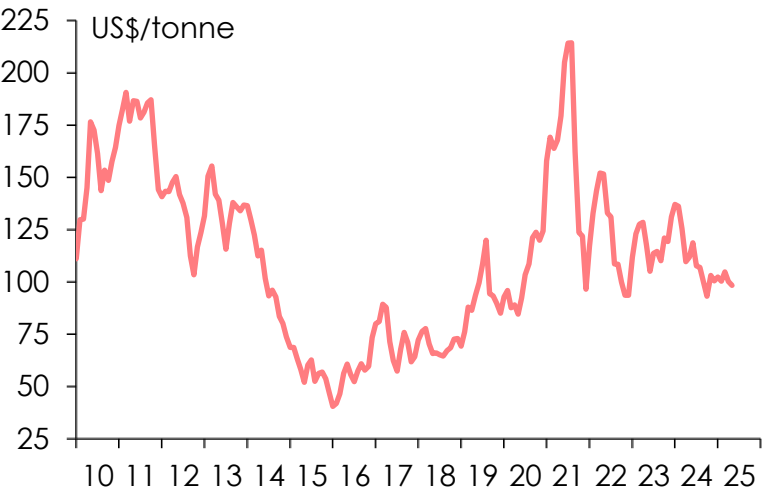
Labour productivity by industry – Germany



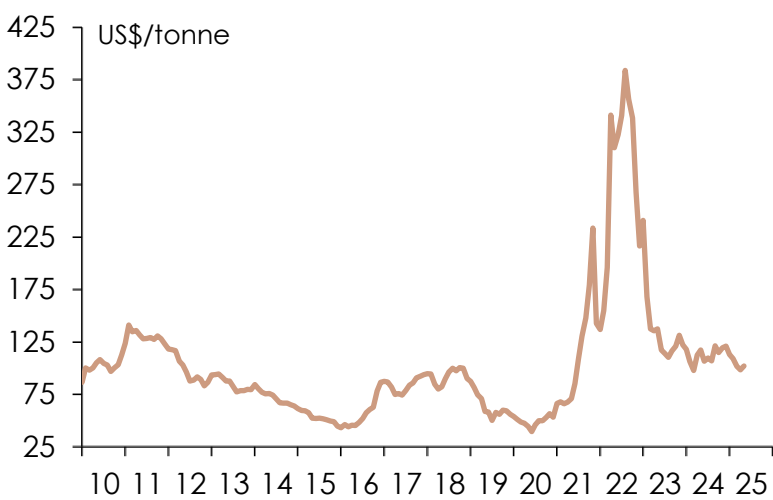
Sources: Australian Bureau of Statistics, [Australian National Accounts: National Income, Expenditure and Product](#) and [Labour Account](#), December 2023; US Bureau of Labor Statistics, [Labor productivity and costs measures - Detailed industries](#), 2022; Luiss Lab of European Economics, [EUKLEMS and Intanprod](#), 2020.

Prices of Australia's principal mineral & energy exports are well off their peaks and seem likely to decline further in 2025

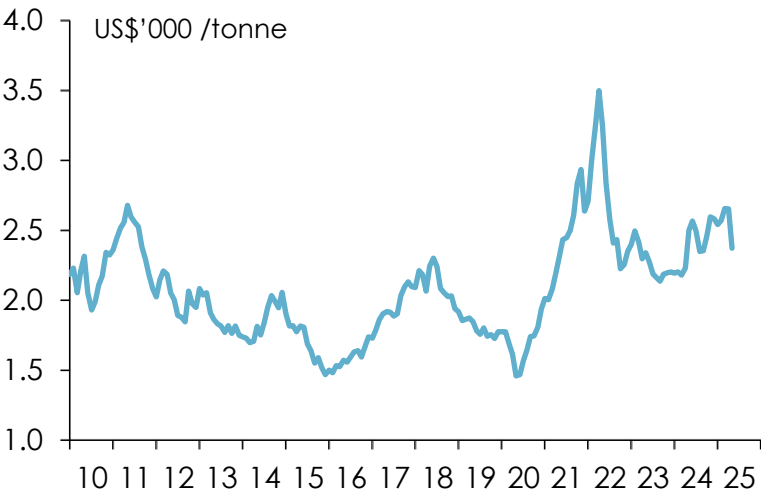
Iron ore



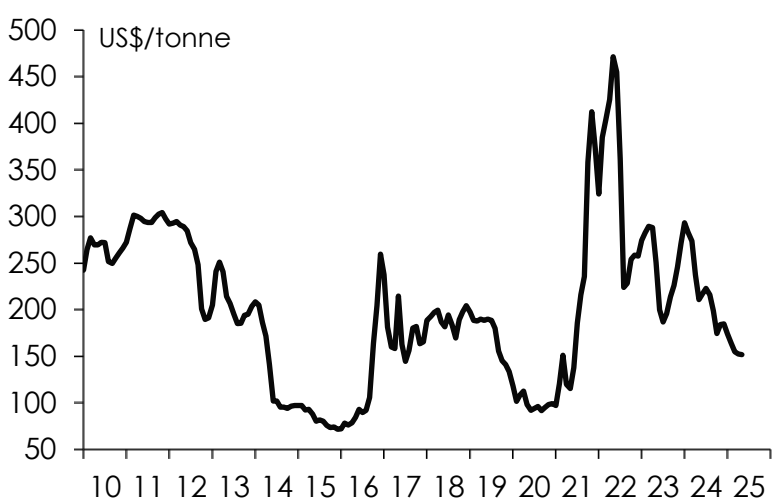
Thermal (steaming) coal



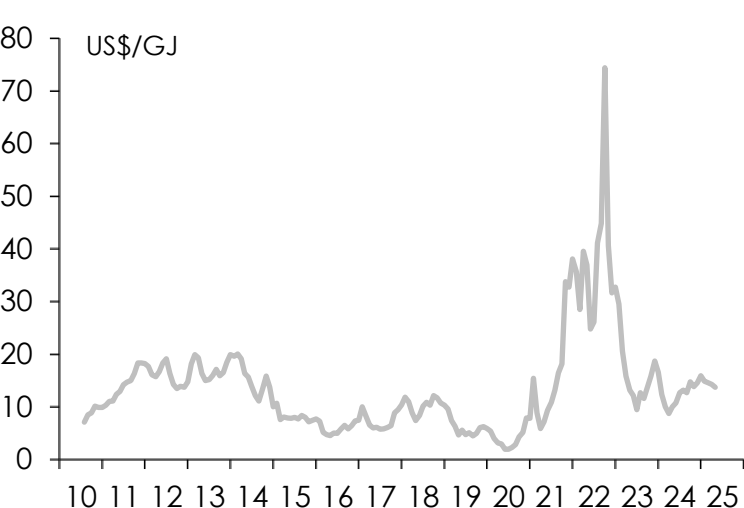
Aluminium



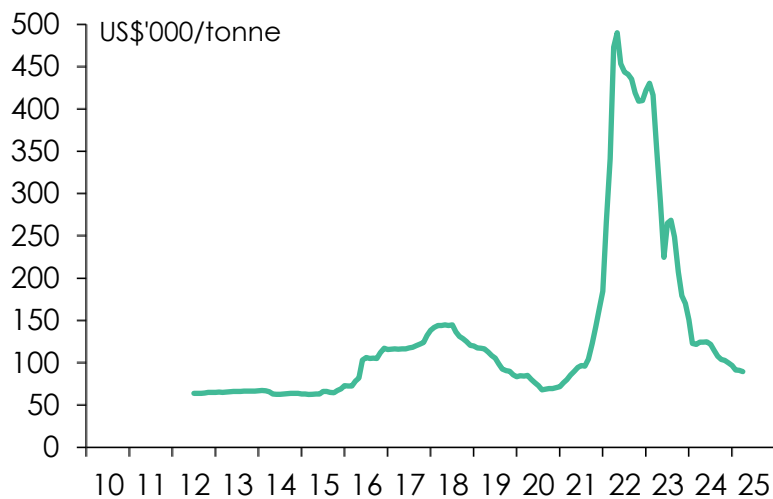
Metallurgical (coking) coal



Liquefied natural gas (LNG)

