The Journal of Australian Political Economy is a refereed journal. Its articles are indexed in APAIS (Australian Public Affairs Information Service), Econlit and IREL (the Australian industrial relations database).
### JAPE No. 64

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Editorial Introduction: Analysing the GFC

This issue of the *Journal of Australian Political Economy* examines the global financial crisis (GFC) that emerged in 2008-9 and considers the implications and lessons for Australia. This crisis has been widely interpreted as the most profound shock to the capitalist economy since the Great Depression that began in 1929. It has also been described as the first truly ‘globalised’ crisis.

By focussing on the GFC, this issue of the journal constitutes, in effect, a companion volume to the June 2008 issue that provided analysis of Australia’s economic boom 1992-2008. At the time that ‘long boom’ issue was published, the first signs of the impending financial crisis were starting to emerge, although the impact had not yet been felt in Australia. A number of the featured articles in the journal emphasised structural problems that the boom had masked and the systemic contradictions that had not been resolved. As the boom gave way to crisis, so this journal now follows the ‘rhythms of capital’ by focussing on the GFC. Like the earlier issue on the boom, this issue on the crisis is also a ‘bumper’ double-sized edition.

The articles come from three sources. First is the edited transcript of a talk presented by Canadian economist Jim Stanford at the University of Sydney in August 2009. This was the second Ted Wheelwright Memorial Lecture, presented to a large audience and providing an interesting and entertaining analysis of the crisis and the importance of grass-roots education in political economy. Stanford emphasises the contrast between the ‘real’ economy of productive work in which value is created and the speculative realm of financial legerdemain that accentuates capitalism’s tendencies to inequality and instability.

Second is a cluster of articles submitted in response to the general invitation that was published in the last issue of this journal. These are the articles by Thomas Bramble, Harry Perlich, Evan Jones, Therese Jefferson and Alison Preston, and Heribert Dieter. They are ‘in-depth’ assessments of various aspects of the crisis and the lessons learned (or,
more typically, not learned by mainstream economists and conservative media commentators.

The third group of articles comprises papers originally presented at a one-day seminar on ‘the GFC and the Australian City’ at Griffith University in Brisbane in August 2009. These include the contributions by Brendan Gleeson, Stephen Horton, Jago Dodson and Neil Sipe, Kurt Iverson, Paul Burton, Ian Manning and Boris Frankel. They are characteristically shorter contributions, reflecting their origins as seminar presentations. They are focussed on issues such as housing, transport, spatial planning and local government, emphasising that the economic crisis is related to the patterns of production, consumption and transportation that structure our lives in an urban society. Steve Keen’s paper also originated from the Brisbane conference, but its macroeconomic focus makes it more akin to the second cluster of articles in its content and style, and it is located earlier in the journal for that reason.

Brendan Gleeson, Stephen Horton and Patrick Troy took responsibility for the primary editorial judgements on this third group of articles and the editors of JAPE thank them for this valuable contribution.

How profound has the GFC been? Has it been just a ‘blip’ in the inexorable growth of the economy, particularly here in Australia, where ‘technical’ recession (defined as two or more successive quarters in which GDP falls) has been avoided? The breakout box printed on the opposite page might seem to suggest so. It is an extract from the speech about the GFC given by the Governor of the Reserve Bank of Australia in November 2009. With its talk of ‘economic flexibility’, ‘the relative strength of the financial sector’, ‘sensible management’ and ‘prudent fiscal and monetary frameworks’, it conveys a general complacency about the national/local significance of the GFC. Certainly, the effect of the GFC in Australia has been more muted than in some other countries such as the USA, UK and much of Europe. However, Australia is not alone in this regard: for different reasons, other countries such as Switzerland, Norway, Brazil and Nigeria had relatively favourable experiences too. Crises always have uneven impacts.
The issue before us is not how to get on to the road to recovery; we are already on it. The question, rather, is how to make sure that the road to recovery will connect to the road to prosperity.

Unless we are prepared to accept it has all been an incredible coincidence, we have to ask why things turned out that way. It wasn't just that China returned quickly to growth. Equally important were other factors, including the relative strength of the financial sector, the economy's flexibility and the willingness and scope to change macro-economic policy.

Those things were not accidents. Financial resilience resulted from sensible management by financial institutions and careful regulation on the part of the prudential supervisor. For the most part, the non-financial corporate sector was also fairly conservatively managed.

Moreover, businesses took a far-sighted view about employment decisions. Given the preceding difficulties in securing labour, they found ways of keeping people on payrolls, even if on reduced hours. They clearly had not only the good sense but also the requisite institutional flexibility to do that, which must say something about the progress that has been made in labour market arrangements during the past couple of decades.

And, finally, long-term investments in prudent fiscal and monetary frameworks paid off. A whole generation of policy-makers painstakingly worked to build credibility by making decisions with a long-run perspective.

G. Stevens, *Prosperity Isn’t Easy*, (extract) also reproduced in The Australian, 6.11.2009.

The authors in this issue of *JAPE* seek to tell a more profound story. While they present different views of the GFC, the common element is an emphasis on its deep-seated structural roots and implications. So there should be no complacency, even if the most recent macroeconomic indicators suggest only a mild downturn and that the worst has passed.

What are the structural problems? Steve Keen’s article emphasises the cumulative problems of unsustainable household debt. Harry Perlich’s piece examines problems of structural imbalance, particularly the ‘dual economy’ character that exists because Australian states have different economic characteristics. Moreover, as the article by Evan Jones documents, Australia’s financial institutions have a lot to answer for – before the crisis, during it and into the future. There are significant international political economic imbalances and tensions too, as Thomas
Bramble’s article argues. There has also been a lack of effectively coordinated governmental responses, as Heribert Dieter shows with particular reference to the European situation. Keynesian stimulus measures have been the limited focus of national governments, leaving many of the longer term structural problems unresolved.

The uneven impacts of economic crisis within Australia are also a major concern from a political economic perspective. Therese Jefferson and Alison Preston’s article highlights the gender dimension, drawing on recent data on employment trends for men and women.

Understanding the spatial inequalities of the GFC is also necessary. The connection between urban problems, macroeconomic problems and balance of payments problems is emphasised in the article by Ian Manning. The articles by Brendan Gleeson and Stephen Horton discuss the importance of temporal and spatial dimensions in the functioning of modern capitalism. Paul Burton looks at the Gold Coast – built on the shifting sands of tourism and property development – to illustrate how economic crisis impacts at the local level. Kurt Iveson’s contribution considers how crises fuel the processes of spatial competition but may also generate a cooperative urbanism. Jago Dodson and Neil Sipe highlight the unsustainability of the modern urban economy, a long-term problem that has to be faced irrespective of the resolution of short-term financial instability.

Reflecting on responses and prospects, Boris Frankel draws a distinction between the risk-taking character of governments and businesses and the risk aversion of the general public. Then, to conclude, we reprint an open letter about the GFC which emphasises the fundamental problems arising from orthodox economics education.

These various articles do not purport to cover all angles of the crisis. There is much more to be said about this complacency-shattering situation. Does the GFC signal the end of neoliberalism, as Prime Minister Rudd has implied, and what would that really mean? Does the crisis usher in a new stage of capitalism? Or are we simply to resume “business as usual”? Future issues of this journal are open for further contributions on these and other themes. Political economic analysis can thereby help us understand and shape the forces influencing our futures.
I am deeply honoured to deliver the second memorial lecture here at the University of Sydney in the name of Ted Wheelwright, one of the pioneers of the political economy movement.

