Economic

Roundup

Issue 1, 2012

ISBN 978-0-642-74810-2

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Contents

China's emergence in global commodity markets

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China today dominates many of the world's commodity markets. Its demand for commodities rose dramatically in the years leading up to the Global Financial Crisis, held up well during the crisis as prices fell, and continued to rise post-crisis. The pace of economic development, and processes of industrialisation, urbanisation, and rising per capita incomes, has seen China become a major commodity consumer on global markets, particularly in metals and energy.

This paper analyses the history of China's demand for commodities — across energy, metals and agriculture — and the potential path of future demand. It compares China's experience in recent decades with that of other recent industrialising economies, and considers the scale and pace of China's commodity demand and its own domestic production on global commodity markets. The long term outlook for Chinese commodity demand remains strong as the underlying drivers of Chinese commodity demand still have some time to run. China's per capita consumption of key commodities, like per capita income, is still well below that of major advanced economies. Moreover, given the scale of China's appetite for commodities, small shifts in its domestic demand-supply balance could have major implications for global commodity markets.

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1 The authors are from International and G20 Division, the Australian Treasury. This article has benefited from comments and suggestions provided by Sarah Woods, Julia Minty, Bill Brummitt, Michael Callaghan, Hui Yao, Veasna Kong, Dougal Horton, Alison Keys and James Holloway. The views in this article are those of the authors and not necessarily those of the Australian Treasury.

Introduction

Since economic reforms began in 1978, China has experienced an unprecedented phase of industrialisation and economic development. Annual economic growth of around 10 per cent over the past 30 years has centred on a development model that is heavily reliant on investment, which has helped accelerate the structural processes of industrialisation, urbanisation and motorisation.

To cater to the demands of rising incomes, and to meet its growing infrastructure needs, China's demand for commodities has risen rapidly in recent decades, and accelerated since 2000. As well as being a substantial source of global commodity demand, China is also a substantial global commodity producer, with significant domestic reserves of many commodities such as coal and iron ore, and the world's largest producer of wheat and rice. Nonetheless, production has not kept pace with the surge in demand, leading China to source an increasing share of its commodity needs on global markets.

Future Chinese commodity demand and supply will be heavily influenced by the trajectory of Chinese economic policy, particularly measures to transition towards sustainable growth with a greater focus on domestic consumption, rather than exports and investment, as the source of gross domestic product (GDP) growth. China has also demonstrated a strong commitment to reduce its energy intensity, by placing a high priority on energy conservation and environmental protection.

China's effect on global commodity markets in recent years has been magnified by delays in the global supply response for many commodities. The sheer magnitude of the pick-up in demand for commodities at the beginning of the last decade, particularly for China and other emerging economies, was largely unforeseen. This unanticipated increase in demand placed considerable pressure on global commodity supplies, which struggled to keep pace with rising demand.

The weakness in the commodity supply response seen in recent years has its roots in the low commodity prices of the late 1980s and 1990s. Low prices led to reduced global investment in research and development, exploration and production. The strong prices of the mid-2000s generated a supply response but it came with a significant lag as producers responded to higher prices only after the trend in prices had become firmly entrenched.[2] Similarly in agricultural markets, growth in production has slowed

2 Many investments in supply were postponed due to the global financial crisis, and many projects initiated prior to the crisis have yet to add to existing capacity, due to the lags in translating the investment into new production, particularly in energy and mining. For example, while investments by 25 leading coal companies rose by about 4.5 per cent to US$12 billion in 2009, this rise was much less compared to 2008, when it rose 18 per cent. See International Energy Agency (2010) and World Energy Outlook (2010).

since the late 1980s, with growth in both yields and the land area devoted to crops declining significantly. The lack of new investment in agriculture reflects, until recently, the multi-decade decline in the real prices of agricultural output (Coates, Devlin and Woods, 2011).[3]

The paper is structured as follows. The first section briefly discusses China's economic development over the past three decades. The subsequent three sections cover trends in Chinese demand, supply and global trade for energy, metals and agricultural commodities. It also compares China's experience in recent decades with that of other recently industrialised economies.

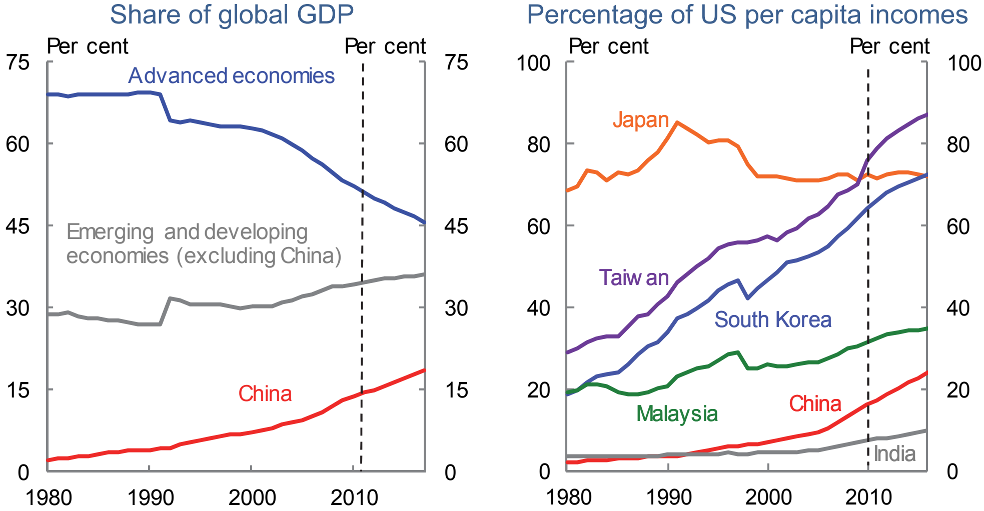
China's economic development, industrialisation and urbanisation

China's remarkable growth over the past 30 years has meant that its economy has doubled in size every seven to eight years. It now accounts for almost 15 per cent of global GDP on a purchasing power parity (PPP) basis and has accounted for almost 70 per cent of the increase in the weight of emerging market economies in global GDP since 1990 (Chart 1). Investment has been a key driver of China's growth, particularly over the past decade, and now accounts for nearly 50 per cent of GDP.

Rapid economic development has spurred rising per capita incomes for Chinese citizens. At the start of the reform period, China's GDP per capita (on a PPP basis) stood at around 2 per cent of that of the United States (US) (less than India, Vietnam, Laos and many other emerging Asian economies). More than 30 years later, in 2011, that share has grown to around 17 per cent. In another five years, the International Monetary Fund (IMF) projects that China's GDP per capita will be close to one-quarter of that of the US and around a similar level to where Korea was in the early 1990s (Chart 1).

3 According to the Food and Agriculture Organization of the United Nations (FAO), the rate of growth in agricultural production is expected to fall to 1.5 per cent per annum between now and 2030, and to 0.9 per cent between 2030 and 2050, as compared to 2.3 per cent since 1961. See FAO of the United Nations (2009).

Chart 1: China's economic development in a global perspective



Source: *IMF World Economic Outlook*, April 2012.
Notes: GDP is in PPP dollars.

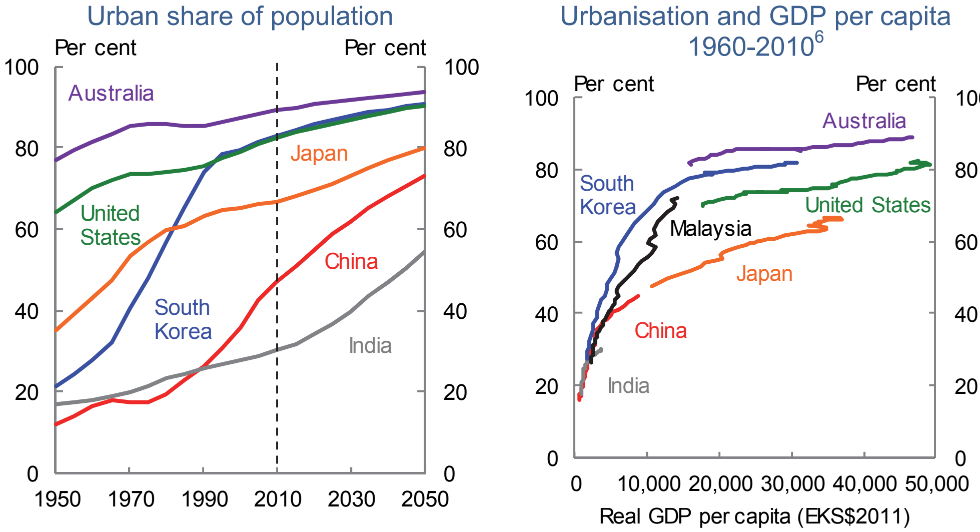
Rising incomes have in turn led to changing consumer tastes, such as increased demand for durable goods (such as cars and whitegoods) and a shift towards more expensive protein and nutrient-rich foods. This trend is set to accelerate with Kharas and Gertz (2010) estimating, based on present trends, that by 2021 there could be over 670 million middle class consumers in China, compared to only 150 million in 2010.[4]

China's economic development has coincided with rapid urbanisation, consistent with the experience of other earlier industrialising economies (Liu and McDonald, 2010). Economic reforms from the late 1970s set in train processes of industrialisation, capital deepening and productivity improvement that increased the demand for labour in urban areas, with workers attracted to cities by higher wages (Zhang and Song, 2003). The urbanisation rate increased rapidly from 19 per cent in 1980 to 50 per cent in 2011, and the United Nations (2012) projects that it will continue to rise steadily to 73 per cent by 2050. While China's urbanisation is rising rapidly, the share of the population residing in urban areas still remains below that of major advanced economies, and below the levels of other industrialising economies – such as South Korea and Malaysia – for the same level of per capita income (Chart 2).[5]

4 The authors define the global middle class as those households with daily expenditures between \$10 and \$100 per person in purchasing power parity terms. The lower bound is chosen with reference to the average poverty line in Portugal and Italy.

5 The future direction of the Chinese *hukou* system, whereby movement of citizens between urban and rural areas is managed, will significantly influence the pace of future Chinese urbanisation (Zhang and Song, 2003; Golley and Meng, 2011).

Chart 2: China's urbanising population

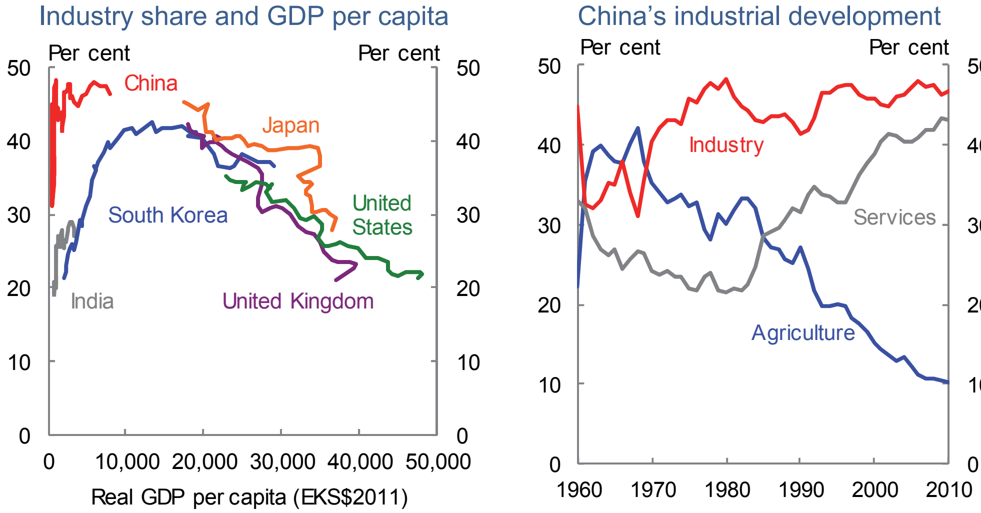


Source: United Nations *World Urbanisation Prospects*: *The 2009 Revision*; World Bank *World Development Indicators 2011*; The Conference Board Total Economy Database, January 2012.
Notes: GDP per capita is in US$2011 weighted using output at Èltetö-Köves-Szulc (EKS) PPP exchange rates.

China has industrialised quickly compared to other Asian economies, reflecting in part its bias towards industrial-led development in a centrally-planned economic system. The industry share of Chinese GDP has remained at or above 40 per cent for the past 35 years, at or higher than the levels seen in earlier industrialising economies, such as South Korea, Japan and the United States, at equivalent income levels (Chart 3) (BP, 2011a). However, it is likely that industry's share of GDP will fall as the Chinese economy continues to shift towards the production and consumption of services. The share of services in Chinese economic output has already risen from 20 per cent to 40 per cent since the early 1980s, broadly offsetting the declining share of agriculture (Chart 3).

6 Data for Japan refer to the period 1965-2010 only.

Chart 3: China's industrial development



Source: World Bank *World Development Indicators* 2011; China CEIC Database, Australian Treasury; and the Conference Board Total Economy Database, January 2012.

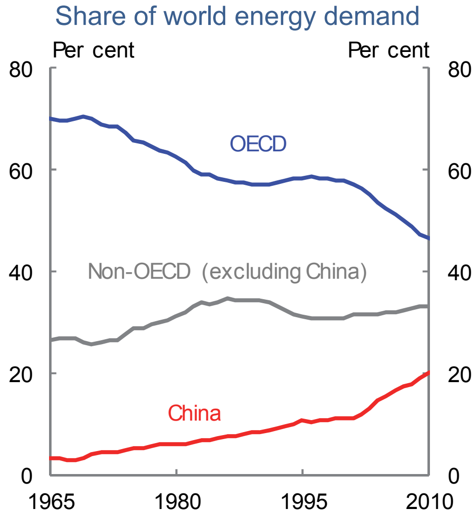
China's rising energy demand

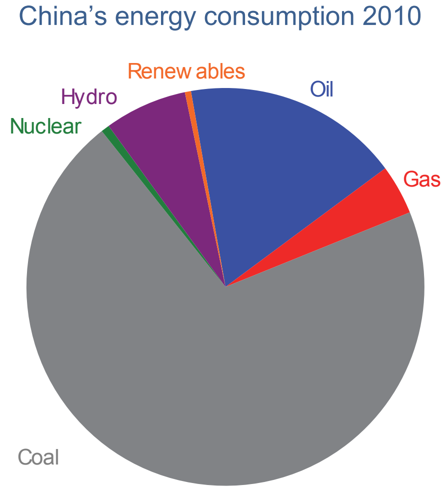
A direct consequence of China's rapid economic rise has been its rising demand for energy, which has had a significant impact on global markets for energy commodities. China's share of global primary energy consumption has risen from 8 per cent in 1990 to 20 per cent in 2010 (Chart 4). In particular, oil and coal demand has increased rapidly over the past two decades, and accelerated since 2000, reflecting China's rapid GDP growth and the structural shift in its economy towards energy-intensive heavy industry and infrastructure investment.

China's energy consumption is sourced predominately from coal, which accounts for 70 per cent of its total energy needs, compared to 30 per cent globally (Chart 4). Reflecting China's strong, energy-intensive economic growth, China's share of global coal consumption has risen to almost 50 per in 2010, up from 29 per cent in 2000.[7] China's dependence on coal-powered energy largely stems from its significant indigenous coal reserves. China accounts for 13 per cent of the world's proven coal reserves (behind the US and Russia) and is currently the world's largest consumer and producer of coal, including metallurgical coal used in steelmaking (BP, 2011).

7 Around one-half of China's coal is used in the electricity sector, with a further quarter used directly in industrial sectors including the production of steel and pig iron. Chinese electricity production has increased fourfold in the past fifteen years (IEA, 2011).

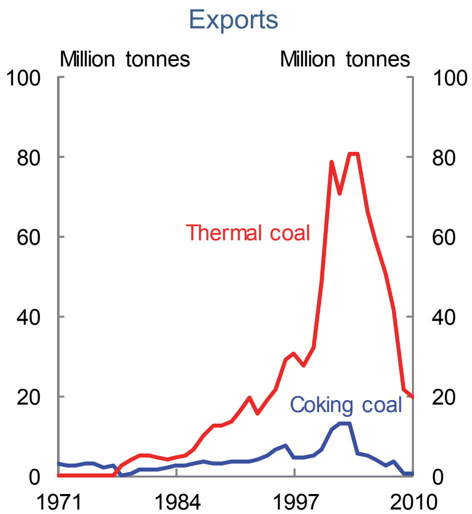
Chart 4: Chinese and global energy consumption

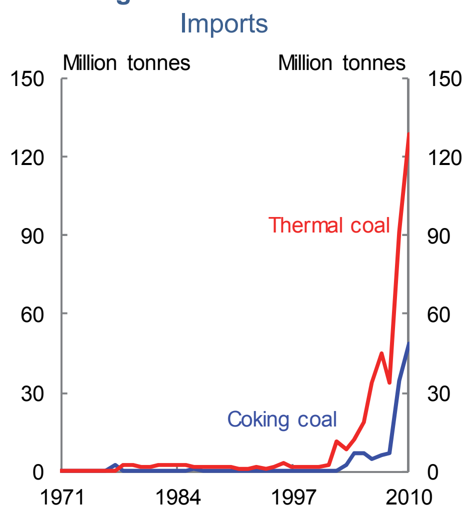




Source: *BP Statistical Review of World Energy*, 2011.
Note: measured in million tonnes of oil equivalent.

Chart 5: Chinese thermal and coking coal trade





Source: International Energy Agency, *Coal Information 2011*, OECD, Paris; and Australian Bureau of Agricultural and Resource Economics and Sciences.
Notes: Thermal coal is the sum of anthracite, sub-bitumous and other bitumous; coking coal refers to bitumous coal; 2010 figures are IEA estimates.