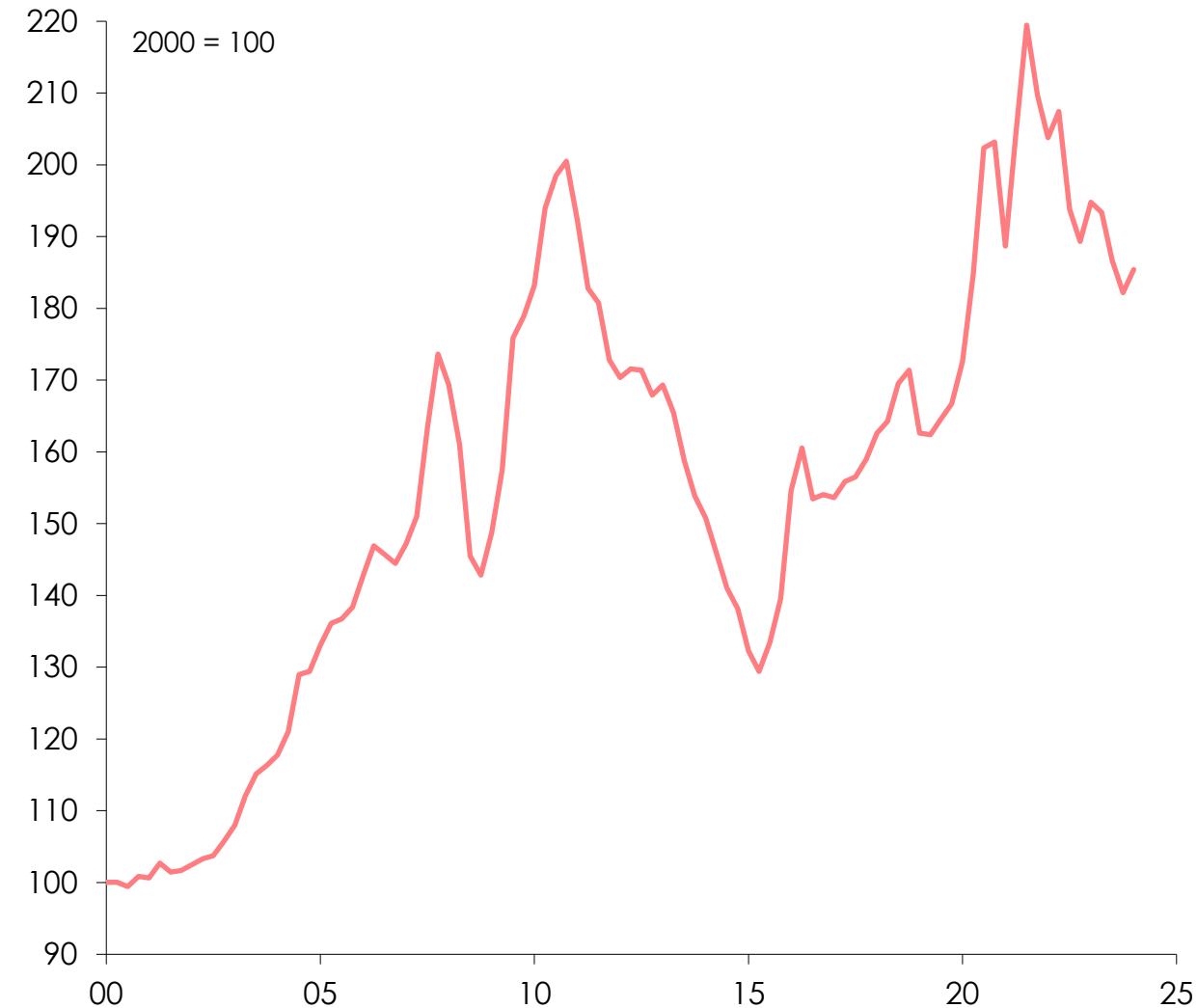


Lithium

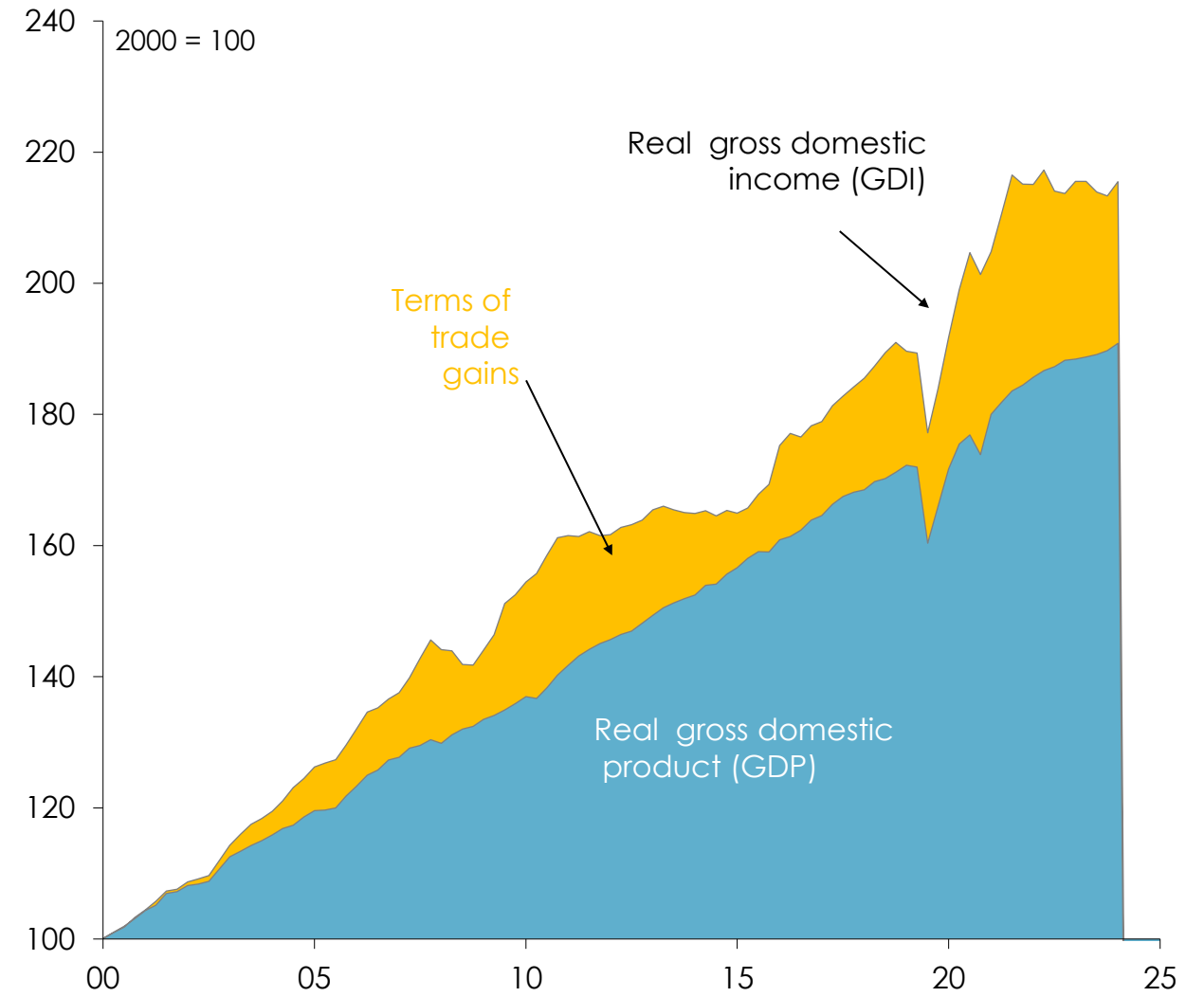


Australia's terms of trade 'tide' is ebbing – and the 'bonuses' our trading partners (especially China) have been paying us will fade away

