



Australia post elections: **a lucky or a sunburnt country?**



**Don't worry about the
world ending today.
It's already tomorrow
in Australia.**

Charles M Schulz (1922 - 2000)



Introduction

This paper provides an overview of the 2022 Federal Election outcome, including the major features of the campaign, economic implications as well as the influence of global economic forces. It is the end of the Morrison government in an Election which has seen the Coalition party decimated. The results of the Federal Election suggest that, overwhelmingly, 2022 was a climate policy election. In our 2022/23 Federal Budget review, we presented Australia's economic and investment case.¹ The incoming Labor government must balance short-term issues, such as cost of living and geopolitical tensions, with longer-term spending and environmental issues, at a time of deficit and a focus on debt reduction.



¹ Australia is facing economic headwinds with the lingering effects of the pandemic, while the Russia-Ukraine invasion and the Solomon Islands' deal renewed focus on national security and energy stability. Yet, Australia is in a better position compared to other developed nations, given its AAA credit rating, export capability, and relatively lower goods and wage inflation <https://www.mercer.com.au/our-thinking/federal-budget.html>

Beam me up Scotty – a new crew in the control room

Labor will form the next Parliament of Australia after winning the 2022 Federal Election on 21 May 2022. Anthony Albanese will become Australia's next Prime Minister with his vision for the country as a place where *"no one is held back, and no one is left behind"* and *"a better future for all Australians"*. The main party agenda is summarised below.²



Accelerate climate action. Boost renewables to 82% of the grid, and reduce emissions by 43% by 2030 and net zero by 2050. Place caps on the biggest polluters, make electric vehicles (EVs) cheaper and build a national EV charging network. Invest in hydrogen highways for heavy transport.



Improve Healthcare and child care. New Medicare Urgent Care Clinics, improved GP access, greater patient affordability, less hospital pressure and better management of chronic conditions, as well as subsidies on child care.



Increase tax on multinational companies (MNC) and limit deductions. Support a global 15% minimum tax on these companies, with changes to begin after 2023.



Support wage growth. Labor supports an increase in the minimum wage to keep pace with inflation, if it is recommended by the Fair Work Commission. Labor aims to close the gender pay gap, especially in the care industry (like healthcare, aged care).



Foreign relations. Labor will provide more aid funding to the Pacific, expand the transmission of Australian radio content, establish a Pacific defence school and boost support for aerial surveillance activities. It will also strengthen ties with the Indo-Pacific and will not allow defence spending to fall below 2% of GDP.



Enhance manufacturing ("Made in Australia") including a home-grown battery industry ("Powering Australia"). Fund investment in projects that innovate transport, defence, resources, agricultural and food processing, medical science, renewables and low emission technology manufacturing. It also pledges support for critical technologies such as quantum computing, artificial intelligence, robotics and software development. Labor wants 90% of Australians on the NBN by 2025.



Education. Provide 45,000 extra fee-free TAFE places and an extra 20,000 extra university places over 2022 and 2023, with a focus on areas where there is a skills shortage. Focus on providing work for apprentices, trainees and cadets on major government projects.



Housing: Under the "Help to Buy" scheme, Australians will be able to buy a home with a deposit of just 2% as part of Labor's equity scheme, which will cut the cost of buying a home by up to 40%. Labor will also make properties cheaper by building social and affordable housing by constructing 30,000 homes for families doing it tough, as well as those fleeing domestic violence, and frontline workers (like police, nurses and cleaners).

² Refer also <https://www.alp.org.au/policies>

Economic track records – Labor versus Coalition governments

It is fair to say that the uncertain international economic outlook emphasises the need for strong economic management. The possibility of a stagflation period akin to the 1970s is looming. Between 1970 and 2022, the Coalition has been in government for 28 years and Labor for 23 years – roughly equal periods. Both parties have shown evidence of reforms and intervention.