The courageous struggles to preserve a space here for critical and progressive thought were reaching their crux just as I began my undergraduate studies in economics at the University of Calgary – one of the most conservative universities in Canada – in 1979. The fact that Ted Wheelwright and his colleagues dared to establish an economics school with radical foundations, and that subsequent leaders and students would fight so hard to defend and nurture it, opened doors for me as I struggled to find alternative visions, and mentors to teach those visions, in my own economics education. The Political Economy program here became one of the most important and inspirational centres of radical economic thought in the English-speaking world. While tonight is the first opportunity I’ve had to visit your campus, your example, reflected in like-minded initiatives on other continents, enhanced my own intellectual and political options by expanding the terrain of debate within our stunted and ideological profession.

Wheelwright’s personal research agenda also had a direct relevance to the traditions of radical political economy in Canada. His focus on critically understanding the economic actions and effects of multinational
corporations, and the dangers of the dependent mode of economic development characteristic of resource-abundant peripheral economies (like Australia and Canada), found immediate resonance in our own analyses of these problems. This included the thoroughly complementary work of scholars such as Mel Watkins (1963) and Kari Polanyi Levitt (1970), who wrote at about the same time as Ted of the economic and political dangers of a multinational-dominated, resource extraction-oriented mode of development. Wheelwright’s *Australia: A Client State* (with Greg Crough) could virtually have been re-issued in Canada, simply by changing the name of the country, so similar have been the circumstances of our respective trajectories of dependence.

And so I would like to begin tonight by thanking all of you here in this program – professors, students and alumni – for your sustained effort, inspired by Wheelwright and the other giants who came together here to nurture and defend this space. Your efforts made a fundamental difference in my life and training. And they did likewise for many thousands of other progressive-minded economics students around the world, who know in their guts that there must be better ways to understand the economic world (and to change it), but need help finding the way. Your program remains one of the best initiatives for showing young progressive economists that way. A coherent, united and high-quality place to study radical economics is a precious, fragile asset. I am so impressed by the spirit of unity and celebration that clearly infuses this event tonight and I urge you all to continue investing the energy and care that this program needs and deserves. It is important not just for training the next generation of radical political economists, but for educating and strengthening our movements and struggles for social change.

The importance of a critical economics pedagogy to those social change movements is the central topic for my presentation this evening. I consider myself an economics teacher, not just a practicing economist. I would guess that about a quarter of my work time is spent ‘teaching,’ in the broad sense of the term – although, unlike most in this room, I do not teach in a formal academic environment. Rather, my efforts to ‘spread the word’ take place among the working people who constitute the membership of my union (the Canadian Auto Workers), and the activist
base of the various grass-roots movements and campaigns in which I am also engaged (as both an economist and an instructor).

So tonight I would like to discuss the importance of critical economics training for these constituencies. For most of the engaged non-specialists whose knowledge and confidence in addressing economic issues and challenging conventional economic ideas will be essential to the success of social change struggles in the future, this will not be a matter of enrolling in a fine university program like Political Economy here at Sydney (although a few highly determined individuals might do that and, of course, I recommend it). Rather, we need to build a more inclusive, accessible and directly activist system for training our leaders and activists in the fundamentals of critical economics and political economy. And we need to do it systematically and energetically. This will strengthen our collective understanding of how the specific challenges we face stem from a common source: the structures and dynamics of a heavily financialized, globalized, aggressive capitalism. That understanding, in turn, will strengthen our collective ability to resist the regressive demands of employers and governments, and to fight for change – both incremental and far-reaching.

In my judgment, trade union members and other working people must have our own ‘story line’ about the economy and economics. Critical-thinking economists can help to build this story line by helping to translate their formal and technical understanding of the workings and failings of capitalism into more popular and accessible training initiatives, resources and materials. I wish that left academic economists generally invested more time and creativity into finding effective ways to share their knowledge with the movements that hunger for economic alternatives: see Stanford (2008). But the challenge of developing a mass critical consciousness about economics requires more than asking some progressive economics professors to come and teach occasional lectures at meetings of trade union activists. We need much more. We need a systematic and high-priority program to build awareness about economics and political economy among our leaders, activists and constituents, and to prepare them to intellectually fight back against the false models and false solutions propagated by mainstream economists and the other ideological servants of neoliberal capitalism.
The immediate circumstances of the global financial crisis, the resulting recession and the dramatic changes in economic policy that have occurred in the last two years in many countries, provide a good case study in the political importance of having our own story line. It seems that workers face a dual threat from this crisis. First, we are exposed to the immediate economic and social costs of the recession itself: lost jobs, lost incomes, lost homes and in many cases lost lives. Second, and more permanently, this crisis could actually and perversely lead to structural changes that further damage workers and their organizations. Far from conceding that there was anything wrong with the neoliberal recipe they forced down our throats, employers and pro-business governments will seize on the fear, confusion and divisions caused by the crisis to push for still more business-favourable measures.

Indeed, as the Canadian author and anti-globalization activist Naomi Klein explains in her latest book, *The Shock Doctrine* (2007), ruling elites regularly take advantage of moments of widespread fear and confusion, arising at moments of economic, social, or even natural disasters, to force through painful changes that they were preparing for years – but that the masses of people would not tolerate under ‘normal’ circumstances. The present global economic crisis will surely provide another test case for shock doctrine strategies. That is why we must be ready to push back with our own analysis of what happened, why it happened, what can be done to insulate working and poor people from its effects, and how to prevent it from happening again.

In my view, economic literacy and political economy training must be a core element of the organizing and movement-building efforts of trade unions and other progressive forces. We must equip our supporters to identify the true culprits, resist false solutions and fight confidently for better alternatives. Learning more about economics – from a workers’ perspective – is a crucial part of those preparations. That motivates much of my personal work as a union economist: whether that’s teaching, writing, interventions in public debates and support for the collective bargaining and other activities of my union.

I want to emphasize the importance of building the confidence of our activists in these economic literacy efforts. I do not believe we will ever teach large numbers of people the specific skills and techniques of
economic analysis (although we certainly need to have our own ‘experts’). In other words, our goal in this pedagogical work is not to train large numbers of ‘activist economists.’ Rather, what we must impart to masses of people within our constituencies is a different way of looking at the economic world, a different and more critical understanding of what the economy is, how it works (and doesn’t work), and who works (and who doesn’t work). We want our members and supporters to know, first of all, that they can discount the pompous and self-interested prognostications of professional economists – the overwhelming majority of whom (outside of academia) are employed by institutions (banks, corporations, business associations, and governments) with a vested interest in the status quo. We want our members and supporters to know that economics is a contested discipline; that there is nothing ‘neutral’ about economics; that one’s view on economics depends on one’s position in the economy. Finally, we want our movements to have an informed confidence in the viability and credibility of the alternative policies and structures we are fighting for. They need to have enough critical knowledge about real-world economics to know that conventional economists are lying when they claim ‘there is no alternative’ – whether that’s to globalization, austerity or corporate domination. And they need enough confidence in the viability and legitimacy of the things we are fighting for to sustain and empower our activism.

After all, we don’t actually win change on the basis of the credibility of our arguments. We win change thanks to the power of our movements and our fightbacks. It is not as if there is some high-level arbitration panel that decides our economic and social policies according to whose analysis and prescriptions are most compelling. Rather, it is the balance of power between conflicting and competing sectors and interests – economic, political, cultural power – that determines the direction of society. Of course, having credible arguments helps to build our power by motivating our supporters and enhancing their confidence to fight for change. But it is that fight, not the knowledge itself, which will win the day. I suppose that is a humbling realization for an economist. We must always be sensitive to the reality that our skills, our arguments and our pedagogy are only tools to be put at the disposal of our movements. It is those movements (not us) who are the main actors in the drama of social
evolution. For that reason, in my view, our work as progressive, engaged intellectuals must always be oriented around the pre- eminent priority of movement-building, rather than indulging in a more arcane conception of the ‘pursuit of knowledge.’