Australia's terms of trade



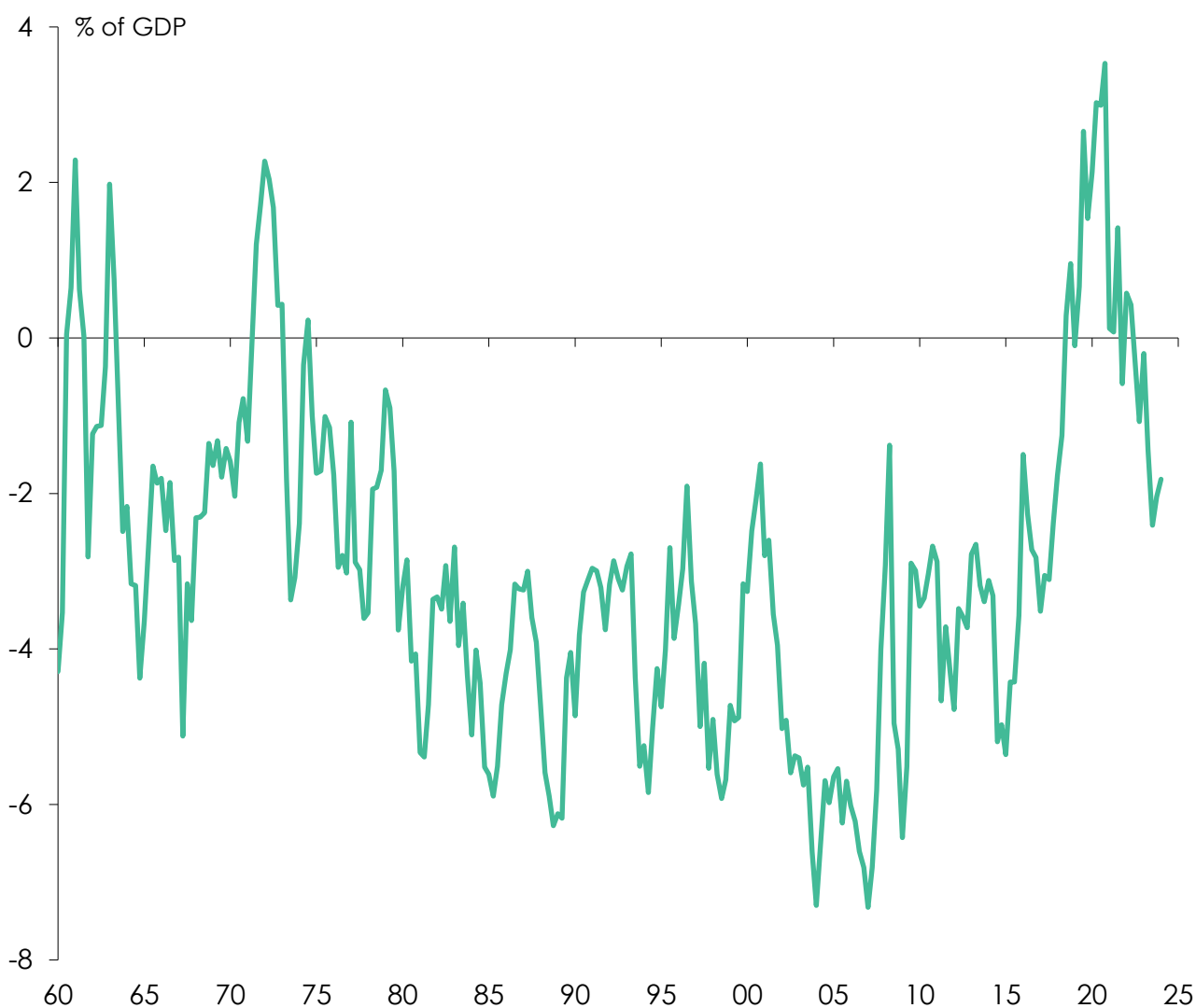
Real gross domestic income & product



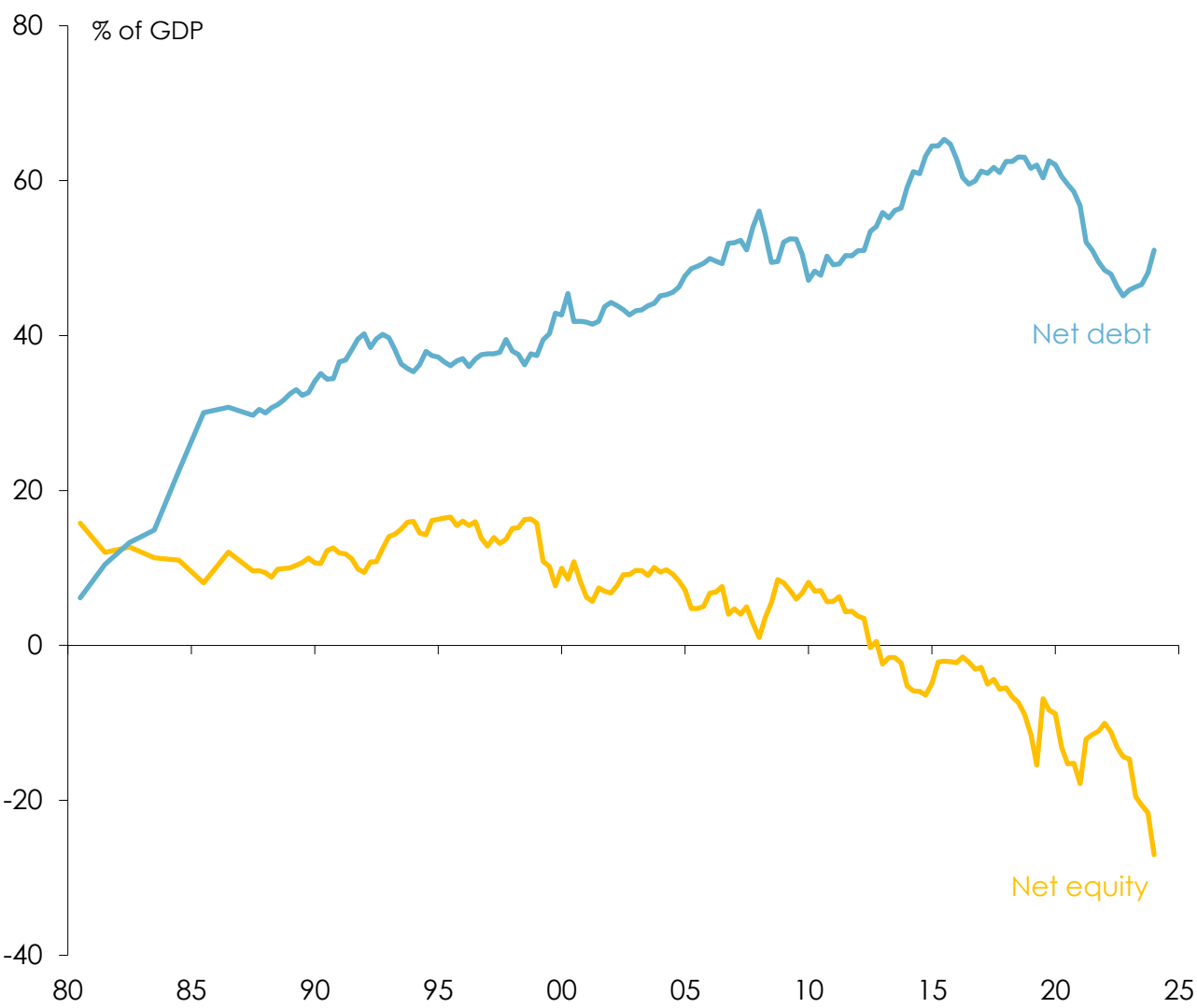
Note: The 'terms of trade' is the ratio of the implicit price deflator of exports of goods and services to the deflator for imports of goods and services. Real gross domestic income (GDI) is measured in the same way except with exports deflated by the implicit price deflator of imports, in order to capture the 'purchasing power' of the total incomes generated by domestic production. Source: ABS, [Australian