- **Reforms:** the Hawke-Keating economic reforms (1983-1996) opened the Australian economy to competition at home and abroad in the 1990s. The most influential economic decisions of the 1980s were the floating of the Australian dollar and the deregulation of the financial system, bringing to an end chronic inflation and balance of payments difficulties. It also saw the introduction of Medicare and superannuation. The Howard government (1996-2007) implemented gun control, privatisation and tax reforms.
- **Intervention:** 2008-09 triggered government stimulus spending by Labor, albeit of a much smaller magnitude than during the 2020-21 pandemic by the Coalition government. However, the size of the 2020-21 economic and social shock was also much greater.
- **International relations:** these have historically been less adversarial under Labor (Rudd, Gillard) than the Coalition (Abbott, Morrison). The Coalition government highlighted China, Russia and the arc of autocracies as a major campaign issue. Labor is likely to place more emphasis on diplomatic tone and conduct. A Labor government would potentially elevate the role of the Department of Foreign Affairs and Trade (DFAT).

It is difficult to assess whether one party has been more or less successful in managing the Australian economy through difficult periods, because we do not know how the economy would have behaved under the alternative party. Junankar (2005) in earlier research noted that overall the performance on economic growth was a draw.³

From the above, indications are individual determination and the incoming government's skills and experience, rather than party alignment, matters - as long ideology is not too extreme. Under the current global economic conditions, governments are running out of monetary and fiscal policy options, while at the same time running into geopolitical and energy security issues.

³ Junankar, P.N., 2005, Who is Better at Managing the Australian Economy: Labor or the Coalition? https://australiainstitute.org.au/wp-content/uploads/2020/12/DP79_8.pdf

Major policy issues facing the incoming government

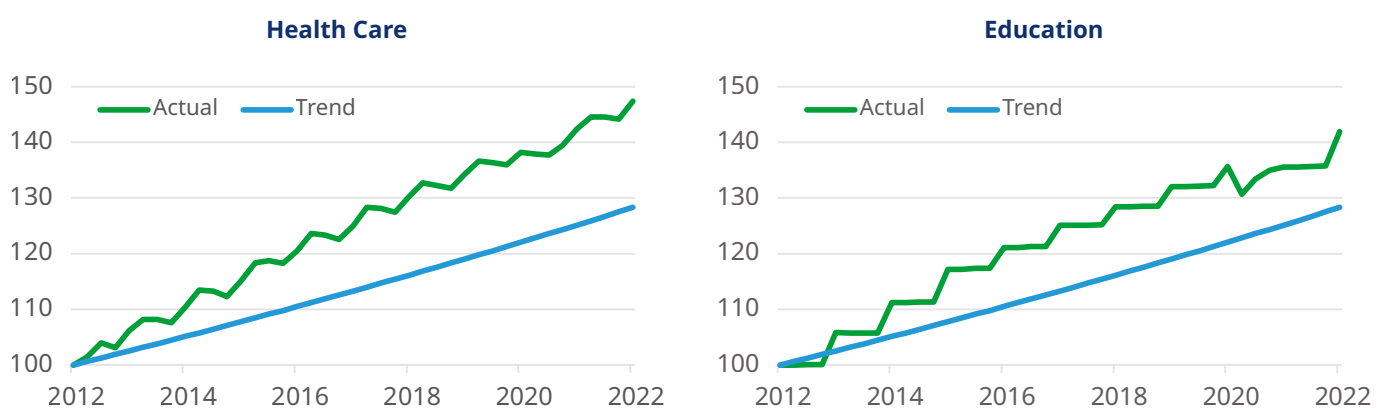
Reducing cost of living pressure – inflation, wage growth and immigration

Cost of living represents a challenge to households and firms, in particular energy prices.

- In the short-term, the government may decide to extend the temporary reduction in fuel excise if global oil prices stay at elevated levels.
- For lower income households, we also expect to see further living assistance rebates and (possibly) the extension of the low income tax offset.
- With household income levels still rising at levels below inflation, the government may influence the award setting process. Unions may also play an increasing role in workplace enterprise bargaining agreements. For many workers, market forces and low unemployment rates should further contribute to pushing up wage growth.

Addressing other cost of living issues, in education and health care, will require long-term solutions that aim to increase capacity.