In terms of responding to the current moment of crisis in global, financialized capitalism, our story line about the crisis, its causes and consequences must similarly aim to enhance the confidence of our members and supporters to reject claims that workers, unions, and/or social programs were somehow responsible for the meltdown of private finance. For starters, the crisis has sparked intense interest in economics among many individuals; I’ve never encountered such widespread desire to learn more about the economy from rank-and-file members of our communities. Beyond that, of course, working and poor people need to be aware and ready to defend themselves in the wake of the crisis. After all, workers are the victims of this crisis, not its cause, and tightening our belts will do nothing to solve it. So we must explain exactly what did cause this crisis – and show how those same factors will cause the next one too if we don’t change the rules of the game.

The financial pundits try to pin blame for the current meltdown on a few misguided practices or poorly designed incentive structures. Our alternative story line, on the other hand, would emphasize that this conflagration wasn’t a random, isolated negative event. Rather, it was the predictable and preventable outcome of running the world economy in a particular way, according to a particular set of rules. Under the extreme financialization which is a defining characteristic of neoliberalism, economic resources of all kinds (credit, creative talent, and even government subsidies) are channeled into potentially lucrative but ephemeral paper schemes. Real accumulation and productivity play second fiddle to the hyperactive circuits of ‘the paper economy’ – which periodically erupt in enormous, credit-fuelled bubbles. These bubbles attract both profits and public infatuation while they are expanding, but inevitably they burst (and always in a disorderly manner, to paraphrase J.K. Galbraith). Unless and until the rules of this game are changed, we will continue to experience chaos like this every few years. In fact, thanks to globalization and the lightning-quick technology of the financial sector, the crises are coming faster than ever – and deeper, too.
Let’s recount the key defining features of this particular crisis. It started with an enormous expansion of private credit. This credit surge was spurred partly by low interest rates – which in turn were a response to the collapse of the last financial bubble (the dot-com mania of the late 1990s) and to the short US recession that followed the events of 9-11 in 2001. But the deeper cause of this credit surge was the thorough deregulation of the private credit system in the 1990s, led by the US and other Anglo-Saxon countries. This deregulation allowed banks and other financiers to expand credit, whenever and for whatever purpose they desire, no matter how unproductive or poorly rooted in the economic realities of production and productivity. This credit did not, for the most part, finance real employment and production. Indeed, if it had, central banks would soon have stepped in to restrain looming inflation and maintain discipline in labour markets.

Instead, credit growth fuelled another asset bubble, the latest in a series that is as old as capitalism itself. This particular bubble was centred on US real estate – not so much in actual real estate properties, as in the new portfolio of financial derivatives that are linked to real estate (mortgage backed-securities, credit default swaps and other exotic instruments so complex that even their inventors didn’t fully understand them). Fortunes were made for a while: by mortgage lenders offering mortgages to people who couldn’t afford them, by speculators buying low and selling high and, most nefariously, by financial executives who personally pocketed billions of dollars in short-term largesse creamed from the froth of the unreal credit boom they were commanding. As with every speculative exercise, the rush to the party was inevitably followed by a panicked run for the exits on the first sign of trouble (which came, in this case, in the form of rising foreclosures in key US real estate markets in mid-decade). Highly leveraged speculators collapsed, followed closely by the lenders who gave them money to play with, leading to a worldwide financial panic. Indeed, perhaps the most memorable legacy of this epoch of globalization will be the unprecedented speed and synchronicity of this financial collapse. Driven by greed and pressured by competition, financiers around the world (even newly-privatized banks in Iceland) rushed to join the unsustainable party that was going on in US real estate. And they all paid the price.
The resulting financial collapse (which reached its worst moments in September 2008, when the failure of Lehman Brothers set the whole global financial system teetering) spilled into the real economy through various channels (falling construction, battered investor and consumer confidence and falling exports). The outcome was a painful recession (for the US the worst since the 1930s), and the first outright decline in the world’s real GDP since the demobilization after World War II. This decline was another consequence of the unprecedented synchronization of this recession. An enormous and unprecedented government rescue effort (aimed first at saving banks and only later and grudgingly at helping the human victims of the meltdown) succeeded in stabilizing the downturn. But this rescue effort has yet to recreate the conditions for true economic recovery. If anything, the dominant outcome of the stimulus efforts (near-zero interest rates, combined with massive handouts to banks which are still free to do with that money whatever they please) seems to be a recreation of the necessary conditions for the next financial bubble. World stock markets have bounced back by 50 percent or more in the five months since March 2009. Banks and other sophisticated investors are borrowing funds at near-zero interest rates, and then investing into various forms of speculation: rebounding equity and bond markets, the carry trade in cross-border lending, intense speculation in increasingly volatile commodity and foreign exchange markets, and others. The global financial industry is in full-fledged recovery – and executives are once again reaping the fruits of that rebound in the form of enormous compensation gains.

Meanwhile, initial discussions (including among G-20 finance ministers) about the need for renewed financial regulation have fallen completely off the agenda. This reflects both the immense political power of the financial industry (which has vigorously resisted any hint of re-regulation), as well as the natural tendency of policy-makers to simply heave a sigh of relief that things are getting back to ‘normal.’ In financialized, globalized capitalism, ‘normal’ simply means a world which rewards credit-fuelled speculation much more than real work and production.

That’s my thumbnail summary of how this particular crisis unfolded and the damage it did. Understanding these details of the current crisis is one
step in building a stronger political economy consciousness among labour movement activists and leaders (all the more so in light of the grass-roots interest in studying economics that the current crisis has sparked). But we also need to explain why this meltdown is merely the latest, especially painful manifestation of deeper problems in the functioning of capitalism. In other words, this crisis was produced by an underlying set of policies and relationships that will produce and reproduce similar cycles and crises, over and over again, unless and until we address and resolve those fundamental problems and practices. We need to identify and understand the key features behind the pattern of repeated financial crisis (which is so visible in the history of capitalism, and all the more so under neoliberalism):

- Speculative greed: the impulse of those with wealth, to accumulate even more wealth simply by buying low and selling high (rather than producing and selling a real good or service).
- The profit-seeking logic of the private credit system – without which the speculative bubble could never inflate too far.
- Lack of government oversight. Following deregulation, governments have permitted financiers to focus on unproductive and dangerous activities. Indeed, governments subsidise those activities through favourable tax treatment of speculative gains. This was a key pre-condition for the rise (and crash) of the bubble.

Those same three ingredients will cause the next conflagration, if our only response to the collapse of this bubble is to sit back and hope that it re-inflates – with the screws being tightened on working people all the while.

This is serious economics. But we need our partisans and supporters to understand these themes. This means finding better ways to teach and communicate economic concepts. For example, at the Canadian Auto Workers, as part of our own efforts to communicate economic ideas in more accessible and entertaining formats, we developed a four-page cartoon book which explains these 3 common ingredients of financial crisis, but in common-sense terms. The cartoon book concludes by
stressing the need to re-regulate and socialize finance, and channel credit into production rather than speculation.¹

However we impart the knowledge, we need our movements to understand these themes. Without understanding how this particular downturn emerged from features and forces that are ‘hard-wired’ into the DNA of deregulated, financialized capitalism, people will be tempted to see the crisis as a random, negative event – an unfortunate but unavoidable challenge that everyone in society must help to overcome. At best, this leads to the conclusion that we simply need to hunker down and wait out the crisis, hoping that the financial bubble eventually reinflates and things get better. At worst it underpins a willingness to accept the sacrifices and concessions that are being demanded by employers and governments – accepting the false logic that ‘we’re all in this together.’