Recently, large government infrastructure-intensive stimulus has added substantially to coal demand for use in steel production and electricity generation. At the same time China has struggled to expand its coal mining and rail-transport infrastructure quickly enough to move coal from its large inland regions to industrialising coastal regions where coal demand has been strongest.[8] In recent years the Government has also stepped up its efforts to alleviate the environmental impacts of coal production and consolidate the coal industry by closing smaller private coal mines, thereby slowing growth in domestic coal production. Therefore, despite abundant domestic supplies, China has become the world's second largest thermal and coking coal importer behind Japan, accounting for 16 per cent of global thermal coal imports and 18 per cent of global coking coal imports (Chart 5).[9]

Similarly, China's consumption of oil has surged over the past decade, increasing at an annual rate of 6.8 per cent, and accounting for nearly one-fifth of global oil consumption. Increased demand for transportation fuel, partly stemming from rising automobile ownership, as well as demand for petrochemical feedstocks and construction-related petroleum products (that is, bitumen, ashphalt, lubricants, and naptha), has led to increased oil consumption (Standard and Poor's, 2011). While China is a significant oil producer, sharply rising demand transformed China from a net oil exporter to a net importer, and subsequently the world's largest importer in 2008 (Chart 6). In 2009, China surpassed the US as the largest consumer of oil, as well as the world's largest automobile market.

Chinese natural gas consumption has also risen, albeit from a low base (Chart 6). While annual consumption growth has averaged 15 per cent over the past 10 years, the share of natural gas remains at only 3 per cent of China's energy mix. Currently, natural gas is largely used as feed stock in chemical fertilisers, but it is expected to play an increasing role in electric power generation and residential energy use. The increase in natural gas consumption has in part been driven by the Government's commitment to accelerate the transition from fossil fuels to cleaner energy sources, the discovery of gas fields and the construction of pipelines. The use of gas is being promoted by a system of price regulation, and facilitated by major developments of gas supply infrastructure — including pipelines from gas fields in Western China and nearby countries, and liquefied natural gas (LNG) import terminals. China has in place a policy objective to increase the energy share of natural gas to 8 per cent by 2015 in order to improve energy efficiency and energy diversification (Jacobs, 2011). This will make China the world's third largest gas market after Russia and the US (IEA, 2010).

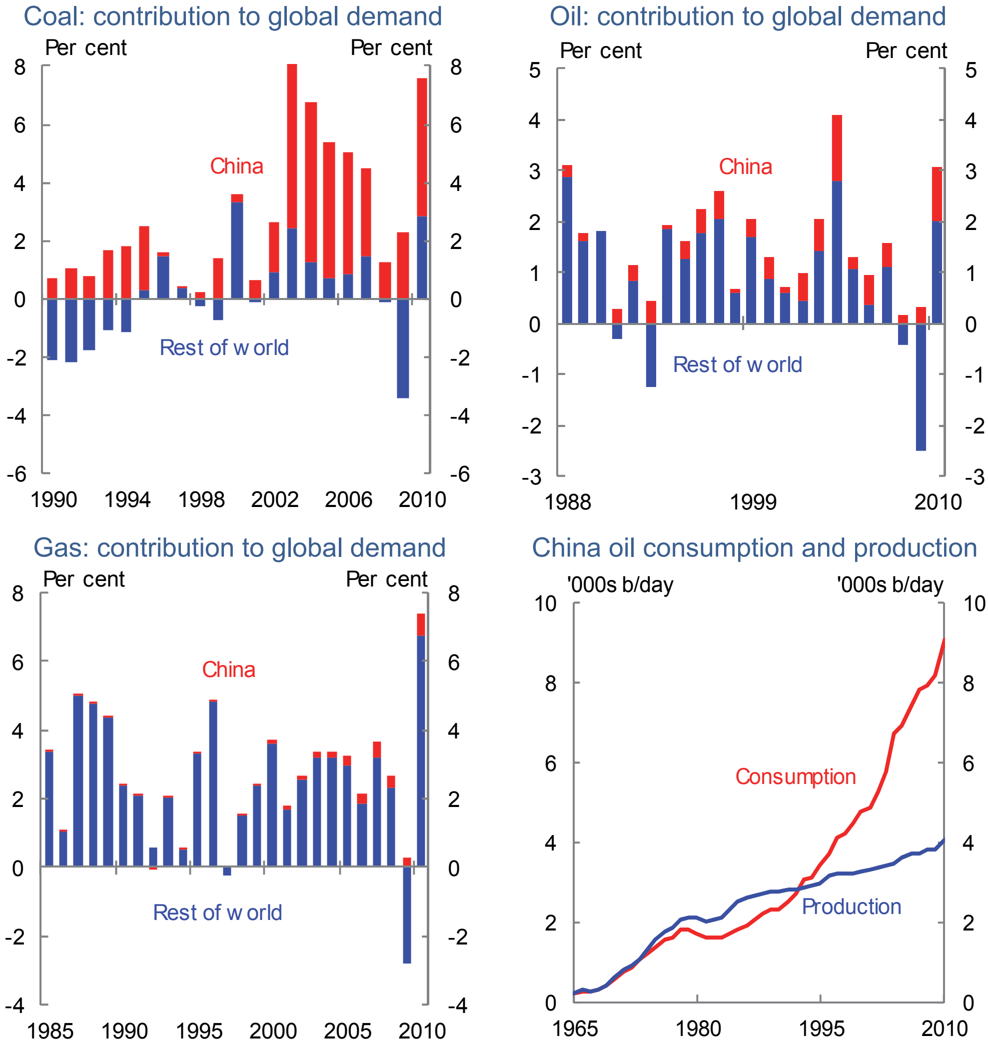
China remains largely self-sufficient in natural gas as a result of large reserves in the remote north and western regions, although China's dependence on natural gas imports is expected to increase further in the medium term. China has only recently established itself as a buyer of LNG, after commencing imports in 2006. LNG now

8 The northern provinces of Inner Mongolia, Ningxia and Shaanxi together account for 70 per cent of total recoverable coal reserves, well away from coal demand centres in the east and south (Tu, 2011).

9 Coal is the least globalised of the world's major energy sources, with only 15 per cent of production traded internationally.

accounts for 12 per cent of total Chinese natural gas consumption, and Chinese imports account for 4 per cent of global LNG trade.

Chart 6: China's impact on global energy markets



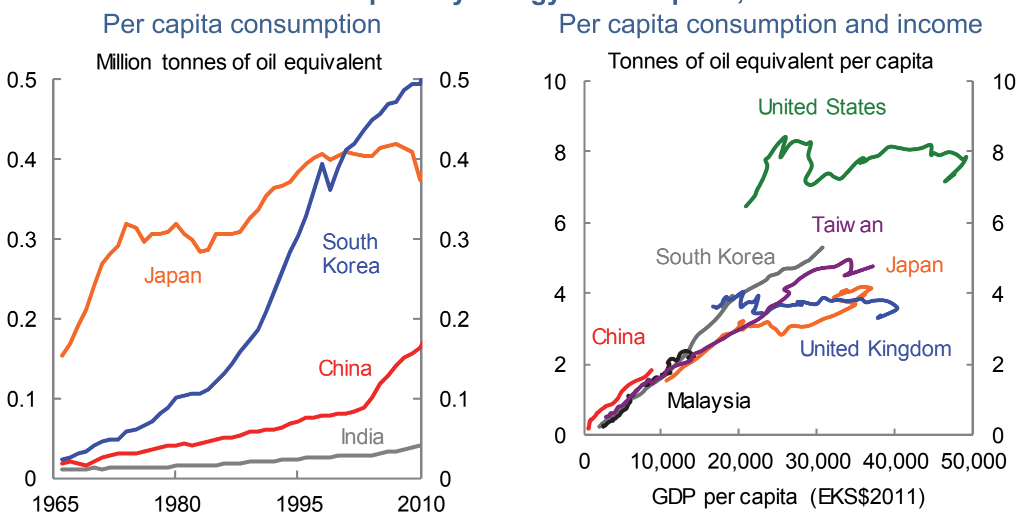
Source: *BP Statistical Review of World Energy*, 2011.
Notes: Coal refers to the sum of bituminous coal and anthracite (hard coal), and lignite and brown (sub-bituminous) coal.

Drivers of Chinese energy demand

China's future energy demand will depend upon the interaction of a number of trends, including the future trajectory of Chinese economic growth, the rate of urbanisation, trends in energy efficiency, the take up of alternative energy sources, and changes in economic structure — particularly the share of industry, and especially heavy industry, in China's future economic output.

To date the evolution of China's per capita primary energy consumption is broadly on par with Taiwan and South Korea at similar stages of their economic development (Chart 7). Growth in Chinese energy demand should slow as income per capita reaches around US$15,000 to US$20,000 as the Chinese economy transitions from heavy and energy intensive processes to lighter, higher value-added production (Cheung and Morin, 2007). In fact, Chinese per capita energy consumption will likely peak earlier than previous industrialising economies due to improvements in the energy intensity of GDP arising from the diffusion of new technologies, China's growing commitment to energy conservation and the prospect of higher real energy prices in coming decades.

Chart 7: Trends in primary energy consumption, 1965-2010

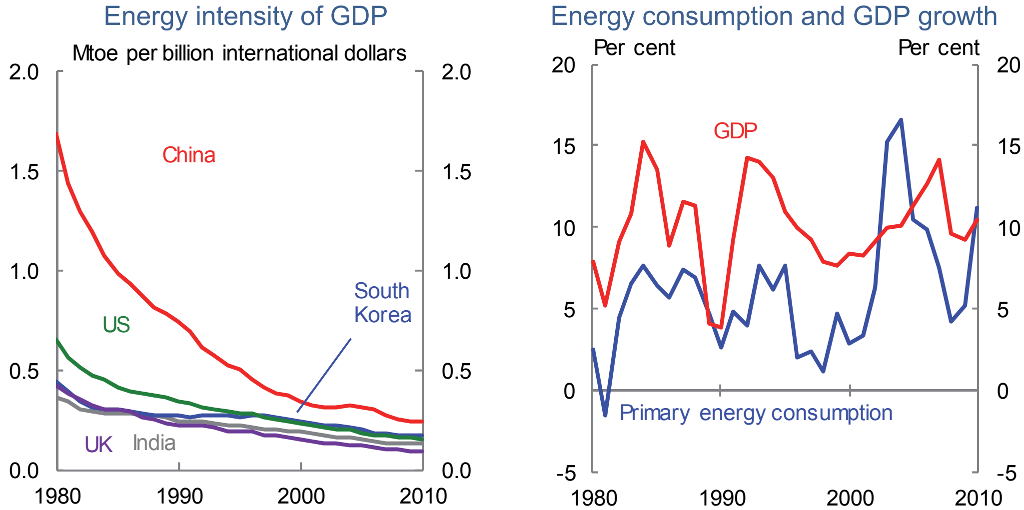


Source: *BP Statistical Review of World Energy 2011*; The Conference Board Total Economy Database, January 2012; and CIEC Asia Database.

After starting out with enormously high energy intensity per unit of GDP during the 1980s and 1990s, China experienced sharp declines in energy intensity (in PPP terms) as it converged with other recent industrialising economies and major advanced economies (Chart 8).[10] These improvements reflected increased trade in energy and the rapid adoption of common technologies arising from intensified globalisation, as well as government regulations to shut down small inefficient power plants and a partial shift away from subsidized prices and central planning (Garnaut, Howes, and Jotzo, 2008). Recently declines in Chinese energy intensity have stalled as the share of heavy, commodity-intensive industry has risen, which, together with increased infrastructure investment, has seen energy consumption growth outstrip GDP growth from 2003 to 2004, and again in 2010 (Chart 8).

10 China's energy intensity is much higher and has declined at a slower rate if market exchange rates are used to compare economies, reflecting the relatively smaller comparative size of the Chinese economy in market-exchange rate terms, compared to PPP terms.

Chart 8: Trends in energy intensity of GDP, 1980-2010



Source: *BP Statistical Review of World Energy 2011* and IMF *World Economic Outlook*, April 2012; CEIC Database.

Notes: The left hand chart refers to energy intensity expressed as million tonnes of oil equivalent (mtoe) per billion international dollars in GDP in PPP terms. GDP growth in the right hand chart is specified in constant renminbi (RMB) prices.

In more recent years, China has also demonstrated a growing commitment to limit growth in its energy consumption by placing a higher priority on energy conservation and environmental protection. China's 12th Five-Year Plan covering the period 2011 to 2015 concentrates on energy efficiency and the use of cleaner energy sources. It includes targets to cut energy consumption per unit of GDP by 16 per cent by 2015 and to cut CO2 emissions per unit of GDP by 17 per cent as well as significant investments in the supply of renewables. China has also announced plans to introduce city and provincial level pilot carbon emission trading schemes in the near future and to develop an economy-wide scheme within the current decade.

Meanwhile global energy prices are at present expected to remain higher than those facing the previous round of industrialising economies, including South Korea and Taiwan, during their equivalent stages of development through the 1980s and 1990s (IEA, 2011).[11] These factors should constrain future growth in energy demand and reduce the peak in China's per capita energy consumption vis-a-vis earlier industrialising economies.

Notwithstanding the potential for energy prices to remain high and pressure to meet environmental goals, prospects for future Chinese energy demand growth remain strong, given that China's per capita consumption of energy remains at only one-third

11 Global energy prices remained below their long-term average in real terms from the mid-1980s through to 2000, based on the IMF's international financial statistics energy price index, deflated by the United States GDP deflator (Coates, Devlin and Woods, 2011).

of the average of Organisation for Economic Co-operation and Development (OECD) members. The International Energy Agency (2011) estimates that China's primary energy demand will rise by 2 per cent per annum to 2035, at which point China will account for 23 per cent of global energy demand. While gas and non-fossil fuels are expected to take on a greater share of China's energy mix in future decades, the transition in the fuel mix will occur slowly due to long asset lifetimes for existing energy infrastructure.

Looking ahead, China is expected to consume nearly 70 per cent more energy than the United States in 2035, be the largest oil consumer and oil importer, and will continue to consume nearly half of world coal production (IEA, 2011). Despite this, China's per-capita energy consumption will remain less than half the level of the United States in 2035 (IEA, 2011). China's electricity demand is projected to almost triple from 2008 to 2035, requiring capacity additions equivalent to 1.5 times the current installed capacity of the United States (IEA, 2010). Industry will still provide the largest single contribution to China's increased final energy demand in 2035, although industry's share of energy demand should decline as demand is increasingly driven by domestic consumption as a growing middle class generates increased demand for motor vehicles, electrical appliances, and other energy-related goods.

China's demand for industrial metals

China's rise as a manufacturing and industrial powerhouse has meant that its demand for industrial metals has surged. The construction of urban housing and the provision of urban infrastructure such as roads, railways, sewerage systems and electricity generation and distribution systems have generated sharply higher demand for metals such as copper, aluminium and steel over the past two decades. Meanwhile long-term investments in manufacturing capacity and infrastructure, particularly since China's accession to the World Trade Organisation (WTO) in 2001 and subsequent manufacturing boom, have also contributed to growing Chinese metals demand. The share of investment in GDP has increased from 35 per cent in 1980 to 49 per cent in 2010. As a share of fixed asset investment, infrastructure accounted for 27 per cent and manufacturing for 31 per cent. Residential investment has also become an important source of commodity demand, with its share of GDP having increased from 5½ per cent in 2004 to around 9 per cent in 2011 (Reserve Bank of Australia, 2012). The bulk of Chinese steel and copper is used in construction and infrastructure.[12]

Industrial metals embodied in Chinese manufactured goods — for both domestic consumption and export — are also an important source of metal demand.

12 Construction accounted for 55 per cent of Chinese steel consumption in 2008, followed by machinery (18 per cent), automobiles (6 per cent), rail, shipping and fuel (5 per cent), and home appliances (2 per cent) (Roberts and Rush, 2010). As of 2010, 56 per cent of copper was used in construction and infrastructure (Hunt, 2011).

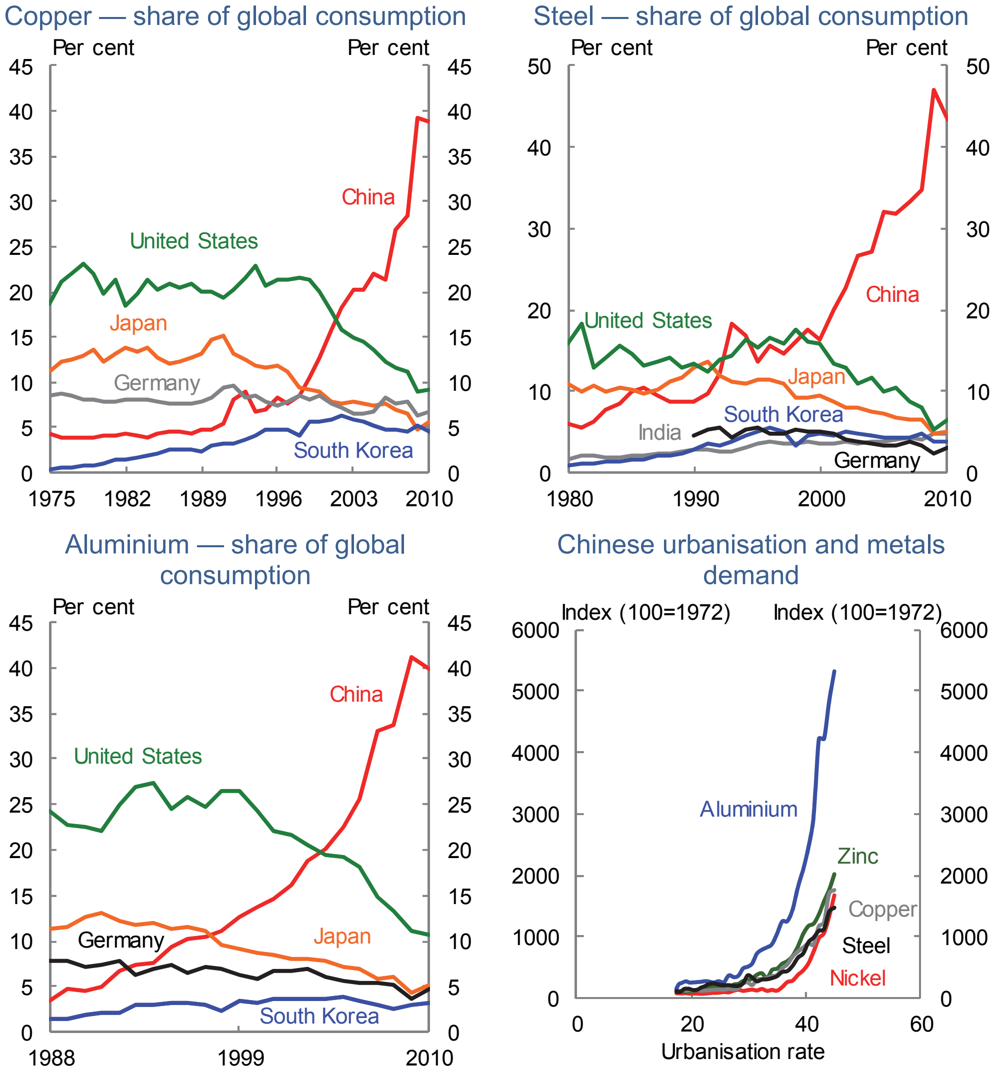
Manufacturing accounts for 40 per cent of Chinese GDP, with at least a quarter of steel consumption directly used in manufacturing industries such as machinery, automobile and home appliances (Holloway, Roberts and Rush, 2010). These sectors are also a key driver of aluminium demand (World Bank, 2009).[13] Moreover Roberts and Rush (2010) estimate that 10 per cent of the domestic supply of metals products are directly embodied in manufactured exports. Embodied metals exports may become an increasingly important share of domestic metals demand as China moves up the value chain towards more sophisticated manufactured goods for export (that is, machinery, automobiles and electronics).[14]

Infrastructure and manufacturing activity has resulted in metals demand sharply outpacing GDP growth. For example, China's consumption of copper and aluminium has increased by annual average rates of around 16 per cent over the past decade, in line with the rising urban share of China's population, and consistent with earlier processes of urbanisation among former industrialising economies (Chart 9) (Liu and MacDonald, 2010). With its rapid growth, intensive use and sheer scale, China has become the world's largest consumer of steel, aluminium, and copper, accounting for around 40 per cent of global consumption for each — a share two to three times larger than that of Japan or South Korea at the peak of their respective metals demand cycles (Chart 9).

