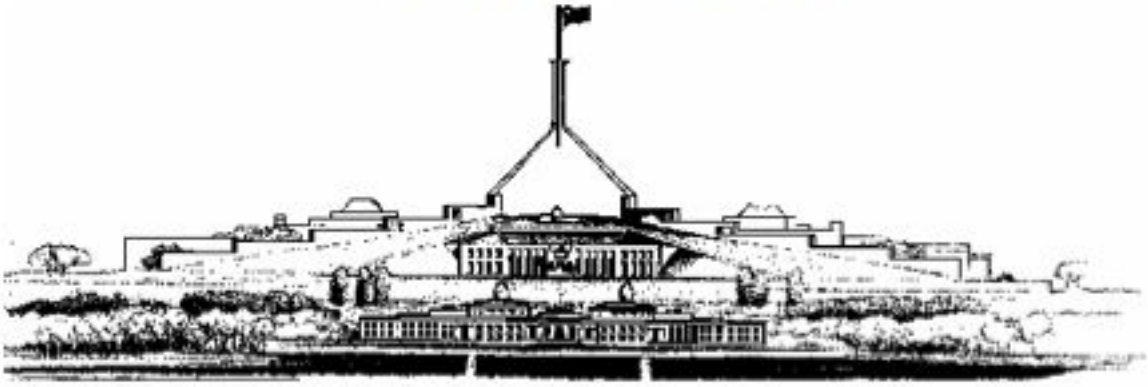
COMMONWEALTH OF AUSTRALIA

PARLIAMENTARY DEBATES



HOUSE OF REPRESENTATIVES

MATTERS OF PUBLIC IMPORTANCE

Economy: Policy

SPEECH

Wednesday, 1 September 1999

BY AUTHORITY OF THE HOUSE OF REPRESENTATIVES

SPEECH

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Page	9638	**Proof**	No
Questioner		**Responder**	
Speaker	Cox, David, MP	**Question No.**	

Mr COX (Kingston) (4.10 pm)—On Monday the Treasurer was finally forced to come back into this House and talk about the current account deficit. He was forced to do that because he had yet another bad current account figure. Before that, day after day, he has come in here and had a rave about how brilliantly the economy is going and a rant about how badly it went under Labor. All of the time I have been in this parliament, the one thing that he has stayed right away from talking about is the unsustainably high current account deficit. He has talked about everything except the one thing that he should be focusing on.

Is he ignoring it? Does he hope it will go away? Or worse, does he not understand it is a problem? One thing is certain, he has taken no action to reduce the current account and he offers no strategy for reducing the current account. He will wait for world economic events to realign and solve Australia's current account problem. It is an optimistic strategy for an optimistic Treasurer—or a fool in denial. Rather than adjusting policy to meet the challenge, the threat, of a high current account deficit, the opposite has been the case.

The fundamental cause of Australia's current account problem is Australia's poor domestic savings performance. In the March quarter of 1996, the last period Labor was in office, the household savings ratio stood at 5.6 per cent. Now after three years with Peter Costello as Treasurer it has collapsed to 0.4 per cent.

On Monday, in one of his rare shifts from rhetoric to brief interludes of substance—and they were brief; there were only about four paragraphs that had any substance at all—the Treasurer used as an authority the FitzGerald report commissioned by Labor in 1993. Mr Costello said:

The one thing that the FitzGerald inquiry and report made clear, the one thing that the Labor Party would agree with—

and we do—

is that building public sector savings is the best thing that a government can do in the face of a current account.

This was confirmed as government policy by the Secretary to the Treasury in his post-budget Australian business economists speech, when he said:

In recent years, we have not been asking monetary policy to address the current account problem. Rather emphasis has been appropriately put on the role of fiscal policy—the generator of budget surpluses and contributor to national savings—to do that job, leaving monetary policy free to concentrate on its objective of maintaining low inflation without undue constraint on growth.

This is a very desirable balance in the use of monetary and fiscal policies which may hold part of the answer to our longstanding current account concern; it is also part of the framework which underlies the judgments on medium term growth potential.

The simultaneous achievement of sustainable CAD outcomes and low and stable inflation would be put at risk by a complacent attitude to the use of fiscal surpluses. A breakdown in the performance of one policy inevitably compromises the other.

My fear is that that complacent attitude to the use of fiscal surpluses is exactly what we are about to see with a dramatic loosening of fiscal policy provided by the Howard government's so-called new tax system. If fiscal policy is the chosen instrument to control the current account deficit, then why is the Howard government contemplating a large fiscal loosening through its tax package when the current account deficit is already historically high?

A second related question is: how sound is the surplus on which this fiscal loosening is built? Let us look at the Treasurer's $5.4 billion estimated surplus this year. In it there is a 43.2 per cent increase in dividends from

government business enterprises—that is, $1.8 billion. Take that away and you have a $3.6 billion surplus. That is a very modest improvement on the 1998-99 outcome of $3.1 billion.