In the coming tough years, therefore, the labour movement and other progressive forces will need to fight hard against efforts to shift the burden of adjustment from those who caused the crisis, onto the backs of those who are suffering from it. We will do our best to protect workers against lay-offs, cutbacks, concessions, and the many other consequences of the crisis. And with other progressive forces we will fight fiercely in the political arena against regressive shifts in social and economic policies, and cutbacks in public programs, that we know will be threatened in coming years by deficit-laden governments. A crucial part of arming ourselves for those battles is ensuring that our members and supporters understand why this crisis occurred, and why it will happen again, unless we change the whole set of neoliberal economic and social policies we’ve been living under for the last three decades. And this is just one example (an especially important and immediate example) of our ongoing need for an economically literate and confident membership base.

More specifically, how can we undertake that task of enhancing the collective economic literacy and confidence of our movements and our

¹ This cartoon book is available for free download and reproduction http://www.caw.ca/en/7754.htm.
supporters? Many avenues would seem to offer good prospects; there is no shortage of work for us to do.

- Systematic and comprehensive training programs (undertaken by unions, community organizations, or popular educators) to lift up the level of analysis and expertise among key grass-roots leaders and activists, covering all the ground of political economy. For example, in the Australian context, I am aware of one ongoing economics training initiative undertaken by the Australian Manufacturing Workers Union, to upgrade the all-round economic literacy of key officials. My union, the CAW, undertakes similar extensive efforts to train our own activists and leaders.

- Shorter-run initiatives such as one-time courses, lectures, and conferences, organized around more specific topics and themes. Saunders (2009) discusses one successful such initiative, undertaken by the city labour council in Vancouver, Canada.

- The development of progressive media, including print, electronic, and web-based, to disseminate critical coverage of economic events and debates, and to enhance the ability of our activists to engage in debates armed with analysis, facts, and above all confidence. Australia already enjoys several such outlets (one of my favourites is the magazine *Australian Options*, which is both readable and relevant), but we need more: alternative media outlets with more frequency, more reach, and more high-quality economic content. This will take a great deal of effort in all areas (organization, fund-raising, and content development), but it is essential for our partisans to be able to go toe-to-toe with the defenders of the status quo.

- Encouraging progressive economists (in academia or elsewhere) to develop and disseminate popularized, accessible, and immediately relevant materials addressing the needs of our movements for economic literacy and economic campaigning (like non-technical books, commentaries and op-eds, blogs, or easy-to-read annotated bibliographies). In this context I recommend the blog site of Canada’s network of progressive
economists, the Progressive Economics Forum (www.progressive-economics.ca). It is readable, timely, and searchable by topic (making it useful for popular economics training); similar no-frills initiatives could be undertaken in other countries.

- Enhancing the profile of progressive interventions in economic debates. Progressive political economic views should be projected directly into the mainstream of day-to-day economic coverage and discussions, using whatever platforms we can force ourselves onto. We can’t afford to be marginalized from these debates. To do this, we can use our own ‘experts’ (to crack the neoclassical monopoly over the talking-head world of economic punditry). More important is to enhance the capacity of our leaders and activists at all levels to effectively challenge received economic wisdom and put our own world view out there.

All these efforts, and then some, will be required for us to build an economically literate and empowered constellation of progressive movements. By building a stronger understanding of how capitalism actually works, through more extensive economic literacy and political economy training initiatives within our own ranks, our movements can better resist the attacks that are coming. Better yet, we’ll be ready to fight for the fundamental change that we all need, and are all hoping for.

Jim Stanford is economist with the Canadian Auto Workers union in Toronto, Canada, an economics columnist with the ‘Globe and Mail’ newspaper, and author of ‘Economics for Everyone’ (Pluto, 2008) – an alternative economics ‘textbook’ for trade unionists and other activists.

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THE GLOBAL FINANCIAL CRISIS, CREDIT CRUNCHES AND DELEVERAGEING

Steve Keen

Speaking at a conference of Business Economists in December 2008, the Governor of the Reserve Bank of Australia, Glenn Stevens, remarked:

I do not know anyone who predicted this course of events. This should give us cause to reflect on how hard a job it is to make genuinely useful forecasts. What we have seen is truly a ‘tail’ outcome – the kind of outcome that the routine forecasting process never predicts. But it has occurred, it has implications, and so we must reflect on it (Stevens 2008: 7).

The proposition that the crisis was inherently unpredictable is a recurrent theme amongst those charged with preventing such events. It is also a convenient untruth. A Netherlands academic did a rather better survey of the literature than Governor Stevens, to identify 12 economists and market analysts who did foresee this crisis—of whom I was one (Bezemer 2009: Table 1). More importantly, he identified common elements to the analyses that led these researchers to foresee what neoclassical economists in particular failed to anticipate. Bezemer noted that though we came from varied intellectual backgrounds, we shared four common factors:

- a concern with financial assets as distinct from real-sector assets, with the credit flows that finance both forms of wealth, with the debt growth accompanying growth in financial wealth, and with the accounting relation between the financial and real economy (Bezemer 2009: 8).
My own analysis extends Hyman Minsky’s ‘financial instability hypothesis’ (Minsky 1977; Keen 1995), using a theory of monetary dynamics known as Circuit Theory, which originated in Europe (see Graziani 2003). Both perspectives played a key role in helping identify that a crisis was imminent. Minsky emphasised the importance of the debt to GDP ratio as the key indicator of financial fragility; while the Circuit School’s insights enabled the development of a purely monetary model of the economy in which changes in debt play a crucial role in determining the level of aggregate demand.

The debt to GDP ratio—which effectively shows how many years it would take to reduce debt to zero if all of GDP were devoted to debt repayment—has been in danger territory ever since the Stock Market Crash of 1987. As the long term data shown in Figure 1 reveals, Australia’s debt ratio in late 1980s exceeded the deflation-driven peak it reached during the Great Depression.¹

Figure 1: Australian Private Debt to GDP Ratio and Inflation Rate, 1880-2009

¹ The pre-1953 debt to GDP data presented in this article is derived from Reserve Bank of Australia (1999) and Battellino (2007); the post-1953 data comes from the RBA Statistical Bulletin Table D02 (http://www.rba.gov.au). Pre-1950 data on the Consumer Price Index comes from vanplew (1987).
Had central banks around the world not intervened in 1987, it is quite possible that we would have had a mild depression back then—a depression because de-leveraging would have depressed economic activity, and a mild one because inflation would have helped reduce the debt burden. Instead, the rescues encouraged financial institutions across the globe to move from one debt-financed bubble to another, with the consequence that for most of the OECD, private debt has risen substantially faster than GDP for the past 3 decades, as shown in Figure 2 below.

**Figure 2: Debt and GDP Growth in the OECD Countries - Average Annual Percentage Change, 1997-2007**

![Graph showing debt and GDP growth in OECD countries](image)

*Sources: ABS, Thomson Financial and World Bank; compiled by Battellino (2007).*

*Note: Data are from June 1984 for New Zealand, and to December 2006 for Ireland.*
Australia’s overall debt to GDP ratio fell slightly during the recession of the 1990s—from 85 to 79 per cent—as deleveraging by businesses more than offset the increase in mortgage debt from the comparatively low base of 20 per cent of GDP. This deleveraging of business investment is shown in Figure 3. But as Australia’s housing bubble went into overdrive, the mortgage to GDP ratio increased fourfold and the aggregate debt ratio reached 165 per cent of GDP—100 per cent above the level at the end of 1929, and two-thirds higher than the previous record level set in 1892 during the 1890s depression. The unwinding of this huge debt burden, coupled with an inflation rate that is now falling towards zero, will cause a deleveraging-led economic downturn that could rival the Great Depression in severity.