13 Alternative estimates from China's official input-output tables suggest that, in value terms, manufacturing may account for a somewhat larger share of steel consumption than these figures imply (Roberts and Rush 2010).

14 This is particularly the case for non-ferrous metals such as copper and aluminium, which have a higher value to weight ratio and are therefore more likely to be traded.

Chart 9: Copper, steel and aluminium consumption



Source: ABARES *Australian Commodities*; BREE *Resources and Energy Statistics 2011*; World Steel Association *Steel Statistical Yearbooks*, various years; World Metal Statistics, various years; United Nations *World Population Prospects: The 2010 Revision*; United Nations *World Urbanisation Prospects, The 2009 Revision*.

Chinese metals production and trade

China's rapidly growing demand for industrial metals has been matched by its increased production. China has been the world's largest producer of steel for the past decade, producing almost half of the world's steel, three times as much the United States and Japan combined, owing to the emphasis on establishing steelmaking capacity since the early days of the country's push for industrialization. The steel industry is of strategic importance to China and has undergone major reforms over recent decades. Greater autonomy of state owned enterprises (SOEs) in the early 1980s, which gave them greater access to advanced technologies, have supported rapid output growth.[15]

In fact, rising production has seen China become a net exporter of steel as well as aluminium ingots and alloys, despite closing some of its least efficient aluminium smelters in 2010 to meet energy efficiency and environmental targets.[16] In contrast copper production continues to lag consumption, leading to rapidly rising imports equivalent to 40 per cent of world refined copper trade.[17] China's increased metals production has in turn spurred rapid demand for intermediate inputs to refined metals production, including iron ore, metallurgical coal, alumina, and copper ore.

In particular, China's share of global iron ore consumption has more than doubled since the beginning of the 2000s to reach 52 per cent in 2010 (Liu and Grafton, 2011). Chinese iron ore production has been unable to keep pace with sharply rising demand as a result of transportation bottlenecks, low-quality ores and high marginal costs of production. Despite being the world's fourth largest iron ore producer (producing 15 per cent of global supply), China dominates global iron ore markets and accounted for around 70 per cent of global imports in 2009 (Christie, Mitchell, Orsmond and van Zyl, 2011).[18] Around 40 per cent of its iron ore imports are sourced from Australia (amounting to an annual trade of around 280 million tonnes, or A$40 billion, in 2010-11).

Over the next decade, the scale of production of industrial metals will continue to increase as its industrial concentration grows and out-dated technologies are phased out, but it is unclear whether this will be sufficient to keep up with rising demand. In any case China is likely to remain dependent on imports for a number of key intermediate inputs to metals production.

Prospects for future Chinese metals demand

Measured in terms of metal consumption per unit of GDP, metal intensity has tended to increase in line with economic growth and as the structure of the economy shifts towards more metals-intensive manufacturing and heavy industry (McKay, 2008). The

15 See Holloway, Roberts and Rush (2010) for discussion on the growth of the Chinese steel industry over recent decades.

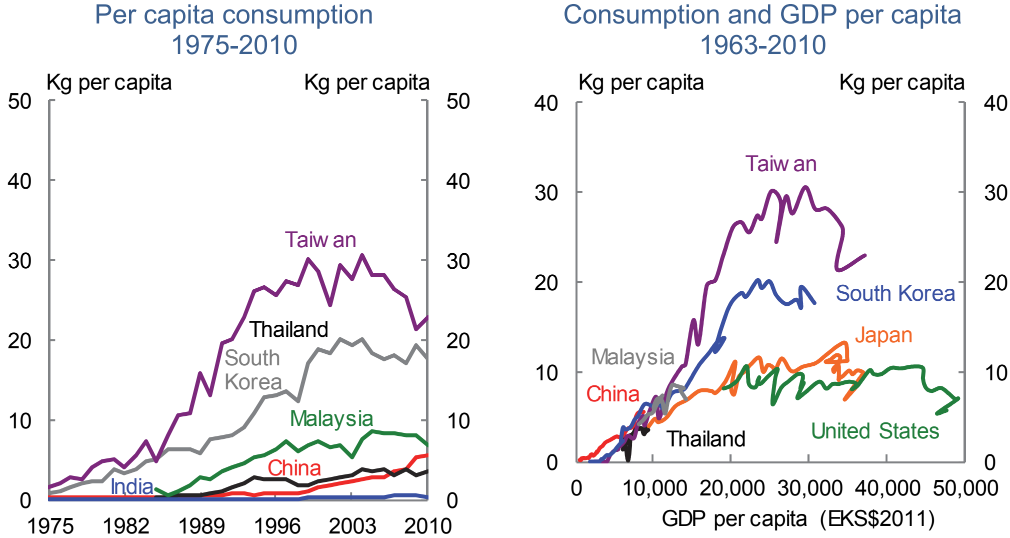
16 Much of China's aluminium is produced at small and midsize smelters that are major employers in their regions, and so they are unlikely to close permanently (Standard and Poor's, 2011).

17 Since 1990, China's demand for copper ore has increased at an average annual rate of nearly 14 per cent, with imports accounting for around two-thirds of copper ore used in China (Yu, 2011). As the global supply of raw copper materials is limited, the secondary copper market plays a key role in the supply of raw copper materials in China, supplying around 30 per cent of total Chinese copper consumption.

18 Chinese production, consumption and trade figures for iron ore are adjusted to correspond to the world average iron content.

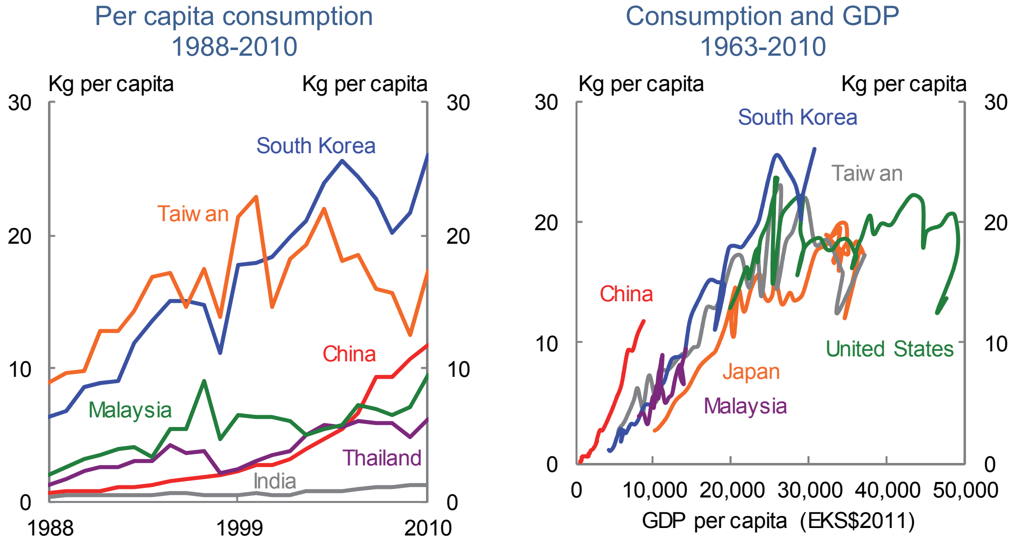
structure of Chinese economic growth has been particularly metals intensive, consistent with the earlier experiences of South Korea and Taiwan. Despite China's present dominance, per capita metals consumption and metals intensity of GDP, like per capita income, remain well below the levels of advanced economies. Indeed Chinese per capita consumption of copper is broadly on par with that of where South Korea and Taiwan were at China's present level of per capita income, while aluminium and steel consumption are higher (Charts 10 to 12).

Chart 10: Trends in copper consumption per capita



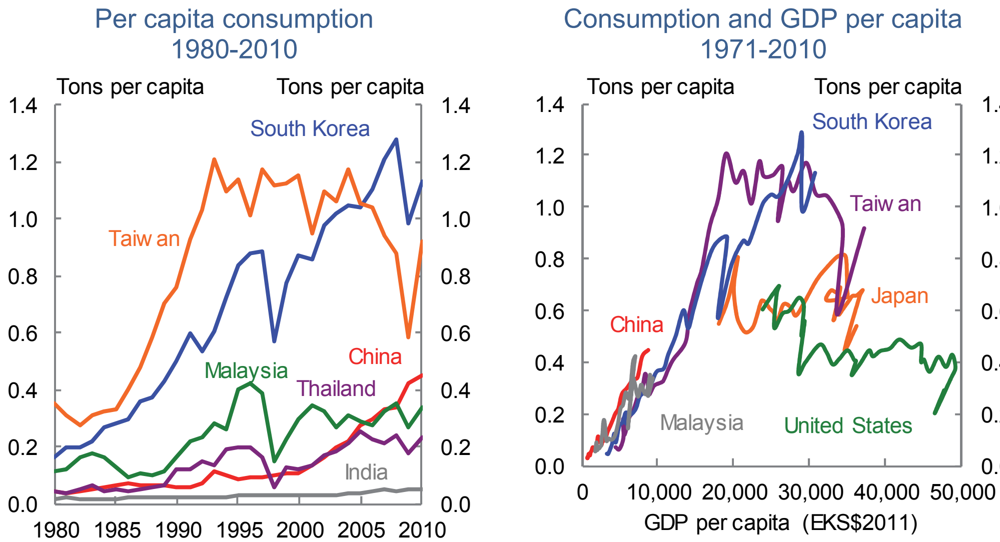
Source: ABARES *Australian Commodities*; BREE *Resources and Energy Statistics* 2011; United Nations *World Population Prospects: The 2010 Revision* and The Conference Board Total Economy Database, January 2012.

Chart 11: Trends in aluminium consumption per capita



Source: ABARES *Australian Commodities*; *World Metal Statistics*, various years; BREE *Resources and Energy Statistics* 2011; United Nations *World Population Prospects: The 2010 Revision* and The Conference Board Total Economy Database, January 2012.

Chart 12: Trends in crude steel consumption per capita



Source: ABARES *Australian Commodities*; World Steel Association *Steel Statistical Yearbooks*, various years; World Metal Statistics, various years; United Nations *World Population Prospects: The 2010 Revision*; The Conference Board Total Economy Database, January 2012.

Looking ahead, the underlying sources of Chinese metals demand are expected to remain strong, with construction, infrastructure, machinery and motor vehicle production projected to grow robustly for some time.[19] Although China became the largest car market in the world in November 2009, it still has a low penetration rate of around 50 cars for every 1000 people compared to 500 cars for every 1000 people in the United States.

While China's specialisation in manufacturing is likely to persist, investment rates are projected to decline over time (the average life span of infrastructure investments exceeds 50 years) so China's metals intensity and per capita metals consumption is expected to stabilise and decline, as did the metal intensities of other Asian economies, such as Japan and South Korea, that followed a manufacturing and export-intensive development path. McKay, Sheng and Song (2010), for example, expect China's demand for steel to continue rising until China's GDP per capita reaches around US$15,000, a figure that will not be reached, according to the authors, until early 2020s if Chinese growth slows to 7 per cent annually. The authors forecast that Chinese steel demand will peak at around 700kg per capita (up from 400kg today), exceeding the levels seen during the industrialisation of Western Europe and North America, but lower than the peaks seen in Japan, South Korea and Taiwan.

China's demand for agricultural products

China is the world's largest agricultural economy, but so far, its economic rise has had a less dramatic impact on world agricultural markets, compared with its influence on global energy and metals markets. This, in part, reflects the fact that only 15 per cent of world food production is traded on international markets, the relatively more protected nature of agricultural trade and China's self-sufficiency goals.

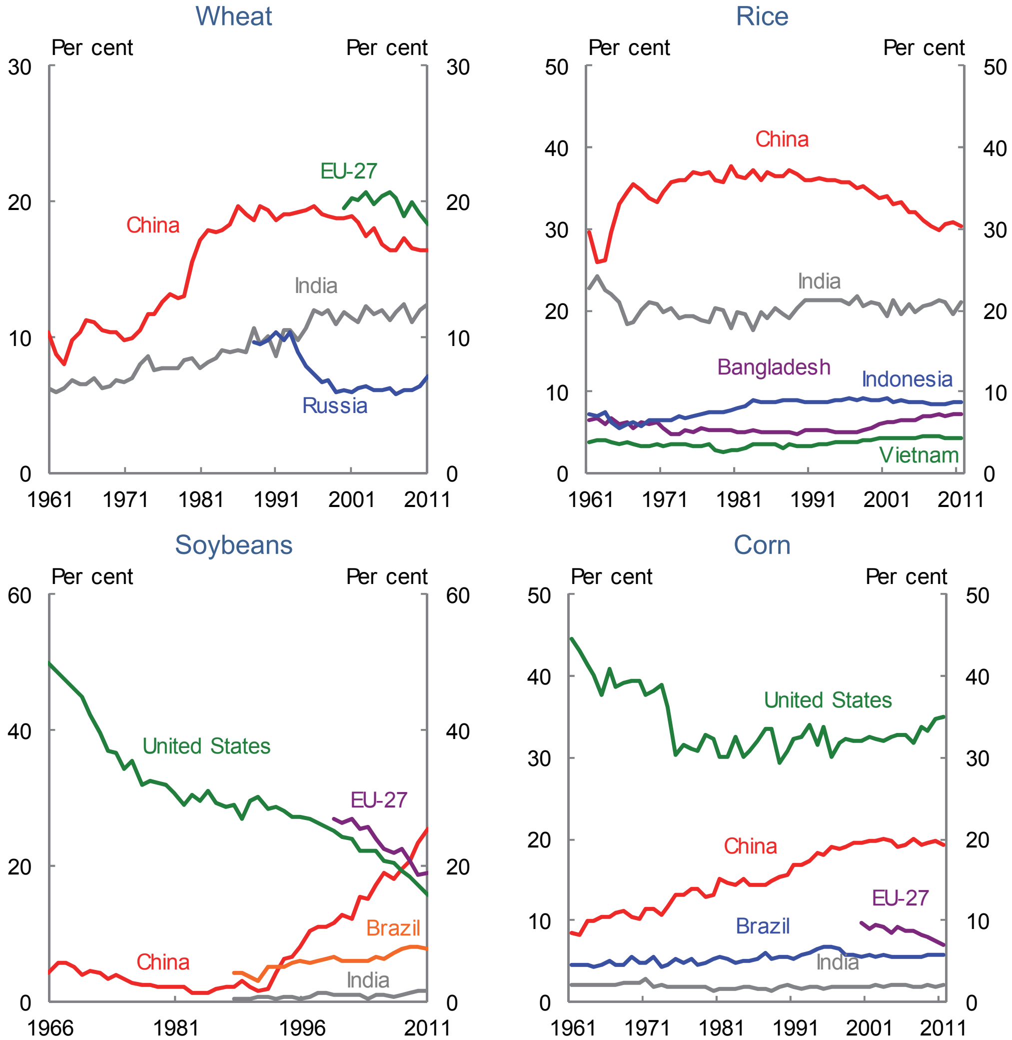
China's impact on world agricultural markets varies significantly across commodities. With the world's largest population, China is the largest consumer of wheat, soybeans and rice, and the second largest consumer of corn (Chart 13). China has been a significant driver of increased global demand for soybeans, meat and dairy products. However, China's share of global wheat and rice consumption has declined in recent years.

Agricultural commodities are important to China not only for human consumption, but also as feed for livestock and as an input into energy production. Feedstock demand accounts for 70 per cent of Chinese corn consumption, 14 per cent of soybeans and 12 per cent of wheat. As the Chinese diet shifts towards more meat consumption, expanded livestock production will exert more pressure on Chinese demand for feed grains. Higher energy prices have also spurred growth in demand for feed stocks

19 The prospects for strong domestic copper demand are promising, given the long term growth potential of the energy, real estate, automobile and home appliance sectors (Shang, 2011).

to support the production of biofuels, although biofuels industries account for a comparatively small share of agricultural consumption.[20]

Chart 13: China's share of world agriculture demand



Source: United States Department of Agriculture Foreign Agricultural Service.

