Opening Statement to the Senate Select Committee on Covid-19

By Saul Eslake, Independent Economist and Vice-Chancellor's Fellow at the University of Tasmania - 2nd July 2020

Madam Chair and Senators,

Thank you for the opportunity to appear before you today.

Australia has done very well in containing the spread of Covid-19, by comparison with what was initially feared, and by comparison with the outcomes to date in other 'advanced' economies. Moreover, what we have attained on the epidemiological front has been achieved at an economic cost which, although very substantial, is also likely to prove less than initially expected and less than that incurred by most other 'advanced' economies.

Nevertheless, our path out of the economic downturn induced by the measures required to deal with the risks posed by Covid-19 is, in my opinion, likely to be much less steep than the path into it was. And the slope of that recovery path will inevitably be influenced by the success, or lack of it, which other nations have in dealing with the virus, as well as by what we do ourselves.

In particular, I am skeptical of suggestions that Australia (or indeed any country) will have a 'V-shaped' recovery from the current recession. I have tried to avoid ascribing a letter to the trajectory that I think economic recovery may follow, because I don't think one exists, either in the Latin alphabet or in any other with which I'm even vaguely familiar.

Let me highlight what I mean by referring to the economic scenarios used by the Parliamentary Budget Office in its *Medium Term Fiscal Projection Scenarios* report published on 5th June. These scenarios were in turn based on the scenarios published by the Reserve Bank in its most recent *Statement on Monetary Policy*, on 8th May.

In the 'baseline' scenario used by the PBO, the *level* of real GDP won't return to its pre-pandemic (2018-19) level until the 2021-22 fiscal year.

Of even greater import, I would argue, is that even in 2021-22, the *level* of real GDP will still be 10% below where it was projected to have been in that year, in the *Mid-Year Economic and Fiscal Outlook* published in December last year.

In each of the years 2027-28 through 2029-30, the level of real GDP in the PBO's 'baseline' scenario is 3% below what had been projected in MYEFO.

This underscores the point which the Governor of the Reserve Bank, Dr Phillip Lowe, made when he appeared before this Committee on 28th May, that "we've got to keep the fiscal stimulus going until recovery is assured".

There is a significant risk of a setback to the economic recovery which seems to have started during May if all of the fiscal support measures which have been put in place since the onset of the pandemic are allowed to expire as presently scheduled at the end of September.

I can understand, and indeed sympathise with, the desire not to repeat the mistake which I think was made in Australia earlier this decade when fiscal support measures instituted during the global financial crisis weren't wound back once it became clear that they were no longer required - as it should have been once the Reserve Bank started raising interest rates in September 2009.

But, equally, we should not want to repeat the opposite mistake made by other countries (such as the UK, the US and Germany) in tightening fiscal policy too soon after the darkest hour of the global financial crisis had passed - as the Governor of the Reserve Bank also pointed out in his appearance before you in May.

Bastions of economic orthodoxy such as the OECD and the IMF have made the same point. In the words of the IMF's most recent *World Economic Outlook*, published last week,

> "The exit for targeted support should proceed gradually to avoid precipitating sudden income losses and bankruptcies just as the economy is beginning to recover its footing ...."
>
> ... and ...
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> "Where fiscal space exists [which I would say is a description which applies to Australia] targeted support can be replaced with public investment to accelerate the recovery and expanded social safety net spending to protect the vulnerable".

I very much agree with the Deputy Governor of the Reserve Bank, Dr Guy Debelle, who told an Economics Society 'webinar' on Tuesday this week that "there are no concerns about fiscal sustainability from increased debt issuance", because so long as interest rates on government debt are less than the growth rate of nominal GDP, growth in the economy will work to lower debt as share of nominal GDP.

In seeking to reduce the ratio of government debt to GDP over time (which I think is a desirable long-run objective), we need to be careful not to pursue reductions in the numerator in that ratio (the level of debt) so aggressively that we risk reducing the denominator (the level of GDP) such that the ratio of the two actually rises - as it did in Indonesia during the Asian crisis of the late 1990s, or in Greece in the early years of this decade.

We also, I believe, need to avoid - in the pursuit of greater 'self-sufficiency' in the sourcing of so-called 'strategic products' or for any other reason - policies which inhibit the movement of 'factors of production' (labour and capital) from low-productivity uses to higher-productivity uses. That is something which is essential if we are to lift the overall rate of productivity growth above the mediocre levels which we have experienced over most of the past two decades - which is in turn something which we need to achieve if we are to attain the growth rates required to reduce unemployment over time in the absence of 'tailwinds' in the form of rapid population growth and rapid growth in exports to China that we've enjoyed over the past two decades.

I'd like to conclude with an appeal to you to make a specific recommendation in your report to the Senate.

As you know, the measured unemployment rate (as published by the ABS in its monthly labour force survey reports) has become a particularly misleading guide to the true condition of the labour market during the current downturn. That's because of the large number of people who are counted as 'employed' even though they have worked zero hours; and the large number of people who, having been stood down or retrenched from their employment, are not 'actively looking for work', and hence are recorded as being 'not in the labour force', rather than 'unemployed'.

In current circumstances, a better guide to the 'true' level of unemployment is the number of people receiving the JobSeeker payment (as it's now called) or the Youth Allowance (Other) payment. Ordinarily this is a little bit higher than the number of people reported as 'unemployed' by the ABS, because people are allowed to earn a small amount before becoming ineligible for these income support payments. But the gap between the two has widened substantially during the current downturn: in May, the number of people receiving Jobseeker or Youth Allowance (Other) payments represented 12% of the workforce, well above the 'official' unemployment rate of 7.1%,

The Department of Social Services publishes monthly data on the number of people receiving these payments on data.gov.au, with a considerable lag. But in fact the DSS compiles this data weekly, as members of this Committee are aware, because the Secretary of the Department provided this data in evidence to this Committee on 30th April.

Otherwise, this information is not available to the general public. I cannot think of any reason why it should be a 'state secret', By way of contrast, the US Department of Labor has been publishing the American equivalent - the number of people filing initial claims for unemployment insurance benefits - at 8:30 am, Washington DC time, every Thursday morning since 1968. It would greatly assist with more timely and accurate assessments of the state of the Australian labour market if the DSS were to do the same.

The Australian Bureau of Statistics is to be commended, I think, for the efforts it has made to provide a wider range of data, in a more timely fashion, to help both policy-makers and analysts, and the general public, track how households and businesses, and the Australian economy more broadly, are responding to the challenges posed by Covid-19 and the measures necessary to deal with it. Other government agencies, including the DSS, should do the same.

I welcome the opportunity to answer your questions.

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