Figure 3: Australian Debt to GDP Ratios, by Sector, 1975-2009
Leverage and Economic Activity

One of the many false assumptions that blinded neoclassical economists to the approaching crisis was the proposition that money has no long-lasting impact on the real economy. In fact, we live in a fundamentally monetary credit-based economy, and in such an economy, aggregate demand is the sum of income plus the change in debt.

When the debt to GDP ratio is small, so too is the contribution that an increase in debt can make to demand, and changes in debt are relatively unimportant. But as debt grows relative to GDP, then even a small change in debt can constitute a major proportion of aggregate demand.

Figure 4, showing the private debt contribution to demand and unemployment, illustrates the rising role of debt in driving demand by showing the correlation between the debt-financed fraction of demand and the rate of unemployment.2

As the private debt to GDP ratio rose from under 50 per cent of GDP back in 1970s to three times that today, the share of aggregate demand that came from an increase in debt rose from as little as 4 per cent in 1972 to as much as 19 per cent in 2007-8.

In the 1950s and 1960s, debt’s contribution to demand had little impact upon changes in unemployment but, from 1975 on, this contribution explained most of the movement in unemployment: when debt-financed spending went up, unemployment went down.3 The economy had become debt-dependent, and the numerous rescues of the financial system by central banks simply extended this period of debt-dependence for another two decades.

This fundamentally monetary contribution to demand was completely ignored by conventional neoclassical economists, yet it was primarily responsible for the illusory prosperity of the last fifteen years.

2 The debt-financed fraction of demand may be defined as the change in debt, divided by the sum of GDP plus the change in debt.
3 The correlation coefficient between the two series since 1990 is -0.94.
Unleveraging by the private sector – reducing the debt to GDP ratio – will soon reduce aggregate demand as it did during the 1990s recession, and drive unemployment up as a result. Given the scale of debt today, at 100 per cent above that of 1929, it could take much more than a decade of unleveraging to reduce debt to levels at which its contribution to economic activity is minor.

That period will be one in which aggregate demand is substantially below GDP, since debt will be reduced by households and businesses spending less than they earn. Growth in GDP will therefore fall below the level needed to sustain the level of employment, adding to the depressing effect of unleveraging.
Can Economic Policy Resolve the Crisis?

Having helped caused this problem by ignoring—and in the US’s case, effectively encouraging—the growth of debt-financed asset bubbles, central banks around the world are now trying to ward off their deleterious effects. All manner of non-conventional policies are being tried—including notably Bernanke’s policy of ‘quantitative easing’ by the Federal Reserve in the USA, which doubled the monetary base in four months during 2008.4

While the Australian central bank has not yet gone this far, the stimuli imparted by the RBA’s 4.25% cut in interest rates in 2008-9 and the Rudd Government’s deficit spending has been enormous. As Rudd’s renowned essay in The Sydney Morning Herald and other Fairfax papers emphasized, the scale of the global monetary and fiscal effort to counter the financial crisis is unprecedented:

On the fiscal front, governments from the world's largest 20 economies are expected to collectively pump about $US5 trillion into their economies by the end of next year (or nearly 8 per cent of global GDP since the crisis began). Altogether, the measures are the equivalent of an extraordinary and unprecedented 18 per cent of global GDP (Rudd 2009).

In Australia, this effort has to date been successful in attenuating the impact of the Global Financial Crisis—though other factors, including Australia’s peculiar position as a developed economy commodity exporter, have also delayed the Antipodean impact of the crisis.

The question remains whether these monetary and fiscal rescues will be sufficient to restore the Australian (and global) economies to their previously customary rates of growth. That is certainly the expectation of neoclassical economists, who are as united in their expectation that the worst is now over as they were previously in their belief that there would be no crisis at all. From my Minskian point of view, their confidence could be well founded under only two conditions, whereby:

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the crisis was solely the result of a ‘credit crunch’ caused mainly by the collapse of subprime lending in the USA; or
• as in all other post-1970 recessions, the debt to GDP ratio could increase after the crisis.

A ‘credit crunch’ can be seen as an interruption to the standard flows of finance when lenders and borrowers suddenly become risk averse. I have developed a dynamic model of a pure credit economy that simulates a credit crunch via a drop in the rate of creation of new credit money, an increase in the rate of repayment of outstanding debts, and a reduction in the turnover rate of bank reserves (see Keen 2009: 13-22 for the technical details). A simple extension of this model allows the simulation of a one-off injection of ‘fiat’ money into this pure credit system.

Figures 5 and 6 (on the following page) show some simulated projections. An injection of an amount equivalent to 3.5% of the aggregate money supply does indeed reduce the severity of the downturn—though the effect is much greater if the money is deposited in debtors’ bank accounts rather than deposited in bank reserves.5

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5 A ‘pulse’ is added externally to the money supply, either via an injection to bank reserves or as a deposit into bank accounts. The former simulates Bernanke’s quantitative easing in the USA; the latter simulates a fiscal stimulus similar to Rudd’s cash handouts to households.
Figure 5: Simulated Money Supply Dynamics in a Credit Crunch with a Government Rescue

Figure 6: Simulated Unemployment Dynamics in a Credit Crunch with a Government Rescue
Thus if the crisis were solely due to an increase in risk aversion, then a government rescue could reduce the severity of the crisis, and a resumption of pre-crisis levels of lending would restore economic activity to its previous level.

However, the current economic crisis is not of this character. With all sectors of the Australian and global economies (except in general governments themselves) carrying unprecedented levels of debt, this crisis was caused not merely by a credit crunch, but also by the unsustainability of economic development that relied upon ever-increasing debt to income ratios. A leverage-led recovery is extremely unlikely—and would only delay the day of reckoning in any case.

The far more likely prognosis, as Prime Minister Rudd acknowledged in his essay, is for a ‘slow and difficult recovery, dominated by deleveraging and deflationary risks’ (Rudd 2009, citing Martin Wolf). Any recovery, therefore, will be in the context of falling debt levels, which in turn implies that aggregate demand will be less than GDP for some substantial time.

This is something that the post-WWII world economies—and current economists—have never experienced. The only precedents are from the deleveraging episodes after the of the 1890s and 1930s depressions. The impact that deleveraging might have today can be estimated from the rate at which deleveraging occurred back then, and the levels to which it fell before stabilizing.

Figure 7 (on the following page) presents relevant data for the earlier historical periods, compared with alternative current scenarios, showing debt as a percentage of GDP.
In the 1890s, Australia’s private debt to GDP ratio peaked at 102%, and then fell at roughly 4% p.a. for 15 years before stabilizing at 40% of GDP. In the 1930s, the ratio peaked at 77% before falling at 3% p.a. until 1939, and then at 12% p.a. during WWII; so that over the entire period from 1930 till 1945 the rate of deleveraging was 8% before debt stabilized at 25% of GDP.

Recovery from the 1890s depression was effectively undertaken in a ‘policy-free’ zone, while the 1930s included everything from active policies (Roosevelt’s ‘New Deal’), through potentially misguided economic ones (Australia’s ‘Premier’s Plan’) and the impact of World War II. We might therefore regard a 4% deleveraging rate as the limit to endogenous debt reduction, and 8% as the policy maximum (this time hopefully avoiding a World War).
Given those parameters, a 4% rate of deleveraging would take until 2028 to reduce the debt ratio to 75% of GDP, while an 8% rate would take until 2018. With aggregate demand as the sum of GDP plus the change in debt, a 4% rate of deleveraging would initially subtract 6% from Australia’s aggregate demand (since private debt is 1.6 times higher than GDP), while an 8% rate of deleveraging would initially subtract 12%. If deleveraging ceased and debt stabilized at the 75% level, then in its last year deleveraging would deduct 3% from aggregate demand at the 4% rate, and 6% at the 8% rate.