National Accounts: National Income, Expenditure and Product](#), December quarter 2024.

With Australia's terms of trade reverting to more 'normal' levels, the current account is back in deficit, and foreign debt might return as an issue

Australia's current account balance

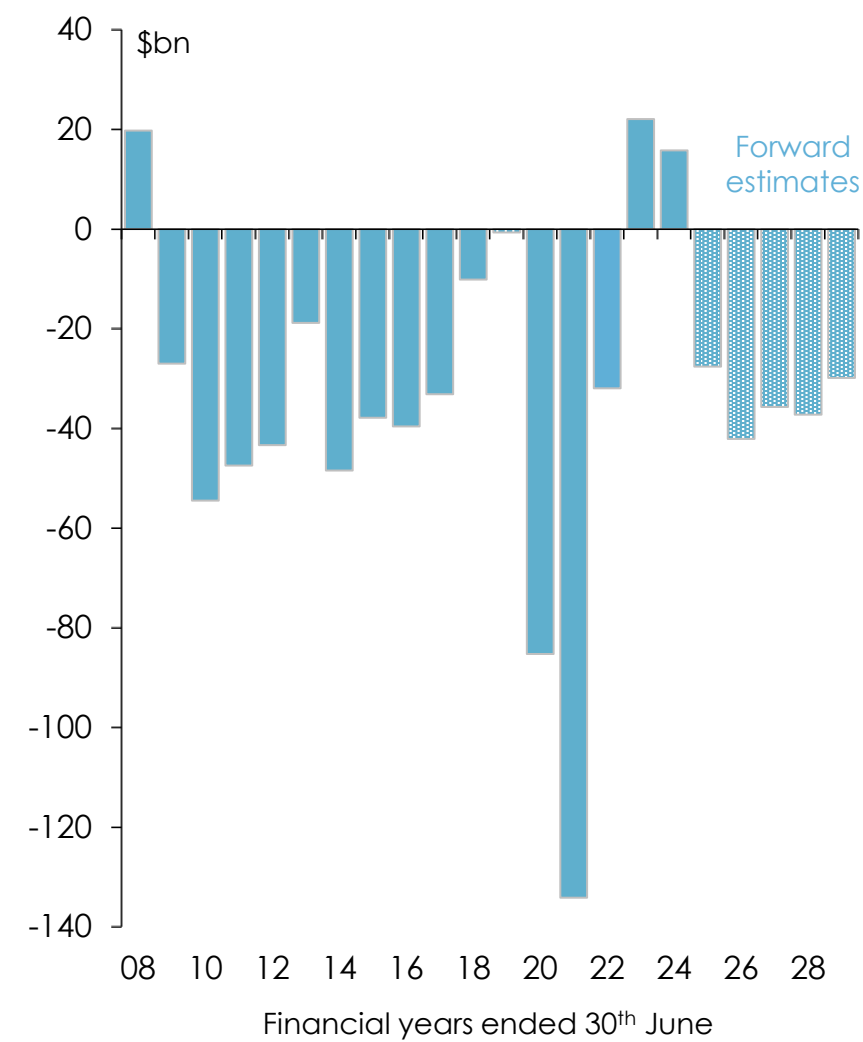


Australia's international investment position

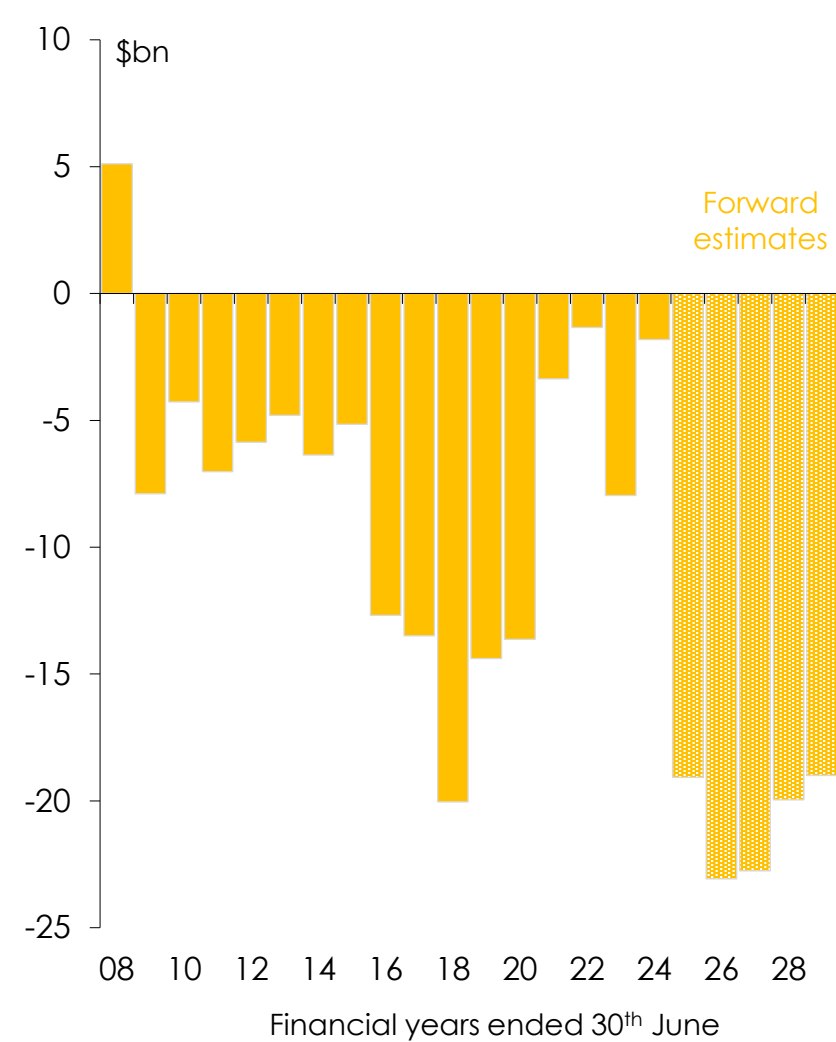


After two successive surpluses, the Federal budget is going back into deficit in 2024-25 – with a large contribution from ‘off-budget’ spending