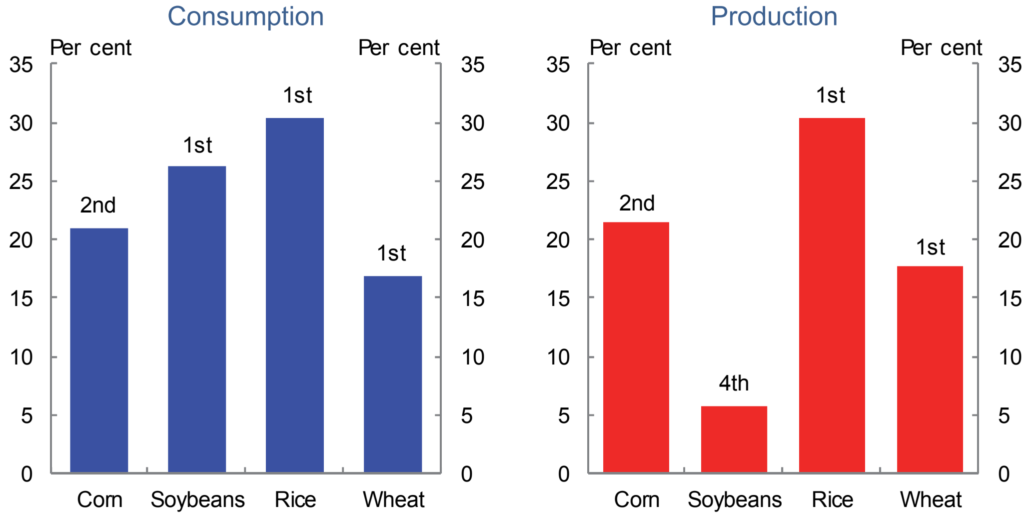
China's agricultural production

China is not only the world's largest agricultural consumer, but is also the world's largest producer of rice and wheat, and the second largest producer of corn (Chart 14). China also produces more than seven times the amount of fruits and vegetables as the

20 Biofuels are expected to account for only 2 per cent of all transport fuels in China by 2030, reflecting the limited agricultural land for feedstock crops given concerns about the security of food supplies (IEA, 2007).

US, reflecting China's comparative advantage in labour intensive agricultural production.

Chart 14: China's share of global food consumption and production, 2010-11



Source: United States Department of Agriculture Foreign Agricultural Service, Production, Supply and Distribution Database.

China's agricultural sector has changed dramatically since it began modernising following the introduction of reforms more than 30 years ago. From 1978, the commune system was reformed to provide greater autonomy to the collectives, and eventually replaced by a system where individual families leased land from the collectives, ensuring that almost all rural households had access to land and were, at minimum, food self-sufficient. As a result agricultural production rose sharply, poverty fell dramatically, and the level and quality of food consumption improved significantly, while rural industries expanded and absorbed a large part of farm labour (OECD, 2005).

China remains largely self-sufficient in most major agricultural commodities reflecting a primary strategic goal for Chinese policymakers — particularly following the widespread famines of the 1960s — and in the mid-1990s it devised a campaign to boost grain production.[21] As China further integrated into the world economy, self-sufficiency goals were relaxed for many products, but leaders remained committed to achieving near self-sufficiency in the production of rice, wheat, corn and other grains. In December 2010, the Central government reiterated its policy of

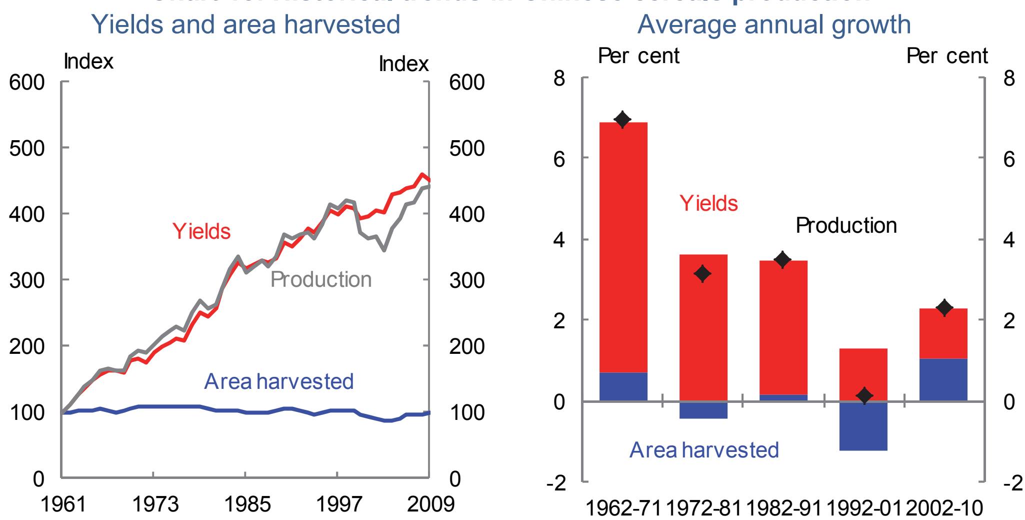
21 In the mid-1990s, the 'Governor's Grain Responsibility System' (also known as the obligatory system) was introduced to ensure adequate domestic supply of grains and arose out of concern over securing food supply. Provincial governors were responsible for their province's self-sufficiency in grains, irrespective of local farming conditions.

95 per cent self-sufficiency in grains. This policy, coupled with support for rural incomes and promoting rural development, remains important.[22]

Achieving self-sufficiency in grains will, however, become increasingly difficult and costly with China's growing population, rising incomes, changing consumer tastes, concerns about the scarcity of water and arable land, and the impacts of climate change. China has less than 9 per cent of the world's arable land and only 6 per cent of the world's water supply but has more than 20 per cent of the world's population. The nutrient deficiencies of China's soils and the intensity of its farming practices make it the world's largest consumer of fertilizer (Potash Corp, 2010).[23]

These concerns have prompted the Chinese government to increase spending on agriculture and to prioritise investment in agricultural research and development.[24] Implementing these policy objectives will, however, require policy makers to carefully balance the competing goals of increasing urbanisation while boosting agricultural production.

Chart 15: Historical trends in Chinese cereals production



Source: *FAO, Australian Treasury.* Notes: left chart indexed to 1961-62.

Chinese grains production has risen more than fourfold in the past five decades, although yield growth has slowed over the past two decades (Chart 15). Meanwhile

22 At the December 2010 Central Economic Work Conference, policymakers agreed to increase subsidies for agricultural production, gradually raise minimum grain prices and boost investment in major grain-producing areas. Under the 12th Five-Year Plan China plans to deepen rural reform, increase funding for agriculture and farmers and direct more spending towards agriculture and rural areas.

23 Prices for nitrogen fertilisers and other farm chemicals are closely related to the crude oil price, so rising oil prices translate into increasing production costs (FAO/OECD, 2011).

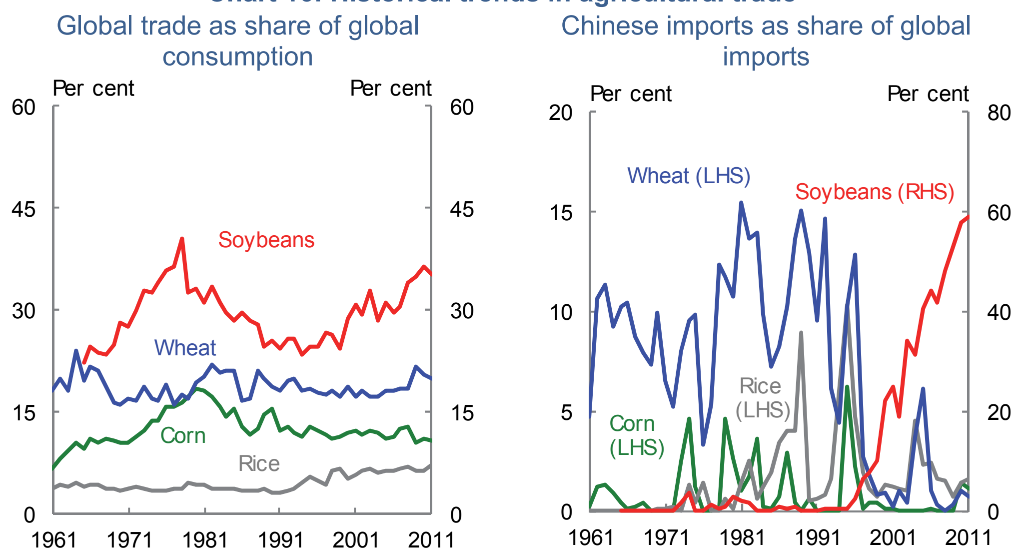
24 See APCO, 2011.

demand will continue growing strongly, albeit at a lower rate than seen over the past 40 years. Consequently the future trajectory of Chinese imports will depend on China's ability to continue increasing yields without commensurate increases in land under cultivation.

China's impact on global agricultural markets

With rising agricultural demand and slowing agricultural productivity growth, China's emergence is having an increasingly significant impact on global agricultural markets. Following China's accession to the WTO – which saw China reduce tariffs and end most of its remaining state monopolies on agricultural imports and exports – China's agricultural trade has grown rapidly. Over the past five years, Chinese agricultural imports have grown 23 per cent annually, with the US the largest supplier of agricultural products to China in 2010.[25]

Chart 16: Historical trends in agricultural trade



Source: United States Department of Agriculture Foreign Agricultural Service, Production, Supply and Distribution Database.
Notes: Global trade proxied by imports.

The small size of global markets magnifies China's presence, with only a small share of global grains traded internationally (Chart 16). For example, China has already become the world's largest importer of soybeans, accounting for nearly 60 per cent of global imports in 2009-10 and is projected to account for more than 70 per cent of global imports by 2014-2015 (Chart 16) (Standard and Poor's, 2011). China has also become a net importer of corn for the first time since 1995, reflecting strong demand for livestock feed.

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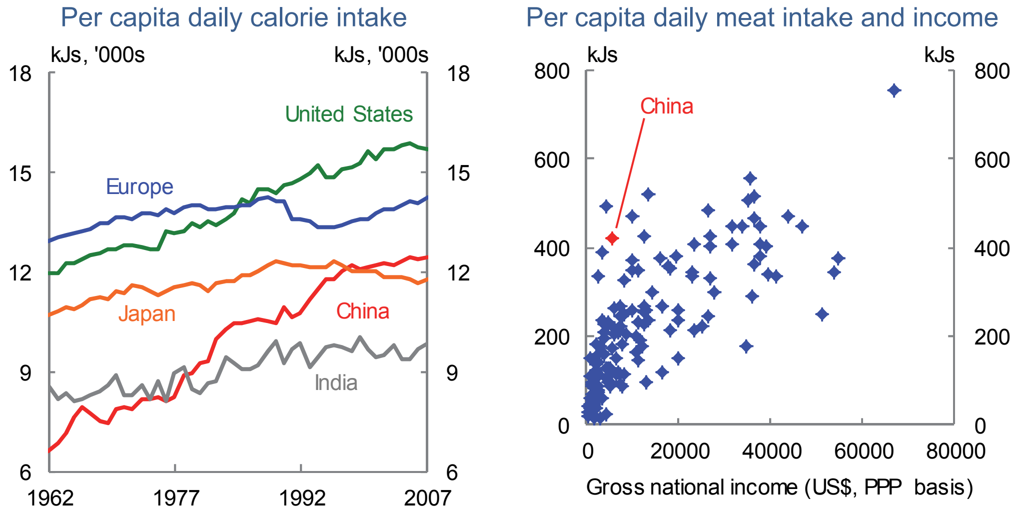
25 The US is a major producer of soybeans, and as such has benefitted greatly from trade with China (US International Trade Commission, 2011).

The impact of rising incomes on food consumption patterns

Rising incomes are a key driver of increased food demand and shifting consumption patterns. Rapid economic growth in China has led to a rise in demand for protein and, partly as a result, the average number of kilojoules consumed on a daily basis in China has converged closer to levels seen in the United States and Europe (Chart 17).[26] Greater access to markets, greater diversity of available food and refrigeration have also supported this shift.

Chart 17: Per capita food intake and income



Source: FAO, World Bank *World Development Indicators 2011*, Australian Treasury; adapted from Rayner, Liang, Hall (2011).
Notes: kJs refers to kilojoules; data for right chart are cross-sectional and represent 158 countries in 2007.

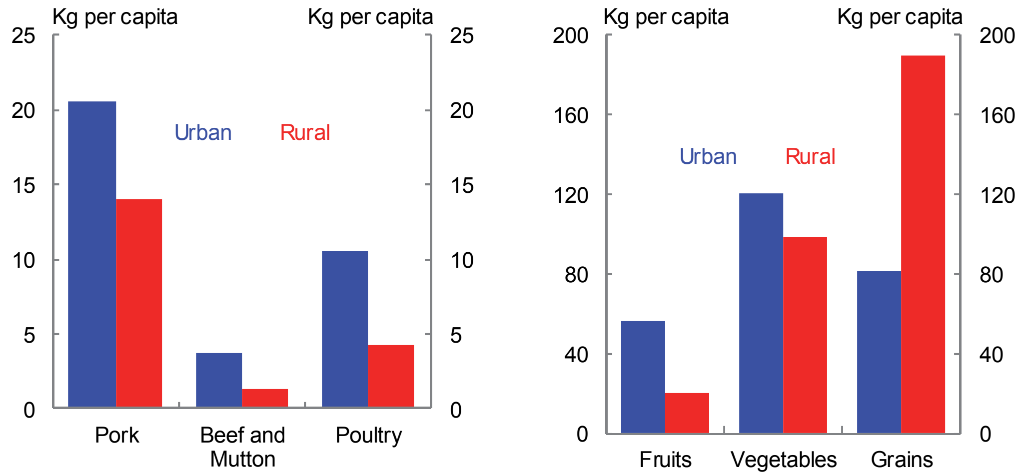
Growth in per capita Chinese meat consumption has outpaced that of other industrialising Asian economies, accounting for around one-third of increased global demand over the past decade, while Chinese per capita milk consumption is also growing strongly. This increase in demand for meat and dairy is — through demands on land use and feed grains — contributing to broad based pressure on food prices. For example, one-third of all cropland is used to produce animal feed; and, on average, it takes 3kg of grain to produce 1kg of meat (United Nations Environmental Programme, 2009).

Differences between rural and urban diets illustrate the impact of rising incomes in developing nations. While average Chinese incomes have risen dramatically over the past two decades, urban Chinese residents continue to earn on average three and a half

26 The Hong Kong Monetary Authority estimates that a 10 per cent increase in overall real household spending per capita is associated with a 1.1 per cent increase in meat consumption in the US, compared with an 11.5 per cent increase in China. See Hong Kong Monetary Authority (2010).

times their rural counterparts.[27] Reflecting rising incomes, urban diets have improved and are more diverse than those of rural citizens. Although urban and rural Chinese households have rapidly increased their consumption of pork, beef, mutton and poultry, and decreased their consumption of grains, urban residents on average consume significantly more meat and fruits, and fewer grains, than rural residents (Chart 18).[28]

Chart 18: Chinese food consumption among rural and urban residents, 2009



Source: National Bureau of Statistics of China, CEIC China database.

A growing population and rising incomes in China will sustain strong demand for agricultural commodities in future decades.[29] With Chinese per capita income still low at around US$7500 in 2010 (PPP basis) — less than one-fifth of that of the US — rising incomes should continue to boost food demand for some time, especially for protein, dairy and soybeans. Moreover, significant income inequality across China means that the majority of the Chinese population continue to receive incomes well below this, which should further support growth in demand for higher-quality and protein-rich foods as their incomes rise.

With additional income to spend on food, demand will continue shifting from staple foods, such as grains, towards meat and horticultural products, such as fruit and

27 In 2010, per capita incomes in urban Chinese households averaged RMB 21,033 compared to RMB 5,919 among rural residents.

28 While shifting to urban areas can lead to a more diversified diet as citizens gain access to a wider range of foodstuffs, shifting patterns of food consumption towards protein are driven more by the coincident increase in incomes than the process of urbanisation itself. See Stage, Stage and McGranahan (2009).

29 Population growth can be expected to boost food demand over the coming decade, but at a slower pace than previously. China's population growth is expected to slow to an average of 0.2 per cent per annum through to 2030, compare to average population growth of 0.8 per cent over the past two decades (United Nations, 2011).

vegetables, although rice is likely to remain a primary staple in Asian diets. Meanwhile declining human per capita consumption of grains such as wheat and corn could be offset by increased demand for use as feed stocks for livestock and biofuels production.[30] These trends will only increase China's importance to global agricultural markets in the decades ahead.

Conclusion

China's rapid economic rise has had a significant impact on global commodity markets in recent years, and will be a key influence on future market developments. China has emerged as the leading consumer of a broad range of commodities — especially energy and industrial metals —and is a significant player in most major commodities markets, including agricultural commodities.

Strong economic growth, underpinned by commodity-intensive investment has sustained global commodities demand since the global financial crisis. With weak growth among advanced economies, China has taken an increasingly large share of global commodities consumption growth over the past five years. Although there will be short-term fluctuations around China's growth, and China faces significant medium-term reform challenges, the long term outlook for Chinese commodity demand remains strong as the process of urbanisation and industrialisation, and a growing middle-income class are set to continue for some time. Per capita consumption of key commodities, like per capita income, is still well below that of major advanced economies.

Economic rebalancing in China could have significant effects on future Chinese commodity demand, with significant implications for global markets. A more rapid shift from investment- to consumption- driven growth could slow the pace of metals and energy demand, although many consumption goods, such as automobiles, are still comparatively commodity intensive. Future Chinese commodity demand may be constrained by its already dominant position in some global commodity markets and the rate of growth of commodity supply.