This is a drag on economic performance that has not troubled us in past recoveries, when as Figure 1 shows, debt levels rose relative to GDP after each crisis. Since neoclassical economists do not consider the dynamics (or even statics!) of credit, they are ignoring this brake on our future economic performance as they predict a return to stable growth.

**Conclusion**

Marx once famously noted that ‘Men make their own history … not … as they please…, but under circumstances … transmitted from the past.’ He continued that ‘The tradition of all dead generations weighs like a nightmare on the brains of the living’ (Marx 1852: 1). No nightmare weighs more heavily on the economy than debt accumulated in unproductive speculation. Until that burden is addressed any recovery from the global financial crisis is likely to be short-lived and anaemic.

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6 I use 75% of GDP as a reference level because that was the level in 1987 when the stock market crash occurred, and this was almost equivalent to ‘peak debt’ during the Great Depression. Even those who greet unprecedented debt to GDP ratios with the ‘this time is different’ argument should concede that this ratio, which is three times the level that applied in 1945-65, should be at the upper end of the debt levels that the Australian economy can sustain.
Appendix: The Credit Crunch Model

Full details of the model are given in Keen (2009); this Appendix describes the design of its financial component.

The model considers a pure credit economy with three classes – capitalists, workers and bankers – where all transactions occur via bank accounts maintained by the banking sector. The government rescue is then shown as a *deus ex machina* injection of fiat money that can be made into either the banking sectors reserve or to the firm sector's deposit accounts.

Though the model is a superficially foreboding set of differential equations, its financial essence is rather easily understood when the financial flows are laid out in a ‘double-entry book-keeping format’ as shown in the first table below. Each row in the table is a specific financial transaction—accrual of interest, payment of wages, etc.

<table>
<thead>
<tr>
<th>Actions</th>
<th>Reserves (Bₐ)</th>
<th>Loans (Fₐ)</th>
<th>Firms (Fₐ)</th>
<th>Workers (WDₐ)</th>
<th>Banks (Bₐ)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Compound Interest</td>
<td>A</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2 Pay Interest</td>
<td>-B</td>
<td>-B</td>
<td>+B</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3 Deposit Interest</td>
<td>+C</td>
<td></td>
<td></td>
<td>-C</td>
<td></td>
</tr>
<tr>
<td>4 Wages</td>
<td>-D</td>
<td></td>
<td>+D</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5 Worker Interest</td>
<td>+E</td>
<td></td>
<td></td>
<td>-E</td>
<td></td>
</tr>
<tr>
<td>6 Consumption</td>
<td>+F+G</td>
<td>-F</td>
<td>-G</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7 Loan Repayment</td>
<td>+H</td>
<td>-H</td>
<td>-H</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8 Money relending</td>
<td>-I</td>
<td>+I</td>
<td>+I</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9 Money creation</td>
<td>+J</td>
<td></td>
<td></td>
<td>+J</td>
<td></td>
</tr>
<tr>
<td>10 Rescue Banks</td>
<td>+K</td>
<td></td>
<td></td>
<td></td>
<td>+K</td>
</tr>
<tr>
<td>Rescue Firms</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>+K</td>
</tr>
</tbody>
</table>

The actions shown in each row are detailed in the following table:
### Terms

<table>
<thead>
<tr>
<th>Action</th>
<th>Description</th>
<th>Terms</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Compound Interest</td>
<td>Outstanding debt $F_L$ is increased at the rate of interest on loans $r_L$.</td>
<td>$r_L F_L$</td>
</tr>
<tr>
<td>2 Pay Interest</td>
<td>Accrued interest on outstanding debt is paid. This involves a transfer from the firm sector's deposits $F_D$ to the bank sector's income account $B_I$, and the recording of this transfer on the debt ledger $F_L$.</td>
<td>$r_D F_L$</td>
</tr>
<tr>
<td>3 Deposit Interest</td>
<td>Interest is paid (at the lower rate $r_D$) on the balance in the firm sector's deposit account $F_D$.</td>
<td>$(1-s) F_D/\tau_W$</td>
</tr>
<tr>
<td>4 Wages</td>
<td>This is a transfer from the firm sector's deposit accounts to workers' deposit accounts $W_D$, using two insights from Marx: firstly that the surplus in production is distributed between workers and capitalists (in shares that sum to 1 in this model—so workers get $1-s$ and capitalists get $s$); secondly that there is a turnover period ($\tau_S$ as a fraction of a year) between $M$ and $M+$ (see Capital II Chapter 12).</td>
<td>$(1-s) F_D/\tau_W$</td>
</tr>
<tr>
<td>5 Worker Interest</td>
<td>The deposit interest rate times the balance in workers' accounts. $r_D W_D$.</td>
<td>$r_D W_D$</td>
</tr>
<tr>
<td>6 Consumption</td>
<td>This employs the concept of a time lag—the length of time it takes workers to spend their wages is 2 weeks (say) or 1/26th of a year so that $\tau_W$ equals 1/26. Wealthier bankers spend their account balances much more slowly.</td>
<td>$W_D/\tau_W + B_I/\tau_B$</td>
</tr>
<tr>
<td>7 Loan Repayment</td>
<td>The rate of loan repayment is proportional to the outstanding level of loans divided by the time lag $\tau_L$ in loan repayment (for a standard housing loan this would be shown as $\tau_L = 25$).</td>
<td>$F_L/\tau_L$</td>
</tr>
<tr>
<td>8 Money relending</td>
<td>The rate of new money creation is the balance in the banking sector's unlent reserves, divided by a turnover lag representing how rapidly existing money is recycled.</td>
<td>$B_R/\tau_R$</td>
</tr>
<tr>
<td>9 Money creation</td>
<td>The rate of new money creation is the balance in the firm sector's deposit account, divided by a time lag that represents the length of time it takes for the money supply to double.</td>
<td>$F_D/\tau_M$</td>
</tr>
<tr>
<td>10 Rescue Banks</td>
<td>This is a ‘Deus Ex Machina’ injection of 100 currency units one year after the crisis begins, for a period of one year, into either the banking sectors reserves $B_R$ or the firm sector's deposit accounts $F_D$.</td>
<td>100</td>
</tr>
</tbody>
</table>

A model of financial flows is then generated simply by adding up the entries in the columns above, as shown in the table below. This is then attached to a simple model of production in which the rate of change money wages $(W)$ depend on the rate of employment $(L/N)$ via a
‘Phillips Curve’, output (Q) is labour (L) times labour productivity (a), and both population (N) and labour productivity grow at constant rates.

<table>
<thead>
<tr>
<th>Rate of change of...</th>
<th>Equals...</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank Reserves BR</td>
<td>H-I+K</td>
</tr>
<tr>
<td>Firm Loans FL</td>
<td>-H+I+J</td>
</tr>
<tr>
<td>Firm Deposits FD</td>
<td>-B+C+D+F+G-H+I+J+K</td>
</tr>
<tr>
<td>Worker Deposits WD</td>
<td>D+E+F</td>
</tr>
<tr>
<td>Bank Income BI</td>
<td>+B-C-E-G</td>
</tr>
</tbody>
</table>

The model is easily simulated in any modern mathematics program (like Mathcad or Matlab) but this kind of work is beyond the capabilities of spreadsheets like Excel.