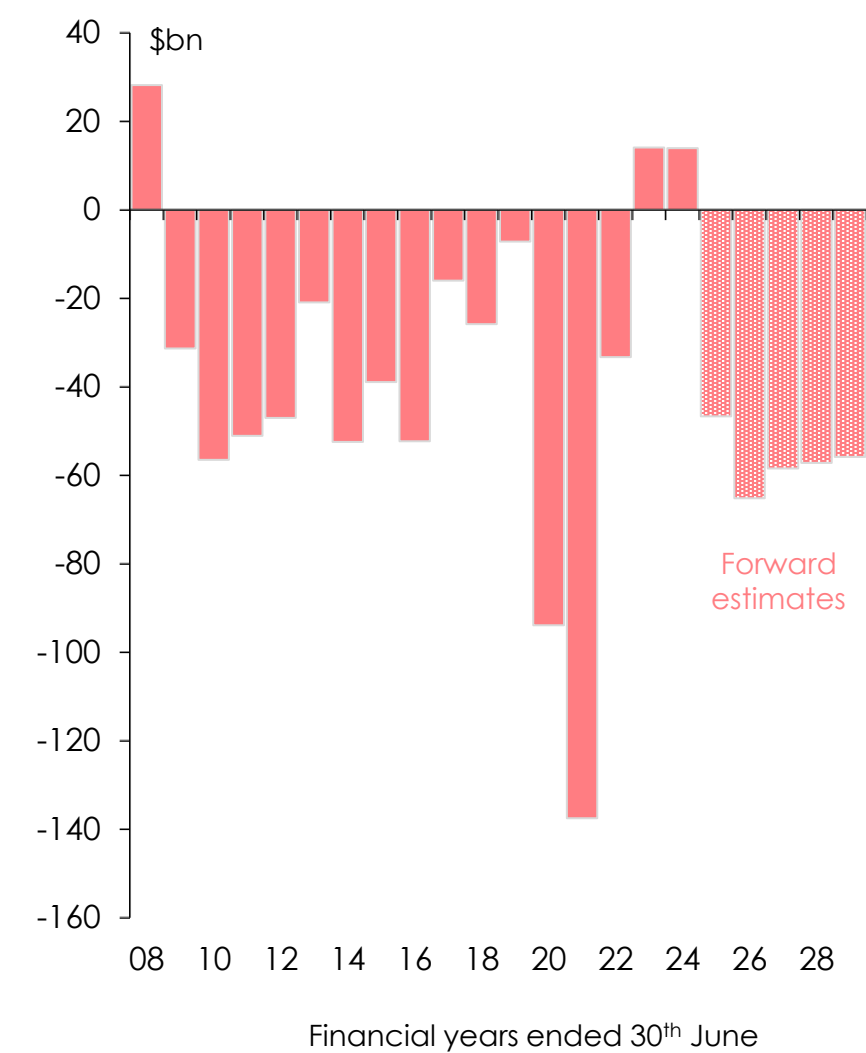
‘Underlying’ cash balance



‘Net investments in financial assets for policy purposes’



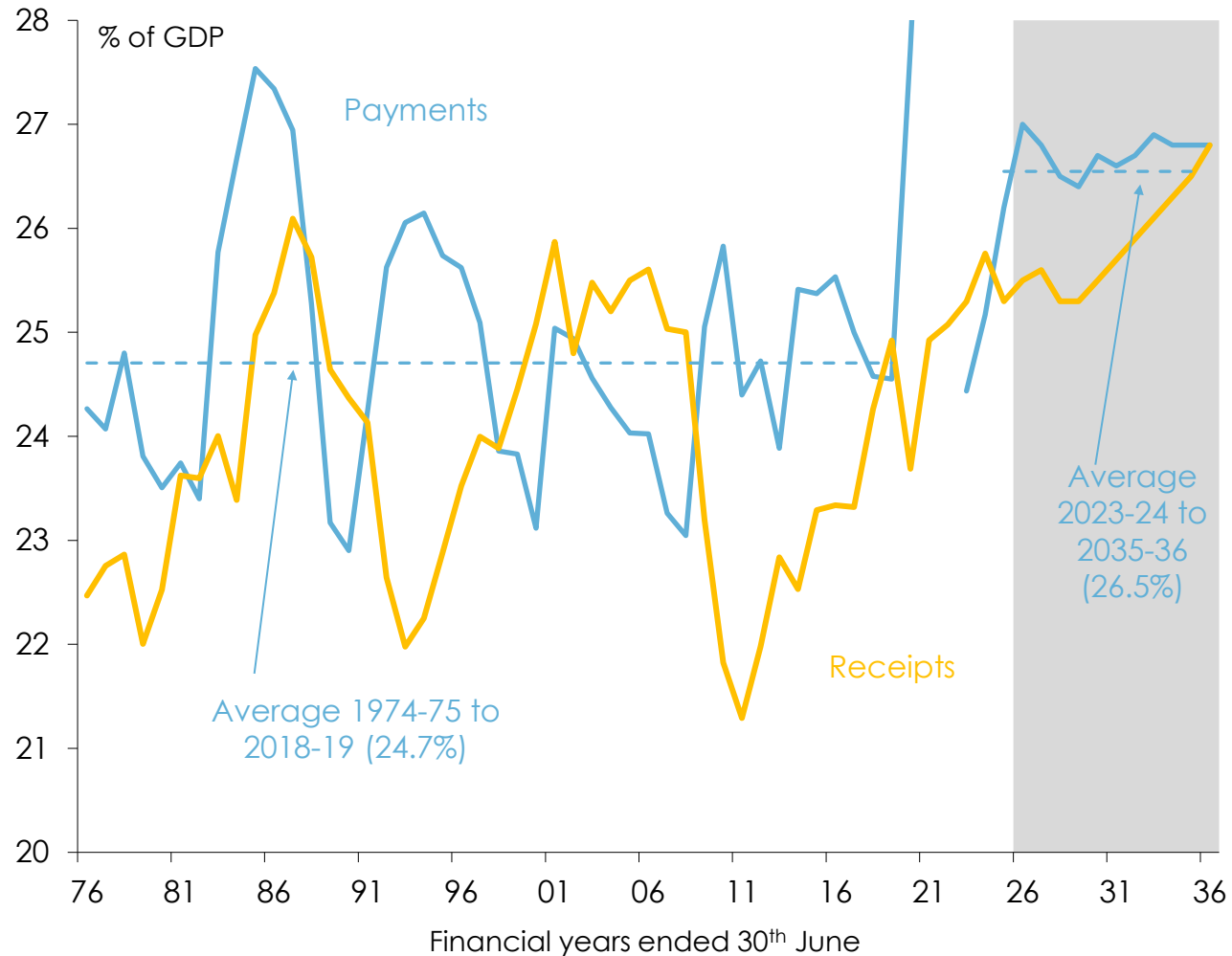
‘Headline’ cash balance



Sources: Australian Government, [2025-26 Budget Paper No. 1: Budget Strategy and Outlook](#), March 2025.