In contrast, China's impact on agricultural commodity markets, has to date been more modest. China is yet to assume a large role in most global agricultural markets, with the exception of soybeans, despite its place as the world's largest consumer and producer of major grains such as wheat and rice. However, continued strong growth in food demand arising from rising incomes and a growing population, together with subdued supply growth, should see China increasingly utilise global markets as a major net food importer in the years to come.

30 Roughly two-thirds of global wheat production is currently used for direct human consumption, but growth from this segment of demand is anticipated to slow down through to 2020 (OECD/FAO, 2011).

Previous industrialising Asian economies provide some guide to China’s future commodity demand. With rapid urbanisation, intense industrialisation and a growing role as a supplier of manufactured goods globally, China shares similar characteristics with other recently industrialised economies such as South Korea and Taiwan. However, unlike these economies, the sheer size of China’s economy, its significant natural resource endowments and the comparatively low per capita incomes when China begun its rapid economic rise mean that China’s development experience, and the trajectory of its commodity demand across energy, metals and agriculture, will ultimately prove unique.

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Consumer financial protection: future directions[1]

Dr Richard Sandlant

With governments around the world taking a renewed interest in effective consumer financial protection, this paper focuses on four key pillars: financial literacy, disclosure, advice, and product regulation. Although there is no one 'silver bullet' that will provide effective consumer financial protection on its own, there are potential synergies between these four pillars (and other measures), which can have a multiplier effect on the effectiveness of individual components, enhancing the overall efficiency of the policy framework[2].

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1 The author is from the Retail Investor Division, the Australian Treasury. This article has benefited from the contributions and comments of participants at the 16th Melbourne Money and Finance Conference (2011). The view in this article is the view of the author and not necessarily those of the Australian Treasury.

2 This article was originally published as Sandlant, R 2011, 'Consumer financial protection: future directions' *JASSA – The Finsia Journal of Applied Finance*, issue 4, pp 42–7.

It is widely accepted that consumer financial protection is important not only to protect consumers but also for financial stability.[3]

Consumers need protection because of the well-known asymmetry between the consumer and the financial services provider. Typically, the consumer has little experience with or understanding of making certain financial decisions, particularly complex financial decisions with long-term considerations. The financial services provider, on the other hand, is usually comprised of a team whose professional specialisation is creating financial products and selling them to consumers.

There is also a view that consumers need protection from themselves, due to their vulnerability to making poor financial decisions, their susceptibility to certain sales messages when framed in a particular way, and their underestimation of their own lack of financial understanding.

Consumer financial protection is also about empowerment and financial stability. The well-being of the Australian people is central to Treasury's mission.[4] Confident and knowledgeable consumers would also be an enormous asset for well-functioning and efficient financial markets, if only we could figure out how to reliably produce them.

The reality is that few consumers meet such high expectations, and with financial services growing in complexity faster than the capacity of regulators (let alone consumers) to stay 'one step ahead', and with consumers increasingly being given more, not less, responsibility for their own long-term financial security, governments around the world are taking a renewed interest in effective consumer financial protection.[5]

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3 'The recent crisis demonstrated the critical importance of financial literacy and good financial decision-making, both for the economic welfare of households and for the soundness and stability of the system as a whole', statement by Ben Bernanke, Chairman of the Board of Governors of the Federal Reserve System, provided for the record of a hearing held on 12 April 2011 conducted by the Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia, Committee on Homeland Security and Governmental Affairs, US Senate, Washington DC, 20 April 2011.

4 See *Policy advice and Treasury's wellbeing framework*, based on paper presented to the meeting of the Australian Statistics Advisory Council on 25 May 2004.

5 For example, in February 2011 the G20 Finance Ministers and Central Bank Governors asked the Organisation for Economic Co-operation and Development (OECD), the Financial Stability Board (FSB) and other relevant international organisations to develop common principles on consumer protection in the field of financial services by their October 2011 meeting. See FSB, *Progress in the implementation of the G20 recommendations for strengthening financial stability*, 10 April 2011. The author is the Australian representative on the OECD Taskforce on Consumer Financial Protection which led the work related to the development of these principles.

Perhaps the rationale also becomes clearer when confused retail investors making poor financial decisions in complex markets take the world to the brink of global financial meltdown.[6]

Four pillars of Consumer Financial Protection

There are many components to consumer financial protection, but I would like to focus on four key pillars: financial literacy (also known as financial education), disclosure, advice and product regulation. These four are not only important individually, but collectively, as we shall see. By this I mean that the sum of the whole can be greater than the parts.

If we look at what has been going on with respect to these four pillars, we find a number of significant policy initiatives and interesting trends.

Financial literacy

Numerous studies reveal that the level of financial literacy among Australians is depressingly low, but low financial literacy is a worldwide phenomenon.[7] This reflects the fact that while financial services have been evolving at a rapid pace, individuals' capacity to understand money has been plodding along by comparison.

In Australia, the Australian Securities Investments Commission (ASIC) takes the lead in advancing financial literacy. In March 2011, ASIC launched the government's National Financial Literacy Strategy[8] and a new consumer financial literacy website: www.MoneySmart.gov.au.

The new financial literacy strategy focuses on four interrelated areas:

- delivering quality financial literacy education to all Australians through schools, workplaces, higher education institutions and in the community;
- providing all Australians with access to the information and tools they need to make good financial choices;
- going beyond education to guidance and other strategies to enhance the financial well-being of Australians, including developing a new consumer website; and

6 Recent economic events have focused attention on the financial decisions made by consumers and the practices of retail financial institutions. Many argue that consumer confusion in the increasingly complex mortgage market contributed to the subprime market meltdown of 2007 which, in turn, triggered the global financial crisis. See Campbell, J Jackson, H Madrian, B and Tufano, P 2010.

7 See, for example, Australian Government Financial Literacy Foundation 2007.

8 ASIC, Report 229, March 2011, *National financial literacy strategy*; see also ASIC Report 230, March 2011, *Financial literacy and behavioural change*.

- developing partnerships between the various sectors involved in financial literacy work and better means of measuring the impact of what we do.

It's a long-term strategy, because improvements in financial literacy require generational change (think 'slip-slop-slap' and suntans). The new consumer website leverages the unique strengths of the internet to deliver financial literacy services to consumers.[9]

Research across a number of fields has shown that people learn something best from actually doing it. Not surprisingly, few want to curl up in front of the fireplace with a good financial literacy book. With this in mind, the new MoneySmart website offers tools and functionality that are designed to be interactive, useful, fun and engaging over time.

The idea is that MoneySmart can become a trusted source of personalised money guidance for financial decisions, even more complicated decisions such as those relating to superannuation contributions, margin loans and income tax.

If we step back and look at the big picture, this website represents the 'first rung' on the ladder of financial advice, providing what is otherwise known as free 'generic advice' to every Australian with access to the internet.[10]

A similar innovation is underway in the United Kingdom where their consumer website, Money Made Clear, became 'The Money Advice Service', a free, independent financial advice service funded by financial services companies. It provides free telephone and face-to-face advice, in addition to website functionality.

The United Kingdom took this further step, they tell us, because 'we found that if you offer people money advice for free, then most of those people will do something as a result of that advice'.[11]

This brings us to the next pillar of consumer financial protection: financial advice.

Financial advice

From a consumer protection perspective, a financial adviser should be a trusted professional who acts in their best interests. The financial adviser should be someone consumers can rely on to navigate complex financial issues and help them to make the

9 See Bottrill, C 'Internet-based tools for behavioural change', paper presented at European Council for Energy Efficient Economies (ECEEE) Summer Study 2007, *Dynamics of consumption*, session 9, paper 211; Stout, P A Villegas, J Kim, H 2001.

10 'A key plank of this strategy is the development by ASIC of a generic guidance service — 'personalised money guidance' — for a mass market. 'Generic' means the guidance does not recommend specific brands of products'. ASIC, *op cit*, p 42.

11 Lemos, G 2011.

right decisions, and someone who is financially literate, highly trained, competent and ethical.

The fundamental challenge with advice has been that advice is also a distribution channel for product providers. Product providers need to invest in their distribution and, for an advice business, this represents a revenue stream that is difficult to ignore.

In 2009, ASIC estimated that around 85 per cent of the 18,000+ advisers in Australia were associated with a product manufacturer (including many independently owned dealer groups that had 'white label' arrangements).[12] The Independent Financial Advisers Association of Australia (IFAAA), by comparison, had seven members in April 2011.[13]

In 2009, in the wake of the collapses of Storm Financial and Opes Prime, the Parliamentary Joint Committee (PJC) on Corporations and Financial Services conducted an Inquiry into financial products and services in Australia examining, among other things, the role of financial advisers and commission arrangements.[14] In its recommendations, the PJC called for a fiduciary duty requiring advisers to 'place their clients' interests ahead of their own' and action to develop 'the most appropriate mechanism by which to cease payments from financial product manufacturers to financial advisers'.

The government responded with the Future of Financial Advice (FoFA) reforms, which include a ban on product commissions and volume payments, and introduce a statutory duty requiring advisers to act in the 'best interests' of consumers. Perhaps the key to understanding FoFA is that the reforms aim to change the source of adviser remuneration from the product provider to the consumer.[15]

In 2010, ASIC reported that up to 80 per cent of adult Australians had never used a financial adviser, and that many Australians want piece-by-piece simple advice rather than holistic financial planning (which can cost upwards of $2,500).[16] The FoFA

12 Parliamentary Joint Committee on Corporations and Financial Services, *Inquiry into Financial Products and Services in Australia*, submission by the Australian Securities and Investments Commission, August 2009, p 4.

13 The IFAAA has a 'Gold Standard of Independence' that few advisers can meet — they can't be affiliated with a product provider, receive commissions or charge asset-based fees. See Power, T 29 April 2011.

14 Parliamentary Joint Committee on Corporations and Financial Services, *Inquiry into financial products and services in Australia*, November 2009.

15 'I strongly believe that financial planners should only have one master — the consumer. Yet, for years, product providers have called the tune because they are the ones paying the planners through sales commissions and other kick-backs like expensive conferences. Any industry that survives on these kinds of practices will not be trusted by consumers. This lack of trust is one reason why up to 80 per cent of Australians have never used a financial adviser. It's time that the regulatory framework governing the provision of financial advice shifted the focus back to the consumer', the Shorten, B (then-Assistant Treasurer and Minister for Financial Services and Superannuation), 2011.

16 ASIC 2010, Report 224 *Access to financial advice in Australia*.

reforms also seek to ensure that financial advice will be more widely available and within the reach of more Australians, by facilitating the expansion of more affordable 'scaled' or limited advice.

Striking the right balance between enabling lower-cost, 'simple advice', while at the same time protecting consumers from 'product flogging', is something of a 'holy grail' in advice reform. A 'best interests' duty is one way to address this issue; another is disclosure, to which we now turn.

Financial product disclosure

The Financial Services Reform Act 2001 enshrined disclosure as a key consumer financial protection measure in Australia. The thinking was based on 'efficient markets theory', and relied on disclosure and conduct regulation to manage conflicts of interest, with the expectation that consumers would use disclosure to make informed decisions and that efficient markets would thereby drive competition and innovation.

The legislation was drafted using a principles-based approach, to provide financial service providers with maximum flexibility. This sounds good but the outcome, as is now well known, was that disclosure turned into a liability-management tool for product providers. Disclosure ratcheted up in size and complexity until it became virtually unreadable. Ever since, the entire reliance on disclosure has come into question.[17]

As ASIC commented to the 2009 PJC Inquiry:

> [ASIC is] querying whether it has gone far enough in protecting retail investors, given the important role, which was not foreseen by the Wallis inquiry, that retail investors would play in the market. They had not foreseen and could not have foreseen the impact that the superannuation levy has had on investment in our markets. In that situation, you have a much broader range of retail investors and retirees. You have groups of people who lose money at the wrong time in their life and it is no answer to them to say: 'Well, it was a risk, you know. There was disclosure. You should have read the disclosure statement'. The fact is that they cannot easily come back into the workforce.[18]

The government has responded with a number of measures designed to improve and simplify disclosure. Product disclosure statements (PDSs) for margin loans, superannuation and simple collective investment schemes have been shortened and

17 See, for example, Kingsford Smith, D 2010, 'Beyond disclosure: how did retail investors and financial consumers fare in the crisis? Is there a need to improve outcomes for consumers and retail investors?' paper presented at the ASIC Summer School.

18 Parliamentary Joint Committee on Corporations and Financial Services 2009, *Inquiry into financial products and services in Australia*, November, p 74.

provide only the key information, in summary form, that a consumer needs to know in order to make their financial decision. Everything additional to this core information is 'incorporated by reference', which means it is provided online or upon request.

Disclosure is important, but the question is now how it can be used more effectively to communicate the key information consumers need to know. One of the key lessons of recent years is that this is very hard to get right.[19] It's not just that we need 'plain English', we need 'stark language' because sometimes the message needs to be really clear and unambiguous.[20] At the 2010 ASIC Summer School, for example, Paul Clitheroe suggested that PDSs should feature a photo of a family standing on the street next to their belongings along with a warning that 'this could happen to you'.[21]

The future of disclosure, I suggest, is to keep working on improving it, and also to look at new ways of using disclosure to assist consumers to make better financial decisions. Assuming that consumers have access to advisers and that advisers are acting in the consumer's best interests, one obvious way is to design disclosure to be more helpful to advisers in comparing products and making their recommendations.

Another, less obvious way is to design disclosure for computers (and even journalists), not consumers. The idea here is that the information consumers need to know can reach them through indirect channels.[22] Complex data that is very difficult for consumers (and even some advisers) to compare meaningfully could be designed for computers to compare. The results could be made publicly available not so much for consumers but for advisers and financial journalists, who could then publish their analysis in a way that consumers actually might understand and care about.

ASIC has recently developed a novel approach to disclosure by setting new disclosure benchmarks for complex products. These benchmarks require issuers to clearly identify the key risks consumers should understand before making a decision to invest. At the same time, ASIC has set benchmarks for how product manufacturers should address these risks in establishing their business model and compliance procedures. The issuer is then required to state in the PDS (and other disclosure) whether they meet these benchmarks, and if not, why not.[23]

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19 'Disclosure policy is tricky. If you remember nothing else from what we say today, that's our bottom line. Getting information policy right and disclosure policy right is tricky indeed. We say this based on our experience as staff economists working on cases and analysing broader regulations', Mulholland, J 2007.

20 For 'stark language', see Godwin, A 2009.

21 'Words are done by lawyers and they are very poor disclosure tools. What I would like on the cover is a group of retirees with their furniture in the street outside their house. Then I'm happy for the words to say: ''This may not happen to you but guess what, mate''. That would get their attention.'

22 See Thaler, R H and Sunstein, C R 2009.

23 ASIC is proposing to introduce disclosure benchmarks for contracts for difference (CFDs): in July 2010 ASIC published a detailed report on the retail CFD market in Australia (Report 205 *Contracts for difference*

The question arises, however, whether it is necessary to go even further for consumer financial protection than all of this, and regulate financial products themselves, which brings us to the final pillar: product regulation.

Financial product regulation

The recent global financial crisis (GFC) has led to a reassessment of the effectiveness of traditional conduct and disclosure regulation. Regulators are now asking how much we can expect from disclosure reform and financial literacy when financial products themselves are becoming excessively complex. In some overseas jurisdictions, thoughts are turning to the possibilities for financial product regulation.

For example, Martin Wheatley, then CEO-designate of the new UK Financial Conduct Authority (FCA), recently asked whether it was time for regulators to consider direct product intervention which, he acknowledged, was a fundamentally different approach from the way most regulatory regimes have operated in the past.[24] The concern here is that it may be inherently difficult for competition in retail financial services to prevent consistently poor consumer outcomes.[25]

If this argument is right then, perhaps, logically the regulator should look upstream and consider measures that might influence the design and construction of products. While still a work-in-progress, the new rules being floated would mandate certain requirements on products and product features and potentially restrict sales of complex and risky products to certain classes of consumers.[26]

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and retail investors). Following this ASIC released an investor guide, *Thinking of trading contracts for difference (CFDs)?*, to help retail investors understand the risks of investing in CFDs and a consultation paper on disclosure benchmarks for over-the-counter (OTC) CFDs (Consultation Paper 146 *Over-the-counter contracts for difference: improving disclosure for retail investors*). A regulatory guide with final benchmarks for OTC CFDs is likely to be released later this year. ASIC has also recently published a consultation paper on financial requirements for issuers of retail OTC derivatives (Consultation Paper 156 *Retail OTC derivatives: financial requirements*).

24 'Many investment products have become excessively complex, and doubts are cast as to whether they make any meaningful economic sense. In some cases, due diligence is not only beyond investors; it is probably safe to assume that intermediaries selling these products or advising their clients on these products find it impossible to grasp the structure of these products … Before the advent of complex structured products, regulatory attention was appropriately targeted at conduct issues, mainly in the selling process. But with investment banks continuing to recruit droves of mathematicians and financial engineers each year, we can expect more complex products to come on stream'. Wheatley, M 2011.

25 See Financial Services Authority 2011, DP 11/1, *Product Intervention*; HM Treasury 2010, *A new approach to financial regulation: judgement, focus and stability*; HM Treasury 2011, *A new approach to financial regulation: building a stronger system*.

26 There is a wide range of policy tools that might be used to achieve such ambitious aims, from requiring product providers to have appropriate product governance processes in place to more prescriptive measures, such as requiring product pre-approval, mandating or banning some products, mandating appropriate charging structures, requiring product benchmarking, and mandating risk warnings. In Australia, Dimity Kingsford-Smith has been an advocate of merit regulation. See Kingsford-Smith, D 2009.

In all of this the UK authorities explicitly recognise that excessive regulation inhibits innovation and competition, which might otherwise be to the benefit of consumers. However, they argue that perhaps this is acceptable where the resulting benefits to a majority of consumers (from not being miss-sold a product) outweigh the costs to a minority who might benefit from being able to access it.

This is a very tricky policy issue, because if we want informed and empowered consumers to stimulate innovation and competition, this might be harder to achieve if governments intervene too much in product design. On the other hand, the potential risk to consumers (and to financial stability) of complex products being miss-sold, particularly when all the other reform elements are still a work in progress, is significant. For this reason, the idea of product intervention in the United Kingdom is no longer 'out of bounds'.