Figure 1: Education and health care expenses have been increasing above trend



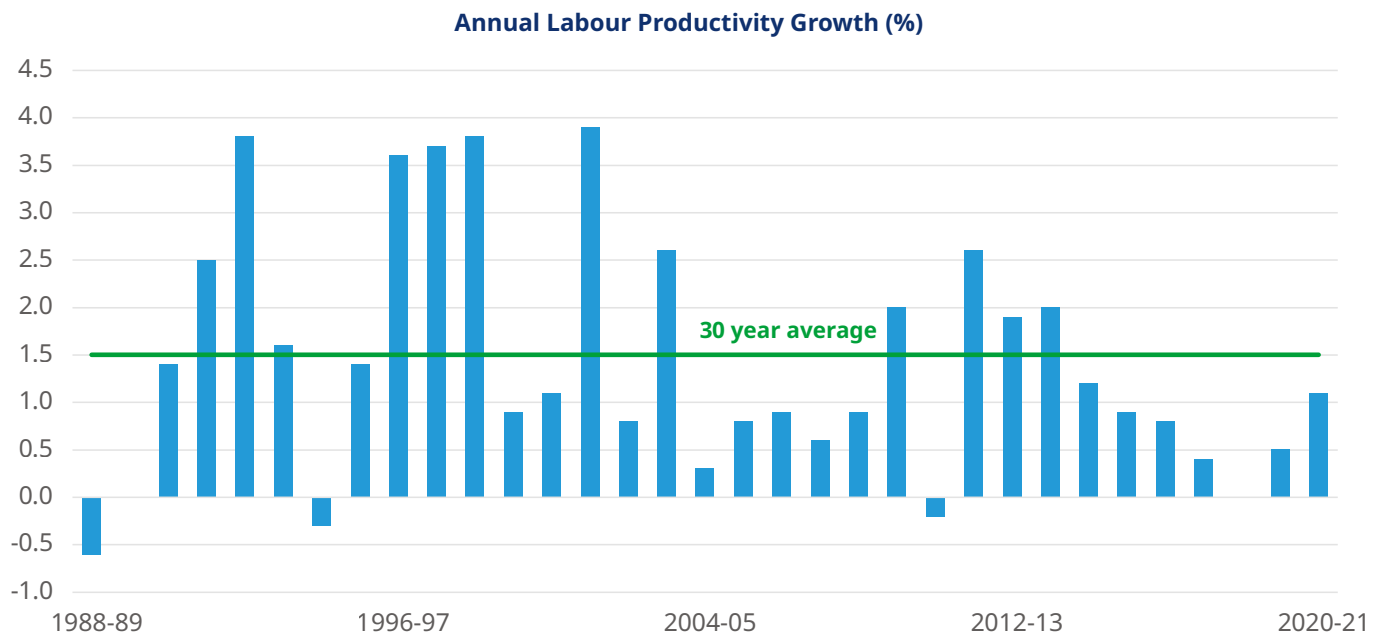
Source: ABS, Mercer

We believe the government will support further investment in education and health care. Immigration remains a key source of growth for the Australian economy and, while net migration flows were challenged due to the pandemic, we expect that the government will raise immigration caps with easier pathways for permanent residency.

Maintaining Long Term Prosperity

While cost of living pressures represent more immediate concerns for policy makers, ensuring Australia's long-term success will be an important policy objective for the government. In Australia, structural reforms undertaken during the 1970s and 1980s contributed significantly to lifting productivity and real wages. In recent periods however, productivity growth slowed along with real income growth. Therefore, further structural reforms in the economy will be necessary to unlock new growth and market opportunities. The global economy is continuing to modernise and markets are becoming increasingly more competitive through technology, digitalisation and growth in new economy sectors.

Figure 2: Australia's Productivity growth is declining



Source: ABS, Mercer

Key areas for improving productivity

Trade. Given continued trade tensions with China, Australia's unique competitive advantage in raw materials and agriculture may be further exploited through trade diversification and expansion into new markets. The Australia-United Kingdom Free Trade Agreement (Australia-UK FTA) was signed in December 2021, creating new export opportunities and jobs for businesses by eliminating tariffs on over 99% of Australian goods exported to the UK. More recently, the government finalised the Australia-India Comprehensive Economic Cooperation Agreement (AICECA).