Australia's long-term structural budget problem should prompt an 'adult conversation' about how to pay for additional spending – but it hasn't

'Underlying' cash payments and receipts



- ❑ Federal government spending in the post-Covid era appears to have settled at about 1¾ pc points of GDP higher than the 1975-2019 average
 - that reflects the Australian public's evident demand for more spending on health, aged, disability and child care ...
 - ... the consensus among the major political parties that Australia needs to spend more on defence (whether the public wants that or not)
 - and the inevitability of more spending on interest as a result of the \$531bn increase in net debt since 2008
- ❑ It's not at all clear that this additional spending can be offset by reductions in other areas of the Budget
 - although scrapping the outrageous GST 'deal' done at the behest of Western Australia would be a good start
- ❑ Neither side of politics appears willing to have an 'adult conversation' with the Australian public about how this additional spending should be paid for
 - which leaves the 'default options' of on-going deficits, and 'bracket creep' pushing up personal income tax

Tax reforms that should be ‘on the table’

❑ Broadening the base and/or raising the rate of GST

- not going to happen while the Feds have to wear the political odium of raising the rate or broadening the base, and the financial burden of compensating one-third of the population for the impact on them of doing so – while the states and territories get to spend the resulting additional revenue
- so the ‘nexus’ between GST revenue (plus ‘top-ups’) and ‘general purpose payments to the states (as they used to be called before the introduction of the GST) would need to be broken

❑ Fixing up the loopholes in the personal income tax system

- 47.2% of the taxable income declared by taxpayers in the top tax bracket – as against only 14.6% of the taxable income of taxpayers who aren’t in the top tax bracket – is in forms other than wages and salaries (capital gains, dividends, rents, trust distributions and payouts from super funds), almost all of which are more lightly taxed than wages and salaries
- A ‘quid pro quo’ might be raising the top tax threshold to (say) \$350,000 – which would be more in line with the OECD median as a multiple of average earnings

❑ Properly taxing resource rents

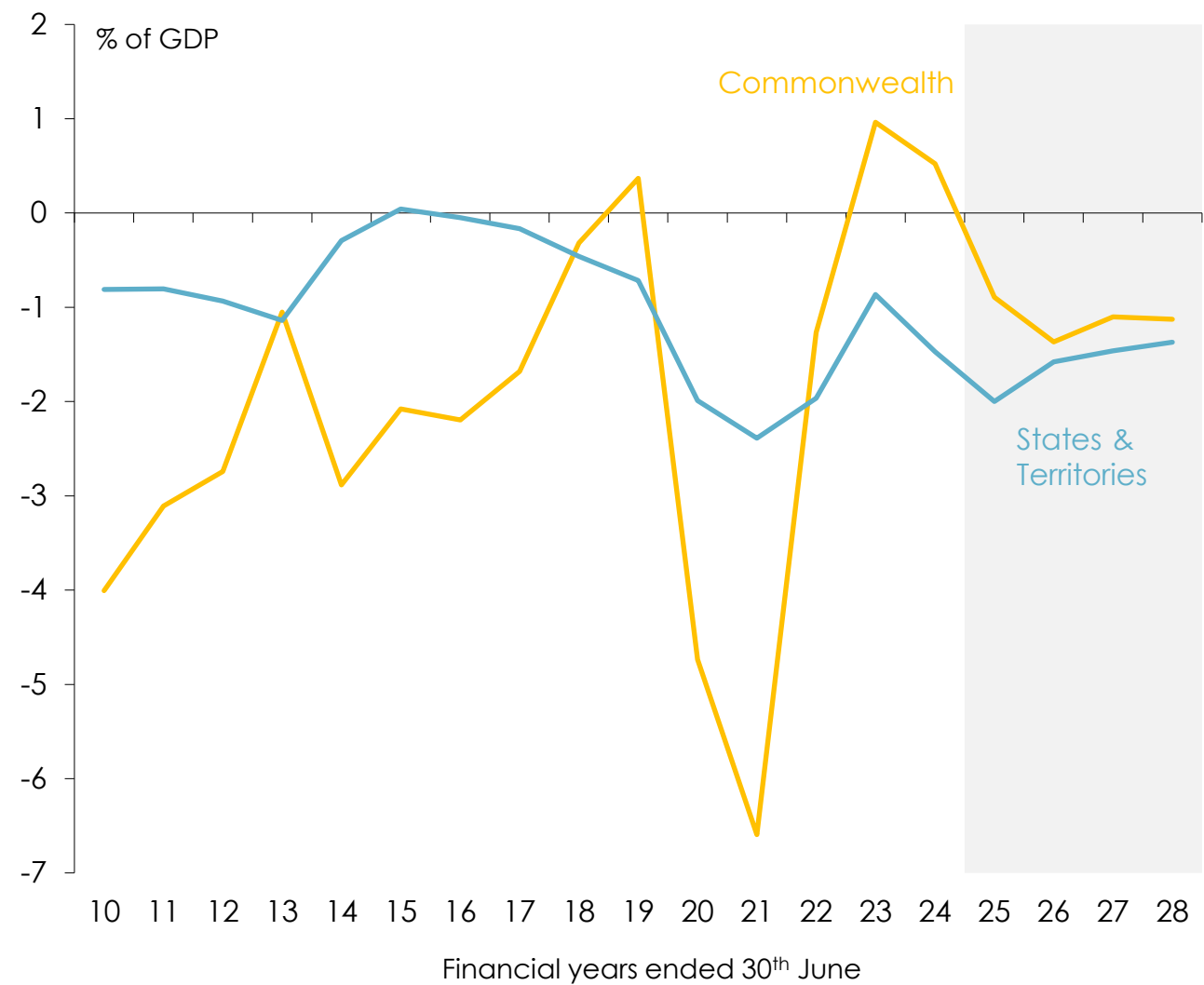
- which the PRRT has conspicuously failed to do
- Ken Henry’s proposed ‘fossil fuel export levy’ is worth considering