The 2009 PJC Inquiry considered whether there should be limitations placed on certain complex and risky financial products so that they were not available to retail investors. It decided that 'it is not for the parliament or the government to determine for whom particular investment products are appropriate. This is a decision for individual investors, in consultation with a financial adviser bound by a fiduciary duty to put their clients' interests ahead of their own'.[27]

In Australia there have been a number of product interventions with consumer financial protection objectives in mind. For example, we see an example of 'libertarian paternalism' in the compulsory superannuation system and recently in the introduction of MySuper.[28]

The United Kingdom has also recently experimented with 'simple' or 'vanilla products', however, some of their experiences illustrate the challenges. For example, the Stakeholder product initiative struggled to appeal to its target market (less experienced, less knowledgeable consumers). Partly, this was due to mandated requirements for low fees, free movement in and out of the products without penalty, and the low balances invested. Product providers simply preferred to sell other products that delivered greater profitability, while the target market itself had little enthusiasm to seek the 'simple products' on their own initiative. Moreover, to keep costs low, distribution had to be through a 'Basic Advice' model which proved difficult to achieve in practice.[29]

27 Parliamentary Joint Committee on Corporations and Financial Services, November 2009, *Inquiry into financial products and services in Australia*, p 143.

28 The idea behind 'libertarian paternalism' is that, if real people don't always make rational choices why not give them a little 'nudge' in the right direction by designing a 'choice architecture' so that if they end up making a choice by default it is actually a good choice. See for example Camerer, C Issacharoff, S Lowenstein, G O'Donoghue, T and Rabin, M 2003; Sunstein, C and Thaler, R 2003.

29 Devlin J 2011.

An alternative to various forms of intervention in product design or creating 'vanilla products' is to tighten the regulation around consumer access to more complex and risky products. In Australia, the government is currently reviewing the retail/wholesale investor classification as part of the FoFA reforms. A number of countries are also exploring requirements for consumer knowledge to be tested before they can access complex and risky products.[30]

Synergy in consumer financial protection

There is no one 'silver bullet' that will provide effective consumer financial protection on its own but there are potential synergies between these four pillars (and other measures) which can have a multiplier effect on the effectiveness of individual components, enhancing the overall efficiency of the policy framework.

For example, an integrated approach can entail using financial education to teach consumers not only financial concepts, but also how to use disclosure more effectively (it should not be assumed that consumers understand how to use disclosure to compare products and services). Financial education could be used to build this capability using relevant 'real life' examples. Feedback from this process could perhaps even lead to improvements in product design.

Similarly, one of the challenges in making 'generic advice' more effective is how to inform consumers that it exists and encourage them to actually use it. Again, financial education can be used to establish awareness about generic advice and give consumers hands-on experience in using the tools and resources that are available. Disclosure can be used to further market the availability of such publicly available resources, especially at the point of sale. Could product design even make 'generic advice' a built-in component of the product's own features?

In all of this, where the rubber really hits the road is the moment when a consumer makes a financial decision. Everything that we have been talking about, from financial literacy to advice, from disclosure to product design, impacts on how effectively the consumer makes that decision.

Consumer financial protection is not just about protecting consumers, we want financial markets to become more efficient as a result of consumers making more

30 For example, Hong Kong recently introduced a derivatives knowledge test requiring distributors to assess consumer knowledge of derivatives and rate them based on that knowledge. The *Securities and Futures and Companies Legislation (Structured Products Amendment) Ordinance 2011* was passed by the Legislative Council on 4 May 2011. Singapore is also reviewing whether advisers need to obtain from consumers 'information that is necessary to ascertain the customer's investment knowledge or experience before selling an investment product'. See, for example, Monetary Authority of Singapore 2010.

informed financial decisions, and we need efficient markets to ultimately improve well-being.

Governments promote competition in financial services because that, in turn, leads to better social and economic outcomes, in the form of lower prices and a better match between financial needs and the products and services provided.

Because of the linkages between all of these elements, it is in our collective interest to get consumer financial protection right. And, as this paper has argued, there are real benefits in thinking through how each of the four pillars can be used to strengthen the other three, to ultimately contribute to well-being and financial stability over the long term.

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Introductory remarks to the Australia-Israel Chamber of Commerce

Dr Martin Parkinson, PSM
Secretary, Australian Treasury

This speech was delivered to the Australia-Israel Chamber of Commerce on 7 March 2012.

Introduction

It is a pleasure to be here with you today.

This is the second AICC event I have spoken at in the last year, a year of global dislocation and change, with financial turmoil emanating from the North Atlantic and the still unfolding implications of upheaval in the Middle East.

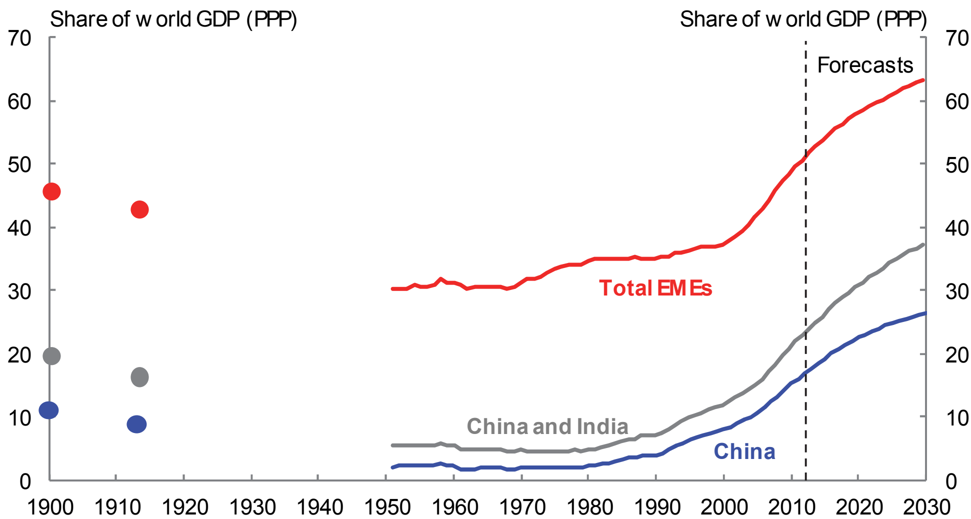
In the 12 months since I became Treasury Secretary I've delivered a range of presentations around the country. But while the venues have been different, there have been three recurring themes.

Global and domestic transformation

First, the world is changing in terms of countries' respective economic weight and, hence, geo-political importance. This transformation is most obvious in the rapid growth and increased global economic importance of the two Indo-Pacific giants, China and India, but it extends far beyond our region, to countries such as Brazil, Turkey, Mexico, Nigeria, and, closer to home, Indonesia and Vietnam.

It is this transformation that has lifted hundreds of millions of people from poverty in recent decades, and has seen low- and middle-income countries increase in importance to half of global GDP and be expected to contribute around three-quarters of global GDP growth over the next five years.

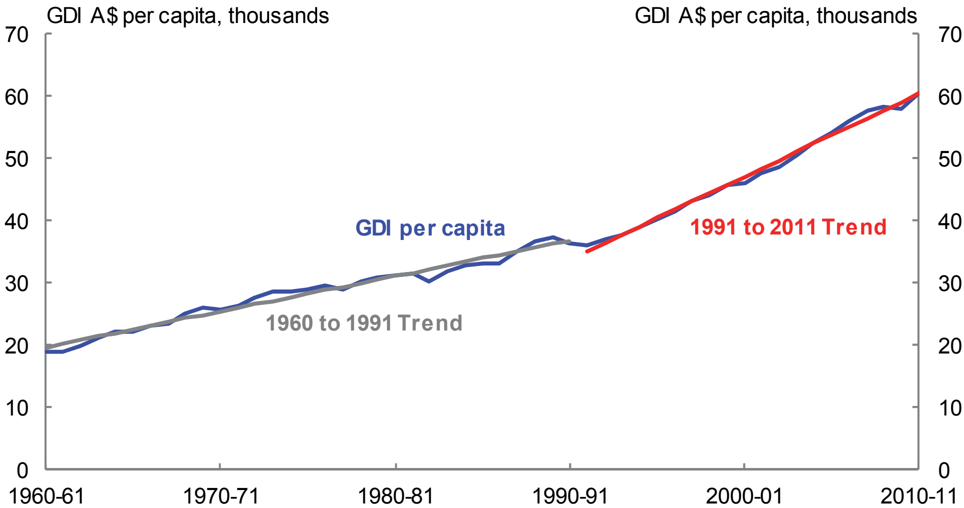
Chart 1: Global transformation underway since 1980s



Source: The Conference Board Total Economy Database, Maddison (2010), IMF World Economic Outlook Database and Treasury.

But the forces leading to this global transformation are also remaking the Australian economy. This adjustment within our economy is causing difficulty for some sectors and is even leading to a questioning of the post-1983 suite of policies that has delivered huge growth in our own living standards and an improved resilience in our economy.

Chart 2: National income (GDI per capita)



Note: Data refers to financial years; reference year for chain volume measures is 2009-10.
Source: ABS cat. no. 3101.0, 3105.0 and 5204.0.

This new world brings with it huge opportunities for Australia, particularly on the back of the growth in the Asia-Pacific (excluding the United States and Canada) middle class which is expected to grow from around 500 million people in 2009, to around 1.7 billion by 2020 and to 3.2 billion by 2030. This group of people will want knowledge intensive manufactures, knowledge intensive services — health, education and professional services, everything from legal and architectural skills to logistical know-how — higher quality diets and great tourism experiences.

If we continue to make the right policy choices, as we showed ourselves capable of in the 1980s and 1990s, we have the opportunity to underpin Australia's future prosperity and establish ourselves as an exemplar for the rest of the world. The decisions we made during that previous period of restructuring have contributed to the living standards we enjoy today, and the decisions we make today will determine our prospects for the years ahead.

To put it simply, Australian policy reform in the face of past structural pressures has raised Australian living standards dramatically. To take one example, the Productivity Commission has estimated that productivity improvements and price changes observed over the 1990s in key infrastructure sectors affected by National Competition Policy and related reforms boosted Australia's GDP by around 2.5 per cent. This means our economy today is around $35 billion larger than it would have been without those reforms.

Australia's governments have previously committed themselves to reducing the impact of regulation on the cost of doing business and to promote competition as part of reforms to achieve a Seamless National Economy. The Productivity Commission's preliminary assessment of 17 of the Seamless National Economy deregulation reforms is that, if completed, these could increase GDP by over 0.4 per cent in the longer run, growing the economy by over $6 billion in today's dollars.

In contrast, had we failed to take the hard choices in the past decade, and pursued populist policies — whether regulatory or fiscal — that reduced competition, undermined price signals and distorted resource allocation, we would have consigned Australia to lower productivity and lower living standards today.

As a nation, we face the same choices again — do we continue to pursue pro-market, pro-competition, pro-productivity reforms — using the benefits of the mining boom to help grasp the opportunities of the global transformation, or do we complacently try to slide through on our natural resource endowment alone while watching the huge opportunities from the growing Asian middle class melt away?

An aging population and a deteriorating productivity performance

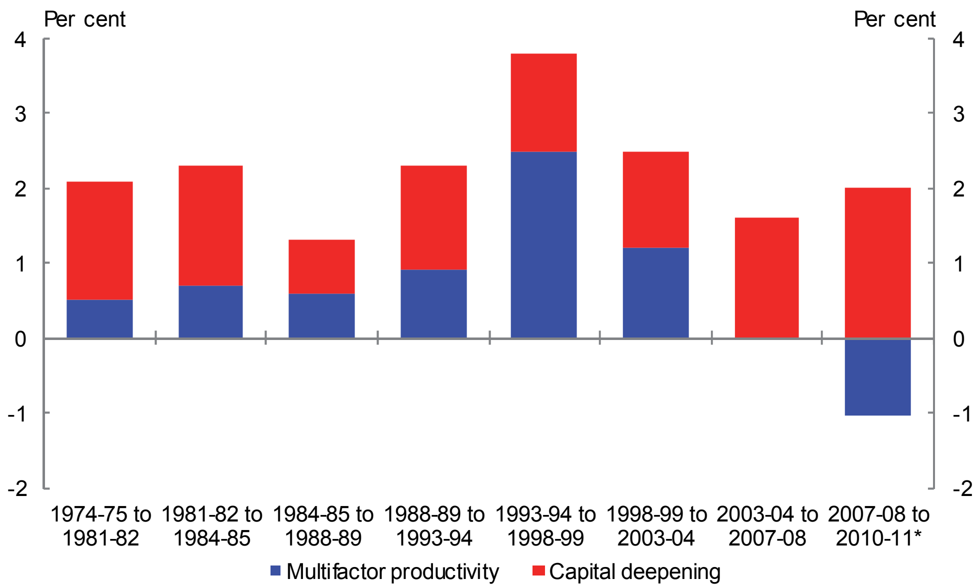
Second, we continue to face the pre-existing domestic challenges of an aging population and a decade long decline in our productivity performance. Coincidentally, there is significant overlap in the policies required to address these challenges and those required if we are to grasp the global opportunities, potentially offering huge co-benefits from the same set of actions.

Notwithstanding the attention that the Global Financial Crisis (GFC) and its aftermath have demanded from policy makers at all levels of government, we cannot lose sight of the fact that our population is aging — the data are well known. In 2010, 11.7 per cent of our population was aged between 65 and 84, and 1.8 per cent were aged 85 and over. By 2050, the comparable figures are 17.6 per cent of Australia's population aged between 65 and 84, and 5.1 per cent aged 85 and over. In percentage terms these may not seem large changes — but it means that we could have over 8 million people aged 65 and over by 2050, of whom 1.8 million people will be at least 85.

Put another way, rather than the 5 people of traditional working age we had for each person aged 65 and over in 2010, we will have around 2.7 by 2050. As the intergenerational reports have noted, this carries with it big challenges for fiscal sustainability and an imperative to improve productivity in the caring sectors, especially health and aged care.

The challenge to turn around our deteriorating productivity performance more generally is also well known — after the significant improvements in productivity flowing from the post 1983 reforms, the beginning of the 2000s saw a marked slowing in labour productivity growth. More disturbing still has been the sharp deterioration in multi-factor productivity — how clever we are at combining labour, capital, resources and ideas.

Chart 3: Productivity growth cycles

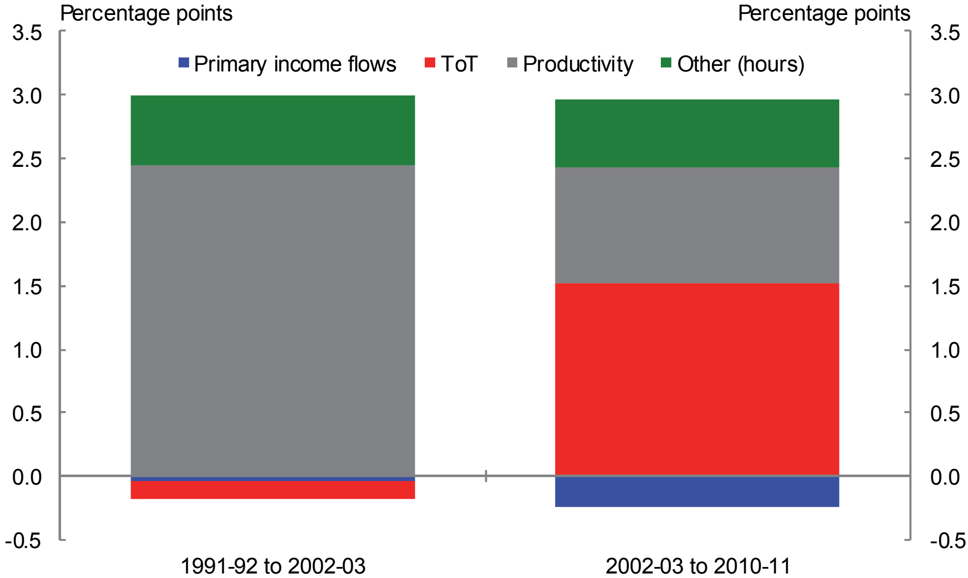


Note: * Incomplete cycle.
Source: ABS cat. no. 5260.0.55.002 and Treasury.

It is true that the growth in mining investment is dampening these figures as we are yet to see the resulting growth in output, and we are increasingly pursuing lower-quality resource deposits, but the story remains, albeit somewhat muted, even if we abstract from mining.

As Paul Krugman has so pithily put it: 'Productivity isn't everything, but in the long run it is almost everything. A country's ability to improve its standard of living over time depends almost entirely on its ability to raise its output per worker'.

Chart 4: Decomposition of growth in real GNI per capita



Source: ABS cat. no. 5206.0, 6202.0 and Treasury.

This is particularly germane to Australia today. After almost all of our growth in national income coming from productivity in the 1990s and early 2000s, over the last decade the contribution from productivity has more than halved — we have maintained the same rate of growth in living standards only because of the huge rise in our terms of trade. If, as we suspect, the terms of trade are unlikely to grow much, if at all, from here, this means that growth in Australian living standards will also slow unless productivity picks-up.

Some of the investments now being made to improve productivity — especially those in infrastructure and skills — will have a significant payoff in the years ahead. But there are some things that can have a more immediate payoff — while we wait for new skills and training to flow through the workforce we should be doing everything possible to ensure existing skills are able to be effectively utilised. For this reason it is imperative that we accelerate implementation of the Seamless National Economy initiatives, including on skill recognition across state boundaries.

Medium-term fiscal strategy and the importance of fiscal credibility

Third, the recent experience in Europe, and to a lesser extent, the United States, highlights the importance of a credible medium-term approach to fiscal policy.

