

# THE AUSTRALIAN

Enjoy the sugar hit as we flirt with economic ruin



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Treasurer Josh Frydenberg visits Carbon Revolution factory in Geelong as he sells the budget. Picture: NCA NewsWire/David Crosling

Economic growth requires political stability and secure property rights. Its drivers include low taxation, an educated, skilled workforce, and technological innovation. But the overwhelming influence for nations such as Australia is investment in business activities, roads and other infrastructure.

The budget papers note that Australia has weathered the COVID crisis better than other nations. Treasury maintains, “new business investment has picked up alongside Australia’s broader economic recovery, supported by government policy incentives implemented in response to the pandemic”. In fact, Australia actually shows a disturbing trend in the business investment component of GDP.

Private and public business investment combined (privatisation has reduced the public component) has seen its share of GDP oscillating on a downward trend.

Sixty years ago (during a mining boom), the investment share of GDP approached 25 per cent. This fell to around 15 per cent in the 1970s recession, recovered to a little under 20 per cent in the 80s mining boom, before falling back to around 15 per cent and again briefly rising to just below 20 per cent in 2013, during the most recent upsurge in mining activity. Business investment has since sunk to a historical low of around 10 per cent of GDP.

The budget papers anticipate an anaemic 1.5 per cent increase in business investment next year.

Rapid economic growth of countries in our region, including China, India, Vietnam and Bangladesh, is being driven by investment shares of GDP that are double Australia's.

Nonetheless, the government's economic forecasts remain bullish. But that is because they are conditioned by Treasury's Keynesian economic framework, in which government deficits stimulate the economy into a growth path.

That outcome is in itself highly unlikely but it rests on the deficit being a short-term measure to soak up under-utilised labour and capital, followed by a self-sustained resumption of growth on the back of an investment recovery with the resultant surge in economic activity repaying the deficit.

What we have instead is a permanent lift in spending bringing a budget deficit of 7.8 per cent of GDP, almost twice the deficits of Keating (1992-93) and Rudd (2009-10). The consequential level of government debt, which only 15 years ago had been eliminated, is 40 per cent of GDP.

Though increased spending offers a sufficient sugar hit to the economy, insulating the government from a voter backlash prior to the next election, its longer-term effects are ruinous.

Among its increased outlays on welfare, education and women, the government does doff its hat to the importance of productive investment. To this end, it has lowered some business taxes through allowing selective rapid write-offs of investment. And it has introduced a 17 per cent tax rate on returns from biotech and medical innovations.

Such "winner-picking" programs have never been successful — politicians and the public servants advising them just do not have the skillsets of merchant

bankers in selecting promising business opportunities, and their incentives are not the profit maximisation that drives business decisions.

The government does, however, understand the importance of lower energy costs to business and consumers, and claims its policies have brought lower prices. Yet here the government does not even fool itself since, while claiming success, it is providing stopgap subsidies for energy-intensive aluminium smelters and for gas plants to cushion the impact of coal plant closures. Those closures of low-cost, reliable plant result from discriminatory government policies favouring high-cost, poor-reliability wind and solar.

Instead of addressing these adverse effects, the government celebrates the billions of dollars spent on renewable energy and the consequent billions spent on augmenting networks, refashioning electricity markets and transforming hydro facilities into services to accommodate the intermittency of wind and solar. In fact, that expenditure detracts from rather than supports the productivity growth on which higher incomes depend.

Hence, not only is business investment languishing but its potency is being blunted by various forms of political intervention.

In addition to energy, this is evident in environment policies that force the dilution of productivity-oriented expenditure into costly time-consuming studies to justify firms' planned expenditures.

And some measures subsidise the transformation of agricultural land into carbon storage venues, while others support the diversion of agricultural water into outlets that supposedly promote environmental values.

Apologists for the budget correctly claim Labor would be even worse. But this confirms how politicians have seized the nation's finances and armed themselves with economic levers to keep themselves in power.

In undermining enterprise, the upshot will bring about either the slow economic decline seen in many Latin American countries or an abrupt economic crash. Australia's Constitution is based on that of the US, which sought to prevent the outcome of Benjamin Franklin's description of democracy as, "two wolves and a lamb voting on what to have for lunch". Such aphorisms by the American founding fathers were based on their studies of the Ancient World. They again seem prescient.

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