❑ An inheritance tax

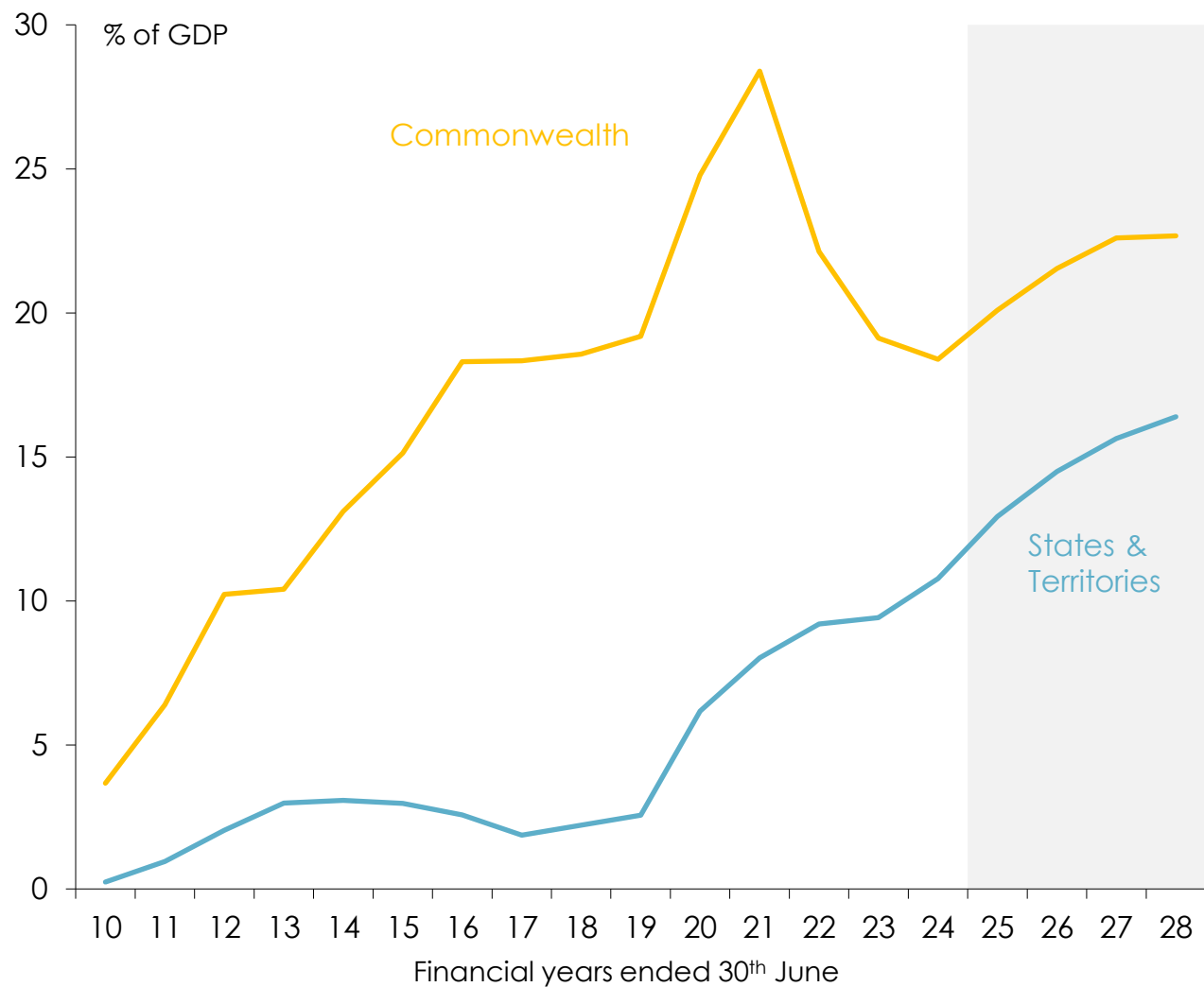
- Australia is something of an outlier among OECD economies in not having some form of inheritance tax
- In particular, the US and the UK (whose tax systems are most commonly used as a reference point for Australia’s) do both have inheritance taxes, and neither Ronald Reagan nor Margaret Thatcher saw fit to abolish them
- why shouldn’t some of the enormous wealth accretions to baby-boomer property owners be taxed to pay for the cost of their care in their declining years?

State and territory governments have been running persistent large budget deficits and accruing growing debts

