How the commodities boom underpins the re-acceleration in growth

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Yesterday's national accounts clearly illustrate the different ways in which the Australian economy is drawing strength from the resources boom. Taking the past two quarters together, Australia's output of goods and services has expanded at a 4.3% annual rate, up from an annual rate of 2.4% in each of the two previous half-years.

Only part of the stimulus from the resources boom is directly derived from increased minerals production – although that is now starting to come through, with mining industry output rising at a 12.6% annual rate in the most recent half (which in turn accounted for about 15% of the acceleration in overall economic growth from the previous half).

The larger impact comes from the flow-on effects of the resources boom, including the impact of the on-going improvement in Australia's terms of trade (the rise in the prices of Australia's exports relative to those of our imports), on income and expenditures. This is captured by the measure which the ABS calls real gross domestic income (output adjusted for changes in the terms of trade), which increased at a 5.9% annual rate over the past half-year, up from an annual rate of 3.8% in each of the two previous half-years.

Again, only part of this gain accrues to mining companies in the form of higher profits. Indeed, the rate at which mining company profits are rising has been slowing since this time last year. Other direct beneficiaries include the increasing number of people employed in the mining industry, companies providing goods and services to the mining industry (including construction, transport and manufacturing businesses), companies providing services to regions where economic activity and property prices have been boosted by the mining boom (including banks), and the increased number of employees in all of these businesses. In all, the share of pre-tax corporate profits (excluding the financial sector) in GDP now stands at around 12.5%, the highest for over 20 years.

Another major beneficiary of the substantial increase in corporate profits has been the Federal Budget. Yesterday's national accounts show that company tax collections now account for over 5% of GDP, up from around just over 4% of GDP five years ago (whereas by contrast, the share of GST revenues in GDP has remained unchanged at just under 4%).

More than any other single factor, the surge in company tax revenues has made it possible for the Federal Government to cut personal taxes (by the equivalent of 0.5% of GDP over the past five years) whilst still keeping the Budget in surplus.

These tax cuts have effectively redistributed a chunk of the gains produced by the commodities boom (and its flow-on effects to other businesses) from the corporate sector to the household sector. Together with rising employment, the tax cuts have boosted household disposable income – which in the past two quarters has risen at a 4.6% annual rate in real terms, the fastest since mid-2004. And with the household saving rate still negative, strong growth in household disposable income has been directly reflected in household spending, which rose at a 4.7% real annual rate in the six months ended March, up from 3.3% in the previous six months.

In effect, therefore, the Budget has redistributed income from the corporate sector, which over the past four quarters has saved the equivalent of 4% of GDP, to the household sector, which over the same period has dis-saved the equivalent of 0.4% of GDP: and in so doing has (almost by definition) boosted domestic demand.

Even though the economy appears to be operating on its thinnest margins of 'spare capacity' for more than three decades, there has thus far been no sign of a sustained acceleration in inflation. The household consumption expenditure deflator (the equivalent in the national accounts to the CPI) rose by just 2.2% over the year to the March quarter, down from a peak of 3.1% over the year to the June quarter last year. And annual growth in unit labour costs has slowed from 4.1% to 3.4% over the same interval – due to easing growth in average employee compensation rather than to rising productivity growth (indeed, disappointingly, productivity growth has actually slowed again over the past year).

So there's no 'smoking gun' in yesterday's figures pointing to an urgent need to tighten monetary policy any time soon.

But from a medium-term perspective the latest national accounts do serve to highlight the risks associated with spending all of the income gains derived from the commodities boom (rather than saving at least a proportion of them); and of any changes to the industrial relations system which might facilitate an acceleration in labour costs.

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