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The current economic crisis has been the deepest in world capitalism since the 1930s, a fact now acknowledged by scores of mainstream commentators. This article provide an overview of the extent of the crisis by reference to data on trade, output, the stock markets, job losses and unemployment, making comparisons both with the Great Depression and other post-1945 recessions. It also considers the evidence for a bottoming-out in the economic freefall in the second quarter of 2009, as well as the reasons for it. The bulk of the article, however, is devoted to an examination of structural contradictions that persist in the world economy and which have either been exacerbated by the measures taken to halt the freefall or which have only temporarily been ameliorated. These factors include the accumulation of vast financial sector debt that has not been seriously tackled nor its dimensions understood, endemic excess capacity in the world economy, unsustainable public debt and stimulus packages, and a series of contradictions in the Chinese economy. The article concludes with an assessment of the prospects for the world economy.

Dimensions of the Crisis

Figures 1-3 demonstrate that, for at least the first 12 months of the current crisis, the downturn tracked or was significantly worse than the Great Depression in terms of world industrial production, world trade and the stock markets. Figure 4 provides data on the drop in GDP in the G7 nations, with output falling by anywhere up to 7%, equivalent to
hundreds of billions of dollars. In the first quarter (Q1) of 2009 business investment in the US fell at an annualised rate of 40%.

Figures 1 and 2: World Industrial Production and Volume of World Trade, Great Depression vs. Today.

Source: Eichengreen & O’Rourke (2009)

1 Note all $ figures in this article are US dollars.
Figure 3: World Stock Markets, Great Depression vs. Today.

Source: Eichengreen & O’Rourke (2009)

Figure 4: Year on Year Change in GDP Q2 2009 (%)

Source: OECD Statistical Extracts
A driving factor in the crisis has been the meltdown in world trade, as shown in Figure 5. Whether in the traditional core of the world system in the USA and Europe or in the so-called BRICs (Brazil, Russia, India, China), which were meant to save the system in the event of a crash in the core, imports fell by anything from 15% to nearly 45% in the year to the second quarter (Q2) of 2009, as shown in Figure 5. Deflation set in: prices fell across the G7 by 2.4% between Q3 2008 and Q1 2009 and in the US by 3.3%.

**Figure 5: Year on Year Change in Imports Q2 2009 (%)**

Source: OECD Statistical Extracts

The implications for the working class have been severe. With US government spending at 20% of GDP, as against 5% of GDP in the early 1930s, and the figure higher still in Western Europe, there is an automatic buffer against the kind of collapse in employment that we saw
in the ‘thirties.\footnote{Five per cent of all US jobs had disappeared by August 2009 when compared to November 2007. In the three years 1930, 1931 and 1932, net job losses as a proportion of total employment were 4.8%, 6.5% and 7.1% respectively (Schiller, 2009).} Nonetheless, the situation is still dire: more than 18 months after large scale retrenchments began in December 2007, the scale of sackings in the USA has been significantly worse than in any other recession since 1945. More than seven million jobs have gone, as shown in Figure 6. By May 2009, the number of jobs in manufacturing in the developed world was down by 12% on a year previously (ILO, 2009a).

Figure 6: Job Losses in Recent Recessions as a Share of Employment

Across the developed world as a whole, unemployment was 46% higher in April 2009 than a year previously (ILO, 2009a). Sixteen million are
now unemployed in the US, and one in three have been out of work for six months or more. Another 22 million are jobless in the EU. Unemployment rates are rising steadily, as shown in Figure 7: in the Eurozone unemployment stands at 9.5% and is forecast to rise to 11% in 2010 (Jolly, 2009). In the Baltic States, which were regarded as economic miracles for most of this decade, GDP collapsed by 20% in the year to Q2 2009 and unemployment rose to 16-18% (Staehr, 2009). Unemployment has hit the young in particular: unemployment amongst teenagers in the USA now stands at 25% and at 18% amongst young workers aged 18-24 in the EU. Elsewhere, unemployment in Russia soared by two million between May 2008 and January 2009 (ILO, 2009b). Half of the unemployed across the OECD, and 80% globally, receive no jobless benefits (ILO, 2009b).

**Figure 7: Unemployment Rates (%)**

Source: OECD Statistical Extracts
If underemployment is added, the US total of workers either out of work or forced to work part-time for lack of full-time jobs was 17.0% in September 2009, up from 10.9% one year earlier (Bureau of Labor Statistics, 2009). Underemployment was on the rise across the G7 even before the onset of the crisis; the rate of increase has now speeded up. Half a million British workers are temping because they cannot find permanent jobs and one million are doing part time work because they cannot find full time jobs (Hyland, 2009). Others have simply dropped out of the labour market - participation rates are down everywhere.

Even amongst those still working full time, weekly hours and overtime have been cut back. Average weekly hours in the US private sector are at the lowest since 1964 (RGE Monitor, 2009). Total hours worked by production workers in US manufacturing fell by 16% in the year to August 2009 and are now 25% lower than in 2002 (Bureau of Labor Statistics, 2009). In Asia, working hours have been reduced across the board.

Employers are using the whip of unemployment to drive down wages and conditions. The Director General of the ILO reported in June 2009 that:

Freely negotiated collective agreements are no longer respected, and workers have to concede hard won wage levels and benefits in order to retain any credible prospects of future employment and income. The risk of clandestine labour or illegal child labour as cheap alternatives is growing in many countries, as is the recourse to forced or compulsory labor (ILO, 2009b).

In the USA the effect of a 2.5 per cent rise in hourly wage rates in the year to September 2009 was more than wiped out by shorter hours and inflation (Bureau of Labor Statistics, 2009). Hundreds of thousands of workers have experienced severe wage cuts. General Motors paved the way when it negotiated a contract with the UAW in 2007 to allow all newly hired workers to start work at half the going rate for established workers. The auto industry, the pioneer of high rates of pay for US blue collar workers, is now dragging wages down. One third of all US employers plan to introduce similar two-tier contracts when current
contracts expire (Bureau of National Affairs, 2008). The US is re-positioning itself as a low-wage economy after decades when manufacturing wages in the unionised sector were the envy of blue-collar workers around the world. All the while, US employers are pushing workers harder: labour productivity rose in the second quarter of 2009 at an annualised rate of 6.4%, as labour costs fell at 5.8% (Healy, 2009).

With unemployment on the rise, the 2008 US Census records that median household incomes fell sharply, by 3.6%, last year (Leonhardt, 2009). Household incomes are predicted to decline even more in 2009 given the further increases in unemployment during the year and are now lower than they were a decade ago. Such a decline has not occurred since the 1930s. *New York Times* journalist David Leonhardt points to the causes:

One, economic growth in the current decade has been lower than in any decade since before World War II. Two, inequality has risen sharply, so much of the bounty from our growth has gone to a relatively small slice of the population’ (Leonhardt, 2009).

Forty million Americans now live below the meagre poverty line of $22,025 for a family of four (Eckholm, 2009).

Along with capitalists in the private sector, the IMF and governments all over the world are intensifying the pressure. It was the Obama administration that insisted on wage cuts in the auto industry as a condition for the bailout earlier this year. In February the Irish government increased the pension levy paid by workers by 7%. The IMF, dominated by the governments of the major imperialist powers, is using the crisis to squeeze the weaker developed countries. The Latvian government, for example, was required to cut public sector wages by 10% in 2008 and is scheduled to cut them by another 20% as a condition of an IMF loan (Taylor, 2009). The Hungarian government, likewise, has cut pensions, social benefits and public sector wages on the orders of the IMF. The Icelandic government is slashing public spending in order to repay money loaned by the British and Dutch governments to bail out the bankrupt Icelandic banks which went under last year with debts equivalent to one-half of the country’s entire GDP.
The crisis is having a devastating impact on many parts of the developing world as well. The Asian Development Bank reported in July that developing Asia is ‘experiencing a precipitous drop in foreign direct investment’ (Gittins, 2009). The crisis shut down export markets for raw materials and manufactured goods. The ILO noted in June that ‘[t]ens of millions of young people are about to leave school and enter a depressed labour market. A lack of decent work opportunities at an early age may permanently compromise the future employment prospects of youth’ (ILO, 2009b).