‘General government’ cash balances



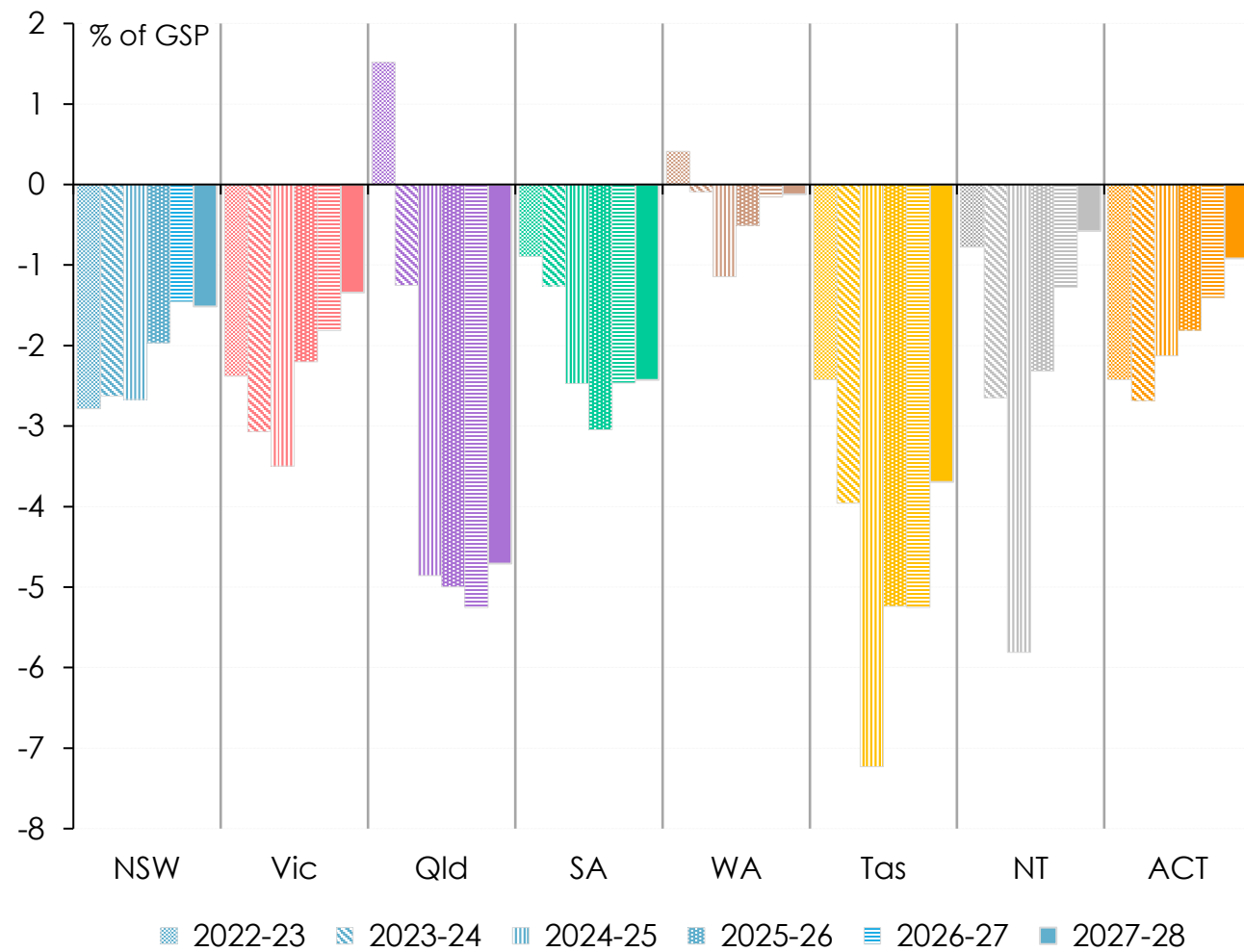
‘General government’ net debt



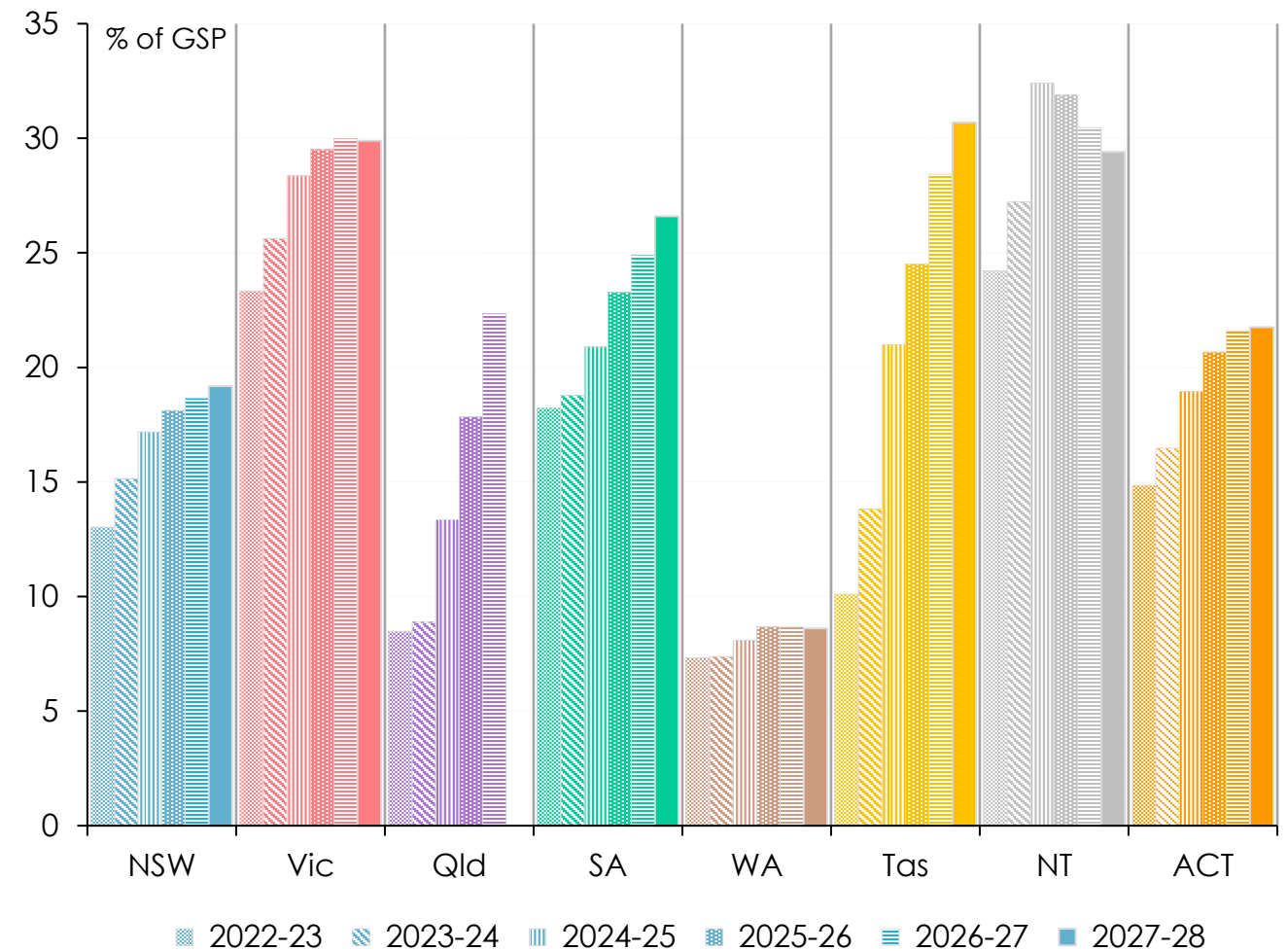
Note: ‘general government’ refers to government departments and agencies funded primarily by taxation revenues or grants from other levels of government, and excludes public financial and non-financial corporations. Sources: Australian, state and territory government annual financial reports, budget papers and mid-year budget reviews.

All states and territories (except mineral-rich and politically powerful) WA have been running large deficits and accumulating debt

State and territory non-financial public sector cash balances



State and territory non-financial public sector net debt



Sources: State and territory government annual financial report, budget papers and 2024-25 mid-year budget updates/reviews.

Is it time to consider re-introducing some forms of federal control over the fiscal policies of state and territory governments?

- ❑ **Should the Federal Government make an annual decision as to the volume of 'general revenue assistance' to the states and territories?**
 - as it did every year between 1942 (when John Curtin's Government acquired a monopoly over personal and company income tax as a 'temporary war-time measure) and the introduction of the GST in 2000
 - that might be a by-product of breaking the 'nexus' between revenue from the GST and payments to the states
- ❑ **Should the Federal Government exercise some control over the amount of borrowing by state and territory governments?**
 - as it did between the establishment of the Loan Council in 1927 (confirmed by one of the very few successful referenda in 1928) and the abolition of the Loan Council by the Keating Government in the early 1990s
 - one of the reasons why the Loan Council was abolished was because states were using state-owned financial corporations (which were exempt from Loan Council borrowing limits) to evade Loan Council controls
 - but those exemptions were intended to avoid unduly restricting state banks, which don't exist any more, so Loan Council controls could be extended to state financial as well as non-financial corporations
- ❑ **Should the Federal Government make explicit that it doesn't 'stand behind' or guarantee the debts of state and territory governments?**
 - the credit rating agencies (and the bond markets) assume that the Federal Government is in effect the guarantor of debts incurred by state and territory governments, which is in turn (explicitly) reflected in their credit ratings
 - this allows states and territories to borrow at lower interest rates than they could otherwise
 - but it also curtails the 'discipline' which bond markets might otherwise exert over the borrowing proclivities of state and territory governments

I'm more likely to see one of these on my front lawn of a morning than for any of the aforementioned suggestions to be aired during this campaign



Important information

This document has been prepared by Saul Eslake on behalf of Corinna Economic Advisory Pty Ltd, ABN 165 668 058 69, whose registered office is located at Level 11, 114 William Street, Melbourne, Victoria 3000 Australia.

This document does not purport to constitute investment advice. It should not be used or interpreted as an invitation or offer to engage in any kind of financial or other transaction, nor relied upon in order to undertake, or in the course of undertaking, any such transaction.

The information herein has been obtained from, and any opinions herein are based upon, sources believed reliable. The views expressed in this document accurately reflect the author's personal views, including those about any and all financial instruments referred to herein. None of Saul Eslake, Corinna Economic Advisory Pty Ltd nor Independent Economics however makes any representation as to its accuracy or completeness and the information should not be relied upon as such. All opinions and estimates herein reflect the author's judgement on the date of this document and are subject to change without notice. Saul Eslake, and Corinna Economic Advisory Pty Ltd expressly disclaim any responsibility, and shall not be liable, for any loss, damage, claim, liability, proceedings, cost or expense ("Liability") arising directly or indirectly (and whether in tort (including negligence), contract, equity or otherwise) out of or in connection with the contents of and/or any omissions from this communication except where a Liability is made non-excludable by legislation.

Any opinions expressed herein should not be attributed to any other organization with which Saul Eslake is affiliated.