There are always extraordinary items in any budget or set of financial statements, but there has not been much, if any, real growth in the size of the surplus. Even after the big fiscal loosening next year with the introduction of ANTS, the surplus will be only $7.2 billion. However, when you look at the underlying cash surplus next year, that is projected to be only $3.1 billion. The principal reason for that discrepancy is the bringing forward under accrual accounting of PAYG, although the tax is paid in subsequent years. That suggests that after the introduction of ANTS the government will not be left with much latitude as far as the surplus is concerned. In his post-budget speech to the Australian business economists, the Secretary to the Treasury, Ted Evans, put all this in some historical perspective. I regret that the minister has left the chamber. Mr Evans said:

Looking at Chart 1, which shows the underlying cash balance over a long period, we see that surpluses stretch out into the projection period. We should keep in mind, however, that of the six years of surplus there shown, only one is currently behind us. The 1999-2000 surplus we could take as being reasonably assured, but beyond that we are talking about mere projections, subject to all of the uncertainties of the world economy. Taking the 1999-2000 surplus as being `in the bag', the cumulative surplus over the three years would amount to 1.5 per cent of annual GDP. The scale of that might be assessed against the surpluses in the late 1980s, our last period of fiscal consolidation. On that earlier occasion, the cumulative surplus over the first three years amounted to 4.1 per cent of annual GDP—well over twice that achieved in the latest round.

The original A New Tax System package had a negative effect on the fiscal balance of almost $5 billion. To that must now be added the further loosening resulting from the Howard government's agreement with Democrats —at least a further $1.4 billion. In my view these are risks which need to be considered after eight years of continuous economic growth when loosening fiscal policy to such a significant degree in the face of a record high current account deficit. The Treasurer's explanation for the high current account deficit is entirely an external one—it is not his fault. He said on Monday:

. . . when you are running a strong domestic economy and you are in the biggest downturn of your time—meaning export values are low—you would expect pressure on your current account. We forecast it. We do not control the prices of Australian commodities.

Australia is presently operating with a current account deficit of about six per cent. A large contributing factor is the high level of domestic demand which is sustaining a higher than expected growth performance. Admitting that fact might cause the Treasurer to have to do something about it. Instead the Treasurer thinks he can forecast the current account deficit away. On Monday he said:

Why is it that we forecast the current account to come down next year? Because the international economy will pick up. The Australian growth rate will be lesser but the international economy will pick up.

What does the Treasury say about that? The first sentence of Statement 1—Fiscal Strategy—of Budget Paper No. 1, says:

The 1999-2000 Budget demonstrates the Government's commitment to maintain the budget in surplus while Australia's economic growth prospects remain sound.

The key word is `while'. What does `while economic growth remains sound' mean? It depends on whether and how far economic outcomes diverge either up or down from the budget forecast. One of the reasons for the early election last year was that the government was, at the time it was called, much more concerned about the outlook for growth this year than it seems to be now.

Statement 2—Economic Outlook—contains a section specifically dealing with risk in this year's budget papers. Weighed against doubts about the sustainability of recovery in East Asia and Japan is the possibility that the US could continue to exceed expectations. Of course, US economic performance may not continue to exceed expectations. Treasury admit that the downside risk is worsening of the current account deficit should the world economy not pick up. On the other hand, we must also look at the upside risks. If growth is stronger than expected, particularly if the contributing factor is higher than expected US economic growth and even a monetary tightening there which would be combined with the impact of the government's loosening of fiscal policy with its raid on the surplus and some additional inflationary pressure, including from the GST, then pressure on the current account will be higher than would otherwise have been the case and the momentary authorities may have to decide that

interest rates will have to go up. This concern was raised in a Senate estimates committee by the Secretary to the Treasury earlier this year.

The high current account deficit means this is not a good time to loosen fiscal policy in the manner prescribed by the renegotiated ANTS package. Australia is presently operating with a current account of six per cent. It has only had to do so three times previously in Australia's recent economic history. The first time was in 1986, and resulted in a currency crisis. The second time was in 1989-90, and it was corrected with monetary policy which resulted in recession. The third time was at the beginning of 1995. That was, however, controlled without crisis by intelligent use of both fiscal and monetary policy. On that occasion we recognised we had a problem, we told the markets and the public we had a problem, and we took appropriate corrective action on both the fiscal and monetary fronts. Let us hope that this current account deficit can be moderated without crisis.

It is certainly the case, as was demonstrated in 1995, that as a result of the economic reforms of the last Labor government Australia is much less vulnerable to external shocks than was previously the case. However, without an appropriate policy response there is a significant risk that there could be a rapid market response with implications for the rest of the economy. *(Time expired)*