Industry and education. Australia's industrial and education policy can be further strengthened to enable development of world-class capabilities. A number of Australian industries have already broken into global markets with the vast majority in agriculture and mining (like BHP), or finance (like Macquarie). More recently, Australian tech companies (like Atlassian, Canva and Afterpay) have joined them, albeit more of their own accord rather than as a result of government policy or direct funding. Australia's higher research capability ranks favourably on a global level and we expect the government to focus on enhancing the education and skills of the Australian workforce.

Infrastructure. Growth in infrastructure is needed to remain competitive as a nation, including the rollout of 5G, fast speed internet and data storage facilities. Under the Labor government, we also expect an increased uptake of EV, the roll out of a national charging grid and further investment into renewable energy sources and battery technology.

Property. Australia's population is projected to reach 38.8 million in 2060-61.⁴ Migration is expected to continue to be the largest source of population growth. Australia's greatest demographic challenge is the ageing population, due to increasing life expectancies and falling fertility rates. People are working later and we have more women in the workforce than in previous generations. Demographics present long-term economic and fiscal challenges, similar to those faced in most comparable countries. An adequate supply of new housing will be crucial in maintaining stable prices. Affordable housing initiatives, build to rent and more flexible zoning regulations will be key in ensuring balanced supply.

Taxation: Leaving aside possible taxes on MNCs, we view taxation policy by the government to remain relatively benign regarding individual tax policy, although it may from time to time engage in policy discussions on franking credits and CGT. At this point, it is unclear whether the government will restrict negative gearing or reduce CGT discounts on investment properties and/or shares, as mentioned in earlier Labor campaigns. The Labor government also proposed franking credit removal back in 2018, which would have especially affected pensioners.

⁴ Source: Intergenerational Report 2021. <https://treasury.gov.au/publication/2021-intergenerational-report>

Conclusions: a lucky or a sunburnt country once again?

Australia has shown remarkable resilience during major crises. Australia's success in overcoming the GFC in 2008/09 can be attributed to increased regulation and government stimulus, but also due to Australia experiencing its own banking crisis in 1992 (with the near failure of Westpac, the collapse of HIH in 2001 and NAB's rogue trading fiasco in 2006). Lending standards helped Australia avoid exposure to subprime and collateralized debt obligations CDOs, unlike American and European banks. Australia's economy was also buoyed by large resource exports to China at the time.

Successfully overcoming the pandemic in 2020/21 can be attributed to our remote location, but also because Australia was in a strong financial position to provide the necessary stimulus. In addition, diversification to economic growth in both Eastern and Western economies helped Australian exports. As a result, Australia outperformed major developed economies during both periods.

Following the Federal Election outcome, some general conclusions seem fair at this point in time:

- **A faster transition to renewables will put additional short-term pressure on traditional energy supply sources and prices.** This needs to be carefully managed.
- **More focus on fair pay and the gender pay gap,** and raising wages in certain sectors, while good for equalising income and wealth distribution, **could accelerate wage inflation, which has so far been relatively dormant.**

Despite the incoming government's best intentions, it should be acknowledged that we are in a global maelstrom.

- The **labour market** is likely to follow global trends with unemployment rates hitting multi-decade lows in many countries and, as a result, this is pushing up wage growth. For Australia, immigration policies are likely to be key. The government wants to end the nation's dependence on short-term visa holders and make it easier for foreign workers to become permanent residents.
- At the same rate, the **housing market** is likely to follow global trends, despite the expected government subsidies for first homebuyers, as similar patterns in interest rates and housing affordability have emerged in many Anglo-Saxon countries. The RBA may lag other central banks at present, but it will eventually catch up, which could lead to a correction in the housing market.
- From an **inflation** perspective, Russia's attack on Ukraine and the lockdowns in China have increased anxiety about global supply chain disruptions. Securing energy and food sources is becoming increasingly important for large and faster growing countries (like China and India) even at the expense of environmental factors.

Given the preponderance of global exogenous factors, a bit of luck will be needed. However, hard work and sound policy formation by the incoming government will be necessary to reduce the short-term cost of living pressures and secure Australia's long-term prosperity. We have highlighted some recommended areas of focus for productivity improvement. Otherwise, a lucky country may risk turning into a sunburnt country!



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