In recent decades, Australia has been well served by a bi-partisan commitment to sustainable public finances. The willingness of Australian Governments to build up fiscal reservoirs in the good times and to deploy those resources when needed to help sustain the economy, as we saw during the GFC, has contributed much to the stability of the economy in the last two decades.[1]

Critically, having deployed our fiscal ammunition during the GFC, the imperative today is to return to surplus and to pay down debt — to begin to recharge our fiscal ammunition for future use if needed, and to ensure that fiscal policy plays its part in delivering macro-economic stability in stronger economic circumstances.

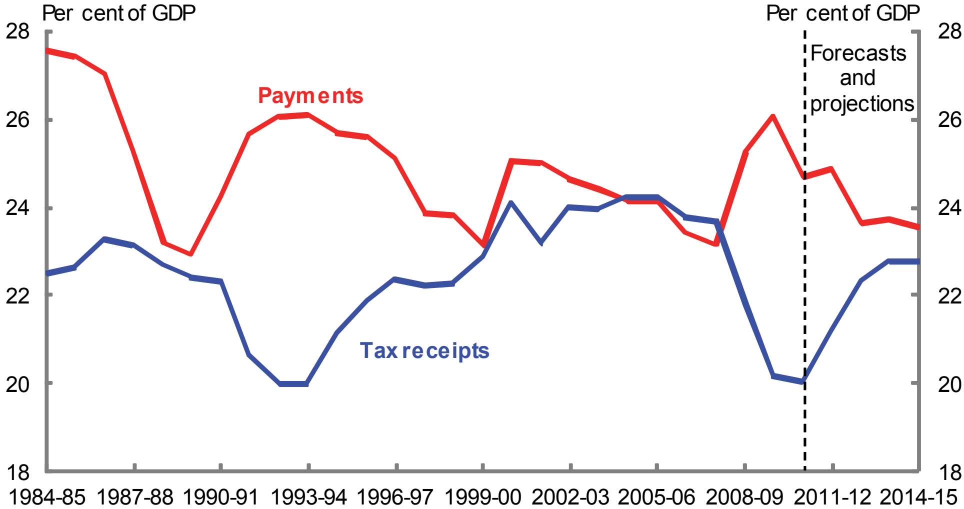
That said, the task of maintaining medium-term sustainability for both the Commonwealth and the States has been made harder by developments in the revenue base. Indeed, for both levels of government, surpluses are likely to remain at best razor-thin without deliberate efforts to significantly increase revenue or reduce expenditure.

This predominantly reflects the sharp weakening of revenue collections over recent years.

The tax-to-GDP ratio has fallen by 4 percentage points since the GFC, and is not expected to recover to its pre-crisis level for many years to come. This reflects a combination of cyclical and structural factors. Capital gains tax has been hit hard in the aftermath of the crisis. Households are more cautious in their spending pattern, dampening indirect taxes in the process. Meanwhile, the resources boom and the increasing importance of the mining sector is having significant impact on tax revenues. Mining companies account for about a fifth of gross operating surplus, yet only around a tenth of company tax receipts, primarily because tax receipts from the industry are affected by the high levels of investment occurring in the sector and the consequent level of depreciation deductions. Finally, the historically high Australian dollar hurts profits in, and taxes from, the non-mining export, and import-competing, sectors.

1 This is not to suggest that policy has been appropriately calibrated at all times, but rather that fiscal policy has tended to lean against the state of the economy at most times since the mid-1980s.

Chart 5: Tax receipts and total payments to GDP since the mid-1980s



Source: 2011-12 MYEFO.

With muted growth in tax receipts projected for much of the next decade, Australia will need significantly greater expenditure restraint in the decade ahead than was seen in the first half of the 2000s if we are to deliver the sort of fiscal outcomes likely to be required for sound macroeconomic management and as we pay down debt.

At the same time, there is an emerging debate about the desirability of a Sovereign Wealth Fund (SWF). Putting aside the fact we already have an SWF (the Future Fund), the conflicting objectives of the different proponents of a new SWF, and whether our superannuation system already has some of the characteristics sought in a new Fund, it is worth making a fairly straightforward observation.

Specifically, Treasury is often characterised as being opposed to an SWF — yet our comments are neither supportive nor critical. Rather, we continue to observe that the creation of an SWF per se does nothing to address either Australia's net debt position or, more broadly, the level of government or national savings over time.

If the Australian Government had financial liabilities of $10 billion and runs a $1 billion surplus, it can reduce gross liabilities to $9 billion, or it can maintain them at $10 billion and buy $1 billion of financial assets to be held in an SWF — in both cases, net financial liabilities are $9 billion.

The only way the creation of a Sovereign Wealth Fund delivers a faster improvement in net debt is if it is used to justify a tightening of fiscal policy that would not otherwise be achieved.

As such, if we are to have a sensible discussion about the merits of an SWF, the proponents of such Funds, whether at the national or sub-national level, need to be clearer about precisely what they have in mind. Absent tough fiscal decisions, an SWF does not constitute a contribution to future fiscal sustainability.

Conclusion

I hope these brief comments have given a little more clarity to some of the things my colleagues and I have been saying over the last year regarding the key challenges confronting Australia.

Thank you.

Key themes from Treasury's Business Liaison program

Overview

As part of its quarterly Business Liaison Program, Treasury met and held teleconferences with businesses and organisations during February and March 2012. Treasury greatly appreciates the commitment of time and effort by the organisations that participate in this program.

Liaison discussions pointed to uncertainty around the global outlook as continuing to weigh down on business sentiment. The strength of this concern remained mixed with firms in the mining and related sectors such as parts of construction and transport reporting a strong pipeline of investment and activity while contacts in retail and manufacturing generally had a more sanguine outlook.

While labour market conditions had eased over the course of 2011, there are some niche areas where skills shortages and wage pressures are likely to remain.

Activity

Strong demand was again evident in the resources sector. Activity and investment continues to be supported by strong demand from emerging Asia, in particular China. On the east coast, firms reported that coal production had yet to fully recover from the adverse weather events in early 2011.

Activity continues to remain uneven across the rest of the economy. Contacts in the retail sector reported that the trading environment was challenging with some retail lines, such as women's fashion, deeply discounted over the Christmas period. Contacts cited the elevated Australian dollar as a key source of pressure with customers increasingly shopping online and greater numbers of Australians holidaying overseas instead of domestically.

Contacts in the manufacturing sector noted that trading conditions continued to be difficult and highlighted the sustained high Australian dollar as a key source of pressure. However, firms did note that there were some positive effects of the high exchange rate, namely that this lowered the cost of imported capital equipment. Contacts in consumer goods areas of manufacturing also highlighted waning domestic demand as a concern and expected that this would continue to be the case in the near term.

Employment and wages

Overall, contacts reported an easing in hiring conditions although, as with activity, the story was mixed across sectors. Recruitment in the mining and energy sectors remain at record levels, with the recent global downturn having no material impact on in hiring. An excess of demand for skilled employees has also seen firms in the mining and related construction sectors being less selective in recruitment, but spending more on training.

Contacts in the mining sector continued to report strong use of fly-in-fly-out workforces with some contacts in Western Australia noting that they are increasingly flying in workers from the eastern seaboard, as well as from Perth.

In the non-mining sector, firms reported a noticeable slowdown in recruitment through the second half of 2011. Some businesses reported responding to global uncertainty by increasing the average hours worked of their existing workforce rather than taking on new employees.

Strong wages growth is expected in the mining and related sectors of the economy, particularly in professions where skills shortages are being felt most acutely. Overall, contacts in non-resources related sectors reported a softening of wage pressures since the middle of 2011.

Financing and investment

Overall, reports on credit conditions remained largely steady this round. Large firms generally noted that, while capital market conditions were challenging in 2011, credit was available at reasonable rates.

Some concerns regarding credit in construction, with contacts in the non-residential sector reporting that, particularly for office space, projects have required increasingly higher levels of pre-commitment to secure finance since the Global Financial Crisis.

In the manufacturing sector, several firms noted the importance of productivity improvement and innovation programs to their business. One firm noted that, despite tough trading conditions, they were continuing to heavily invest in new product innovation.

Harold Holt: an urbane treasurer

John Hawkins[1]

Harold Holt is regarded as one of the most amiable and diligent treasurers. His reputation as treasurer was enhanced by strong economic growth and low inflation and unemployment, although the 1961 credit squeeze was a blot in his copybook. He oversaw the establishment of the Reserve Bank and the smooth introduction of decimal currency. Sadly his career as treasurer and prime minister was overshadowed by the political difficulties in his last year and the tragic circumstances of his death.

Source: National Library of Australia.[2]

1 The author formerly worked in the Domestic Economy Division, the Australian Treasury. This article has benefited from comments and suggestions provided by Selwyn Cornish, Tom Frame, Ian Hancock and Terry Larkin. The views in this article are those of the author and not necessarily those of the Australian Treasury.

2 ‘Portrait of Harold Holt, M.H.R. for Fawkner, Victoria’, Bib ID: 1020573.

Introduction

The Right Honourable Harold Holt was renowned for amiability rather than intellectual rigour; a 'thoroughly decent man', a bon vivant with 'a ready smile and natural charm'.[3] Enid Lyons, however, saw 'greater depths of character than appeared on the glossy surface'.[4] Holt was 'not a natural orator'.[5] He had 'a capacity for calmness in situations where others may have been disposed to panic'.[6] He placed particular importance on loyalty.[7] Menzies recalled of Holt 'his besetting sin – he wanted everyone to love him'.[8] Perhaps this reflected that he 'never received the parental affection he appeared to crave'.[9]

Sadly 'the circumstances of his death came to overshadow the achievements of his life.'[10] It was rumoured he had once prophesised that he would not live to sixty and that this drove him to try to achieve before then.[11] His wife recalled that as treasurer Holt 'never had one holiday at all ... or even a weekend when he didn't work'.[12] He kept himself fit and projected an image of vitality. He had 'astonishing stamina'.[13]

Holt's early life

Holt was born in Sydney on 5 August 1908. His father was then a schoolteacher, but he subsequently pursued a career as a hotelier, theatrical manager, filmmaker and radio

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3 Hancock (1996). Among his cabinet colleagues, Spender (1972, p 29) recalled 'a great mixer who loved life intensely'. Snedden and Schedvin (1990, pp 66, 257) recalled 'a very charming man'. Perhaps more telling, political peers from outside the Liberal Party shared this view. Fadden (1969, p 150) recalled him as 'one of the kindest men I knew in politics'. Whitlam called him 'tolerant, humane and broad-minded … a truly civilised human being'; *Hansard*, 12 March 1968, p 13. Similar views are expressed by those outside parliament who knew him; Golding (1996, p 227), Fricke (1990, p 174) and Horne (1967, p 26). He was not without some vanity; by the 1960s his speeches in parliament were prepared on a special jumbo script typewriter so he could avoid wearing glasses while reading them.

4 Lyons (1972, p 25), She cited 'his scholastic attainments and the substance of his speeches'.

5 Pemberton (2003, p 57), with whom Hughes (1976, p 167), Lyons (1972, p 25), Reid (1969, p 17) and Whitington (1972, p 124) agree.

6 Frame (2005, p 125). Holt's greatest inspiration was Kipling's poem "If".

7 Rodan (1977, p 287).

8 Menzies interviewed in 1974; *The Age*, 28 November 1979, p 9. Coombs (1981, p 270) referred to Holt as 'too nice a person to exercise power effectively'.

9 Clark (1973, p 246).

10 Peter Costello, another member for Higgins, deputy Liberal leader and long-term treasurer; in his forward to Frame (2005, p ix).

11 E. Holt (1969, p 139). His father had died before sixty. Holt himself died aged fifty nine.

12 Z. Holt (1968, pp 35, 75). Hughes (1976, p 167) called him 'a hard worker, obsessive perhaps'.

13 Hancock (2000, p 283); Warrender (1973, pp 147-8). Horne (1967, p 29). Holt could survive on little sleep; Hancock (2002, p 169) and Larkin and Baker (1968, p 13).

station manager; divorcing Harold's mother Olive when the boy was ten,[14] and moving around a lot. As a result, Harold was sent to boarding schools, briefly at Abbotsholme where he met another future treasurer William McMahon, and later at Wesley in Melbourne. He studied law at the University of Melbourne, graduating in 1930. Holt was a member of the university debating team and appeared in amateur theatrical productions. He also captained his college in cricket and represented it in tennis and football. Holt was admitted to the bar but the depression was a difficult time to start a career as a barrister so he began practising as a solicitor.

Holt showed an interest in politics at university. His wife recalled him saying 'I'm not interested in making money. I only want to get things done'.[15] Holt became a member of the Young Nationalists, of whom Menzies was a leading light.

Into federal parliament

Holt stood unsuccessfully for the United Australia Party in the 1934 election against former prime minister and treasurer Jim Scullin, and contested another Labor seat in the Victorian state elections. Helped by support from Menzies, he was preselected for a safe federal seat in 1935, entering parliament as its youngest member at a by-election as the member for Fawkner, which he held until he transferred to the new seat of Higgins in 1949.

Early on he supported funding to relieve unemployment, particularly youth unemployment.[16] The promotion of physical fitness was another common theme.[17] Holt sponsored the formation of a National Fitness Council. He also found time to give women fashion advice, warning that short dresses 'are anything but subtle and frequently unbecoming' and recommending pastel coloured summer frocks.[18]

In 1939 he became an assistant minister to Casey at the new Department of Supply and Development, at the age of 30 one of the youngest ministers there had been. But when Menzies re-formed the coalition in March 1940, Holt had to be dropped to make space for a Country Party minister.

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14 Holt's mother died when he was sixteen.

15 Z. Holt (1968, p 33).

16 He argued the government could create employment in two ways; 'first, it can create an atmosphere in which private industry can flourish, and thus of itself create employment, and, secondly, it can grant financial assistance to the States for works which, most effectively, will help to improve the employment situation'; *Hansard*, 14 May 1936, p 1749. He also discussed youth unemployment in his speech on the budget; *Hansard* 14 October 1936, pp 1101-4, and in parliamentary speeches on 17 June and 2 September 1937.

17 eg *Hansard*, 14 October 1936, pp 1105-7.

18 *Table Talk*, 22 April 1937, p 11.

Holt then enlisted for military service and trained as a gunner but after the death of three ministers he was recalled to Canberra by Menzies before having the chance to serve overseas. After the September 1940 elections he joined cabinet as minister for labour and national service. Menzies resigned as prime minister, with Holt in his first and only act of disloyalty not offering him support. Holt continued as a minister in the Fadden Government until it fell in October 1941. The secretary of his department in 1941 was the 'rising star' Dr Roland Wilson who made a 'formidable team' with Holt.[19] In March 1941 Holt introduced national child endowment.[20]

While in opposition Holt was the Liberals' main spokesman on industrial relations. He also often spoke on economic issues. While admiring Chifley the man, he criticised Chifley's first budget for taxing companies excessively.[21] He criticised later budgets for taxing employees excessively.[22] Unusually for a leading politician in a free enterprise party, Holt argued that, at least in a wartime context, 'the Government should determine what is a fair price for a company to charge for its products. Then if such a company can, by raising its efficiency and applying greater skill and energy to its problems, increase its profits, whilst at the same time maintaining a fair price to consumers, the Government should encourage its activities…'.[23] He also called for government finance to be provided at low interest rates to facilitate the construction of housing.[24]

After the defeat of the Chifley Government in December 1949, Menzies again appointed Holt as minister for labour and national service. From 1949 to 1956 he was also minister for immigration and in addition had ministerial responsibility for the 1956 Melbourne Olympics.

Holt announced his candidacy for the deputy leadership of the United Australia Party after the 1943 election defeat but withdrew when Hughes stood. When the post

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19 Frame (2005, p 24). Menzies had also identified Wilson's ability and planned to ask him to be his economic adviser but Holt got in first; Cornish (2002, p 23).

20 The payments covered all but the first child. In his speech Holt went back to a speech by Pitt the Younger in 1795. He also quoted Keynes' *How to Pay for the War* to justify introducing the measure during wartime; *Hansard*, 27 March 1941, pp 338-9. Fadden as acting prime minister gave the responsibility of introducing the legislation to Holt as 'it would be to his great advantage to be associated at this stage of his career with such a major measure'; Fadden (1969, p 149).

21 *Hansard*, 5 November 1941, p 104.

22 For example, speaking on the 1944 budget, he said 'men of all walks of life are refusing to give of their best because they would reap no personal reward'; *Hansard*, 19 September 1944, p 968. When a Labor member referred to the 1945 budget as 'scientific', Holt retorted that it was 'as about as scientific as a meat pie and its ingredients are equally dubious'; *Hansard*, 19 September 1945, p 5587.

23 *Hansard*, 5 November 1941, p 104.

24 *Hansard*, 2 October 1945, p 6259.

became vacant again in 1944 Holt did not stand. By 1949 Holt ranked fourth in the cabinet, behind only the leadership team. In 1956 he became deputy leader of the Liberal Party, confirming him as Menzies' likely successor, and leader of the house.[25]

Holt married Zara Fell (nee Dickens) in 1946. They had courted as students but she had gone abroad and married in the interim, publicly resuming their relationship after her divorce.[26] Zara contributed to maintaining the Holts' lifestyle with her successful fashion business and in time her 'exuberant candour and breezy, effervescent modern style' made her probably the best-known prime ministerial consort since Enid Lyons.[27]

Treasurer

When Fadden retired in December 1958, his successor as Country Party leader, McEwen instead stayed as minister for trade and Menzies appointed Holt as treasurer. Views differ about whether McEwen was offered the treasurer's job but preferred to stay at trade (as McEwen himself claims) or whether, as Roland Wilson recalls, it was more a case of a distrustful Menzies not offering it.[28] In terms of interest, Treasury may not have been Holt's preference. Holt's biographer said 'Treasury was not a portfolio which intrinsically interested Holt … Holt's experience in economic matters was limited'.[29] Holt was, however, keen to take the job lest someone else use it to establish themselves as a rival successor to Menzies as prime minister.[30] Holt gave up gambling on the horses when he became treasurer; perhaps concerned at the image it would create or perhaps regarding taking the job as a political gamble itself.[31]

After almost two decades Holt was reunited with Wilson, 'a source of strength for him'.[32] Indeed Holt was blessed by the array of talents advising him, with his tenure coinciding with the peak of both Treasury's power and that of the public service

25 There had been speculation about his imminent succession as far back as 1951; Frame (2005, pp 54, 57) and West (1965, p 225). Menzies seriously contemplated retirement in 1961 but believed Country Party leader McEwen would then seek the leadership of the coalition, and when the Liberals denied it to him would refuse to serve under Holt and split the coalition; Menzies and Henderson (2011, p 89).

26 It is widely believed her twin children had been fathered by Holt; Frame (2005) and Hancock (1996). Holt had also dated Lola Thring, daughter of his father's business partner (and sister of flamboyant actor Frank Thring), but she not only rejected Holt but married his father.

27 For accounts of Zara's life, see her autobiography, Z Holt (1968), and Langmore (1992).

28 McEwen and Jackson (1983, p 57), Golding (1996, p 128), Reid (1969, p 34), Frame (2005, p 99) and Costar (1995, p 103) give conflicting accounts.

29 Frame (2005, p 100). Larkin and Barker (1968, p 17) suggest 'his real love was external affairs'.

30 Reid (1961, p 12).

31 Reid (1961, p 12).

32 Nugget Coombs (1981, p 270). A future treasurer called Wilson 'probably the most able and cleverest man the public service has ever employed'; Bury (1975). See also Cornish (2010a) and recollections of Treasury colleagues in Treasury (2001, pp 57-59).

'mandarins'.[33] Other than Wilson, Holt's main advisers were Treasury deputy secretaries Richard Randall and Lenox Hewitt.[34] Also influential were some economists in the Prime Minister's Department; Wilfred Salter and Ron Gilbert. The academic Trevor Swan was also drawn on.[35] Reserve Bank governor Coombs was less influential than he had been with Fadden.[36]

Views differ about how Holt's appointment was received within Treasury. Hasluck recalled 'Roland Wilson and Len Hewitt…did much doleful head-shaking in anticipation of Holt's appointment … [but] they did come to regard him as one with whom they could work satisfactorily'.[37] Another account says 'Treasury generally approved of the appointment: Holt had the requisite seniority and skill in cabinet to win a brief, and he did not have a dangerously independent mind or a personal agenda.'[38]

In contrast to most of his predecessors (notably the anglophile Menzies), Holt 'travelled widely throughout south-east Asia, where he believed Australia's economic future lay'.[39] He enjoyed the travel, commenting 'finance ministers – who normally must exhibit the professional gloom of the undertaker – are never happier than when exclusively together'.[40]

Holt expressed the focus on economic growth that characterised Treasury; 'growth is our watchword as a government on behalf of the people of Australia. It is also the password for the sentry at the gate to our security and our prosperity.'[41] With macroeconomic conditions stable, Holt concentrated in his 1963 budget speech on measures to promote longer run economic development, including by 'direct aids and incentives to private enterprise'.[42]

The resources sector expanded with the opening up of iron ore mines. Holt referred to recently 'discovered mineral wealth beyond our dreams' and expected to soon draw on nuclear power.[43] Treasury was even more enthusiastic, referring to 'the greatest

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33 Cornish (2010a).

34 The upper ranks of Treasury were remarkably stable, with Wilson (appointed secretary back in 1951) and Randall holding their posts for the whole time Holt was treasurer.

35 Martin (1999, p 431).

36 This was partly a matter of geography; the Queenslander Fadden often stopped off in Sydney on his way home from Canberra but the Melbourne-based Holt was less often there.

37 Hasluck (1997, p 128).

38 Hancock (1996).

39 Warrender (1973, p 150). Horne (1967, p 26) describes Holt as developing a 'feeling for the Asian-ness of Australia'.

40 Holt, referring to a London conference in his diary, 11 September 1962, NLA MS 8431.

41 Holt (1967, p 3). By contrast the Reserve Bank was more concerned about avoiding inflation.

42 *Hansard*, 13 August 1963, p 10.

43 Holt (1967, pp 4 and 17).

breakthrough in point of resources since the crossing of the Blue Mountains a hundred and fifty years ago'.[44]

Early budgets

Holt inherited a strong economy. Real GDP expanded by over 7 per cent in 1958-59. Many economists, including in Treasury, were coming to regard inflation as the greater medium-term economic challenge than maintaining full employment.[45] Wages, property prices and equity prices all accelerated through 1959.

Holt's first budget, in August 1959, was dubbed the 'give and take' budget. It added to the inflationary pressures by introducing a 5 per cent rebate on income tax and raised pensions, but increased postal charges. Holt observed that it was criticised both for its supposed timidity and its alleged recklessness.[46]

Holt's first budget employed Keynesian language. He said of the 1963 budget that 'given unused plant capacity … the budget should have a strong expansionary effect'.[47] In his 1965 budget he said 'some years it appears right that, to stimulate expansion generally or in some sectors, expenditure ought to be allowed to rise ahead of receipts, in other years there should be some check on the rate of increase in demand'.[48]

1961 credit squeeze

With inflation reaching 4½ per cent in 1959, Treasury became increasingly concerned and made these concerns public.[49] In February 1960 import licensing was abandoned, at least in part as an anti-inflationary measure, but the balance of payments started to deteriorate. While Treasury and the Reserve Bank were pushing hard by early 1960 for tighter fiscal policy, little was done until the budget, when Holt announced the abolition of the 5 per cent rebate on income tax and increase in company tax.[50] In

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44 Cited in Whitwell (1986, p 149).

45 Whitwell (1986, pp 124-5). Treasury (1960, pp i, 27) says 'what appears necessary for a greater success is a more general resolve to resist inflation as an evil in itself and a threat to the continuation of steady expansion…any degree of inflation is harmful to the broad interests of the economy … a moderate rise in prices can seldom if ever be kept moderate'.

46 *Hansard*, 27 August 1959, p 688.

47 *Hansard*, 13 August 1963, p 22.

48 *Hansard*, 17 August 1965, p 32.

49 Treasury (1960, p 17) remarked 'at the beginning of 1960 … the price and cost movement … had already become too fast … it was certain to become faster'.

50 In March Holt acknowledged 'inflationary pressures' but regarded a call up of special accounts by the Reserve Bank, removal of import controls and calling on the Arbitration Commission not to increase the basic wage as an adequate response; *Hansard*, 15 March 1960, p 223.

November, however, Holt agreed to Treasury advice[51] and announced a package of deflationary measures including increased sales taxes on cars and some reduction in interest deductibility for company tax.

Monetary policy was also tightened through 1959-60, with the Reserve Bank increasing the amounts the trading banks had to place with it and their holdings of government securities, and requesting they moderate their advances. In mid 1960 the Reserve Bank wanted to raise interest rates but Holt rejected the idea. The Bank considered using the formal provisions for resolving differences between the Bank and the government but refrained, and Holt agreed later in the year to the rate rise.[52] The banks were told in November 1960 that they must achieve a 'considerable reduction' in advances by March 1961. Holt said 'this outpouring of bank credit … must be stopped'.[53] This set of measures passed into history as the 'credit squeeze'.[54] Some saw it as a repeat of the 1951 'horror budget' with deflationary action both too late and too strong.[55]

By historical standards, and compared to recessions to come, the 1961 recession was strong judged by GDP but relatively mild in its effect on employment.[56] In some ways Holt was the victim of Fadden's success; before the War or since the 1970s a 3 per cent unemployment rate would be seen as very low but the unemployment rate had averaged under 2 per cent during the 1950s.

The credit squeeze was blamed for the Liberal-Country Party coalition almost losing the 1961 election. There were calls for Holt to be removed as treasurer, but he retained Menzies' confidence.[57] The 1961 budget announced temporary cuts in immigration and some reductions in sales taxes.

In response to signs that the economy was weakening more than was desired, a 'mini-budget' was announced by Menzies in February 1962 which restored the 5 per cent rebate on income tax, cut sales tax on cars, restored full interest deductibility for companies and introduced a generous investment allowance. Import restrictions

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51 Hancock (2000, p 274). Wilson, Randall, Coombs and some other senior Treasury officers had drawn up the package. Among the politicians, Menzies and McEwen had been involved in their preparation.
52 Cornish (2010b, p 125).
53 Hansard, 15 November 1960, p 2853.
54 Sometimes referred to as the 'Holt jolt'; Millmow (2010) and Pemberton (2003).
55 Whitwell (1995, p 176; 1996, p 138).
56 In real GDP terms it was comparable to the recessions of the early 1950s, mid 1970s and early 1990s but smaller than that of the early 1980s; Ewing and Hawkins (2006, p 30).
57 Even in the following campaign in 1963 Holt was given only a minor role for fear of public resentment about the Treasurers' role in the credit squeeze; Whitington (1964, p 74). Menzies, however, pointed out the credit squeeze reflected cabinet decisions, so Holt should not be blamed; Frame (2005, p 116) and Millmow (2010).

were reintroduced. The banks were encouraged to lend more for housing. Public works expenditure was increased and there was a rise in the unemployment benefit.

This reversal was characterised as 'stop/go' or 'confusion' in some quarters[58] but Treasury defended it as the government's willingness to 'adapt its measures to changing circumstances' given 'the effect of economic measures cannot be calculated in advance with close precision'.[59]

Central banking and bank reforms

In 1959 Holt reintroduced Fadden's bill splitting the Commonwealth Bank off from the Reserve Bank, which had been blocked in the Senate prior to the 1958 election, paying generous tribute to his predecessor.[60] The special deposits were replaced by statutory reserve deposits, giving the Reserve Bank what Holt regarded as 'ample powers of regulation of bank credit'.[61]

Holt noted the development of the short term money market and that the central bank had taken measures 'to ensure the further development of the market will be soundly based' by providing lines of credit to authorised dealers at an interest rate set 'to discourage too frequent borrowing'.[62] This was an early step towards a more market-based system of implementing monetary policy, as well as a means of addressing the seasonality of rural and government finance.[63] Holt was lobbied by foreign banks but, under Treasury's influence, opposed their entry.

Decimal currency

Holt was treasurer during the preparations for the introduction of decimal currency. Holt convinced cabinet to reverse the earlier stance (most likely inspired by Menzies) and to call the new currency the 'dollar' rather than the 'royal'.[64] The Royal Australian Mint also opened during Holt's tenure as treasurer.

Economic planning and the Vernon Report

As in the UK, the early 1960s was a time when interest grew in Australia in longer-term economic planning, although there was never any enthusiasm for it within

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58 This adoption of many Labor policies they had excoriated at the election two months previously was described as 'one of the most dramatic somersaults of this highly gymnastic government'; *Australian Financial Review,* 8 February 1962, p 1.

59 Treasury (1961, p 31).

60 *Hansard*, 26 February 1959, pp 375-6.

61 *Hansard*, 26 February 1959, p 383.

62 *Hansard*, 25 February 1959, p 260.

63 Chapter 8 of Schedvin (1992).

64 Frame (2005, p 129).

Treasury.[65] In 1963 a committee was appointed to examine longer run economic issues, headed by Sir James Vernon, managing director of the Colonial Sugar Refining Co.

The report was given to the Government in May 1965. In September Holt was explaining their failure to release it on the grounds it would be 'quite unsatisfactory … to table the report without first having taken time to study it closely'.[66]

When its voluminous report was finally tabled some days later, Menzies was dismissive, declaring it had exceeded its brief by commenting on policy, and taking especial opposition to its support for a degree of economic planning.[67] Through Holt, Treasury had sent cabinet highly critical submissions about the Vernon Report, which may have been motivated by concerns that the Report's recommendations could have established alternative sources of economic advice to Treasury.[68]

Later budgets

Holt 'streamlined the procedure'[69] of preparing the budget and established a pattern of retreating to his northern Queensland holiday house for a fortnight before the Budget. The media presented this as Holt putting together the budget although of course the real work was being done back in Canberra by Treasury officers. The August 1962 and 1963 budgets were described by the press as 'same again' and 'even keel' with no dramatic initiatives.[70] Holt himself characterised the 1962 budget as part of an 'expansionary programme until the economy is operating at the highest level of activity we can hope to sustain'.[71] But he was in a cautious mood, commenting 'we do not want another boom like that of 1960'.[72]

Publicly Treasury was very optimistic in June 1963, arguing that 'expansion has broadened out rather than gained markedly in tempo. If there ever were a time when stability and growth went together, this is it'.[73] But there were again concerns that the

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65 Whitwell (1995, pp 176-7; 1996, pp 139-40).

66 *Hansard*, 16 September 1965, p 964.

67 *Hansard*, 21 September 1965, pp 1078-87. Menzies proclaimed 'the Committee…predicated a degree of planning and direction of the economy which in our opinion would not either be appropriate or acceptable'. Earlier Holt had been sufficiently open to the idea of planning to talk to the Italian finance minister of 'recent Australian discussion about the possibilities of a greater degree of national planning' in Australia; Holt's diary, 5 September 1962, NLA MS 8431. Holt did not speak in the parliamentary debate on the Report.

68 Martin (1999, pp 530-4) and Corden (1968, p 54). A potential supporter of the report, McEwen, was out of the country when it was released; McEwen and Jackson (1983, p 66).

69 Howson (1984, p 103).

70 Pemberton (2003, p 15).

71 *Hansard*, 7 August 1962, p 14.

72 *Hansard*, 7 August 1962, p 15.

73 Treasury (1963, foreword).

economy was overheating, in part due to increased government spending. Holt was less concerned than his Treasury about expanding government spending. Indeed he saw it as inevitable; 'public spending is bound to continue rising because it represents the foundation of our economic growth.'[74]

This concern about inflation was one reason Menzies called an early election in November 1963. Menzies won comfortably, setting the stage for an orderly transition when he decided to stand down. With the election out of the way, some deflationary measures were adopted in the 1964 budget, with the income tax rebate discontinued, company tax increased, higher taxes on cars and cigarettes and an increase in television licence fees. Monetary policy was also tightened and the Government opposed any increase in the basic wage. The following year income tax was increased further, with increased taxes on beer, alcohol and tobacco products – a classic 'beer, cigs up' budget in tabloid parlance.

Inflation did not in the event rise much. The last, and the best received, of Holt's seven budgets was delivered in 1965 in an economy with 'virtually full employment'.[75] A feature was 'the largest expenditure increase for which a Commonwealth budget has ever had to provide'[76] as defence and social welfare spending and payments to the states were increased markedly.

At the end of his treasurership, Holt regarded as his achievements prosperity, full employment and high levels of home ownership and foresaw 'a decade of very dramatic economic development, based partly on the mineral discoveries'.[77] He observed, however, that 'treasurers are not normally popular people because of the taxes they have to impose and because of their role as critic and analyst of spending proposals put up by their cabinet colleagues'.[78]

Other aspects

Holt was the first treasurer, in 1960, to chair the annual meetings of the IMF and World Bank in Washington. He was a regular attendee at overseas meetings as treasurer, taking an overseas trip every year after presenting the budget.

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74 Holt (1967, p 16).
75 *Hansard*, 17 August 1965, p 43.
76 *Hansard*, 17 August 1965, p 31.
77 Interview in *The Age*, 21 January 1966, p 3.
78 Harold Holt, interviewed in *The Age*, 21 January 1966, p 3.

While Holt was treasurer the first steps were taken against restrictive trade practices. But this was handled by the attorney-general.[79]

Prime minister

When Menzies retired, Holt was the unanimous choice of the party room to take over as prime minister on Australia Day 1966, bringing a new informality and modernity to the role. He won a resounding victory over the septuagenarian Arthur Calwell at the 1966 elections.[80]

In 1967 the new opposition leader Gough Whitlam put him under more pressure, and he lost by-elections and a referendum proposal and suffered a large swing at a half-Senate election as the Vietnam War was losing public support.[81] His decision not to follow the UK in devaluing the currency was attacked by the Country Party leader John McEwen, stranded in Geneva, but Holt held firm.[82]

Holt made a fateful decision to enter a rough surf on 17 December 1967 and was never seen again. While there have been suggestions Holt may have been depressed or even suicidal, and some even more fanciful theories, his death appears to be the result of a display of bravado by a man no longer in peak fitness, and possibly distracted by political challenges, entering a dangerous surf and either drowning or being taken by a shark.[83] His memorial service was attended by the British prime minister and

79 As Whitington (1964, p 63) puts it this involved a 'series of remarkable alarms and excursions … [with] industry protesting violently about what it feared might be happening, constitutional experts questioning the Government's powers, lawyers and retired public servants saying the Government was proposing to do either too much or too little'.

80 The coalition won a then record majority of seats and the two-party preferred vote of 57 per cent remains the largest ever recorded.

81 He may not have planned to stay on as prime minister that long. Larkin and Barker (1968, p 17) suggest 'his real love was external affairs' and he planned to step down and take that portfolio once he identified a suitable successor.

82 Holt regarded facing down McEwen as ‘his most satisfying experience as prime minister’, according to those interviewed by Rodan (1977, p 242). He did, however, include a large support package to appease McEwen.

83 For conflicting accounts of Holt's condition at the time of his disappearance see the TV documentary by Butt (2008) and accounts by Commonwealth and Victorian Police (1968), Davey (2010, p 118), Frame (2005), Fricke (1990, p 181), Hancock (1996), Henderson (1994, pp 188-191), Howson (1984, pp 361, 366, 368, 427), Larkin and Barker (1968), McNicholl (1978, p 44), Menzies and Henderson (2011, pp 172-3), Reid (1971, p 24), Snedden and Schedvin (1990, pp 77-78), Trengrove (1969, pp 178-9 and 184), and the letters to the editor, most notably from Holt's press secretary Tony Eggleton, in *The Bulletin*, 27 November 2007. Some of these accounts suggest McMahon was plotting against him. The most fanciful theory was by Grey (1983), who suggested he was picked up by a Chinese submarine. Eerily, Holt once said of drowning, 'if you've got to go, this would be the way'; Larkin and Barker (1968, p 11).

opposition leader, the US president, the Prince of Wales and senior representatives of twelve Asian nations. Ironically, one of the memorials to him is a swimming pool.

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