The crisis is also leading to a sharp reduction in remittances by the world’s estimated 200 million migrant workers. The World Bank estimates conservatively that migrant remittances, which are worth approximately $300bn and make a major contribution to poor families, will fall by more than 7% in 2009 as migrant workers are thrown out of their jobs and sent home. Foreign aid by OECD governments has been cut. This, on top of the food price inflation that occurred in the first half of 2008, has seen living standards squeezed for tens of millions. Food prices traded by commodity markets fell sharply in the first half of 2009 but prices in the shops have remained at record highs. As a result, the UN estimates that the number of hungry around the world will rise by more than 85 million to one billion in 2009 (White, 2009).

A (Temporary?) End to the Freefall

In January and February 2009 the first mention of ‘green shoots’ began to appear from the mouths of leading government figures in the UK and USA. At the time this was no more than wishful thinking: GDP in Q1 2009 fell by as much as in the previous quarter as the world economy continued to plummet. However, by June economic data began to suggest that the freefall was indeed ending, and by August the talk was of a ‘recovery’ under way. Figures 1, 2, 3 and 8 demonstrate the basis for this optimism. After two quarters of sharp retreat, the rate of decline in GDP in the G7 economies slowed down, with positive growth recorded in France, Germany and Japan. China, which appeared to be slumping to only 6% growth in the first quarter (well below the rate required to keep unemployment from increasing sharply), was back on track to 8% by

**Figure 8: Quarterly Change in GDP (%)**

Other indicators confirm the appearance of some feeble ‘green shoots’ during 2009. For example, the various international Purchasing Managers Indices, which measure current manufacturing activity and which had fallen to the low 30s in December 2008, had recovered by August to the low 50s (50 indicating the break point between contraction and expansion): this was the highest level for between 16 months and two years. Similarly, the OECD’s Composite Leading Indicators bottomed out in March 2009 and began pointing towards recovery (OECD, 2009a). House prices in the US edged upwards in June and July, albeit to a level still 15% lower than a year earlier (Standard and Poor’s 2009). After months when every successive prediction for growth and every report on past results was being downgraded, predictions for 2010 are now being modestly upgraded.

Three things have been responsible for an end to the freefall since April 2009. The first was the easing of the world’s credit markets due to the
government guarantees (i.e. open taxpayer-funded cheques) given to the banks over the northern winter. The US alone has shored up the big banks with $250bn in taxpayer funds since late 2008. US economist Joel Geier suggests that the total of bank subsidies, loans, credits and guarantees by the US Government amounted to $13 trillion (Geier, 2009). The result was that the banks regained confidence that money lent to other banks would not evaporate, and credit began to flow again, albeit by no means as freely as before.

The second factor has been the massive stimulus packages by the USA, Japan, China and the European Union. The USA has thrown in a stimulus package of $787bn, China, about one third of the size of the US economy, has devoted more than $585bn to boosting spending and infrastructure, Japan, $270bn, and the EU, $290bn. Across 50 countries, stimulus packages totaling $3 trillion have been unleashed. In the Great Depression, the budget deficit averaged across the 24 largest economies was less than 4% of GDP. In the USA and the UK in 2009, thanks to stimulus packages, it was 12%. The effect of the government stimulus packages was boosted by lower oil prices and lower mortgage rates. All over the world big government is back in favour as the ‘market solutions’ beloved of the neoliberals are quietly pushed into the background. Production in the auto industry began to recover in the northern summer of 2009 with the ‘cash for clunkers’ deals by American and German governments.

The third factor responsible for an end to the freefall was the decision by the major central banks to print money and reduce interest rates to virtually zero in late 2008. Again this is in sharp contrast to their reaction in the Great Depression when the central bank rate in the major economies never fell below 3%. This time around, money supply expanded rapidly, whereas in the Depression money supply collapsed. Aggressive and semi-coordinated action by governments around the world has therefore halted the catastrophic drop in all the major indicators experienced in the northern winter of 2008-09. This has not, however, ended the crisis. These measures are essentially unsustainable and in the long term only create their own problems.
A Systemic Crisis

We are currently experiencing a systemic crisis in the world economy and there is little prospect of sustained economic growth returning to the world economy in the next few years. The more sober-minded mainstream commentators recognise the depth of the crisis and the fragile character of the ‘green shoots’. The United Nations Conference on Trade and Development argued in September 2009 that ‘The likelihood of a recovery in the major developed countries that would be strong enough to bring the world economy back to its pre-crisis growth path in the coming years is quite low.’ (UNCTAD, 2009: i). US Treasury Secretary Timothy Geithner told the US Congressional Oversight Panel in the same month that ‘[w]e still have a long way to go before true recovery takes hold’ and pointed to ‘substantial headwinds’ from the financial sector because of foreclosures continuing at an ‘aggressive pace for some time’ (Crittenden, 2009). The Wall Street Journal in August 2009 referred to ‘a barrage of negative reports’ in the middle of that month amidst all the hyperbole about the recovery in the stock market: ‘personal bankruptcies surged 34% in June compared with last year, the number of homes subjected to foreclosure proceedings rose 32% as against a year ago; the number of people out of work for 27 weeks or longer reached a record 5 million; and retail sales dipped in July’ (Wall Street Journal, 17 August 2009).

A series of factors continue to weigh on the system, some of which have their origins in the factors that brought on the freefall in the northern winter of 2008-09, and some which arise from the very measures that were taken to arrest the collapse.

Mountains of Financial Sector Debt

The main means by which capitalism resolves its crises is by destruction of capital through recessions and wars. Since 1945, however, governments have been reluctant to allow the clearing-out process to

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3 The treatment of crisis that follows in this section and the next rests on an analysis set out by Harman (2009), Chapters 8 and 9.
work its way through for fear of multiple collapses following the failure of one or two large companies. The result was that the crises of the postwar decades were shallower but also that the recoveries were also not as rapid or large. In the past 10 years the situation has changed a little as the US government has allowed some large companies to go bust (e.g. Enron, WorldCom, and now Lehman Brothers) but the experience of the last was that the costs were simply not worth it. The entire financial system threatened to melt down as banks refused to lend for fear that their debtor too would go out of business. In order to tackle the credit crunch, the US Government injected billions of dollars to bail out the banking system. However, although huge quantities of capital, both fictitious and real, have been wiped out in the current crisis, including the bankruptcies of some giants of corporate America such as GM and Chrysler, the destruction has been insufficient to allow the system to fully rebound.

The IMF estimates that total write-downs in the global banking system amount to $3.4 trillion (IMF, 2009). Less than half of this has so far been accounted for and dealt with. As the losses are gradually unwound, prudential regulations require banks to cut their lending by ten times the amount of the losses revealed – a deleveraging process of up to $34 trillion. The banks have only just started down this road.

Uncertainty about the exact extent of accumulated write-downs means that the sheer extent of potential bank defaults is shrouded in mystery. In August the US Congressional Oversight Panel declared that ‘[i]t is impossible to resolve the argument about whether banks are or are not solvent because of the uncertain value of their loans’ (O’Connor, 2009). Early in 2009, fearing further collapses in the banks, President Obama allowed US banks to revalue their ‘assets’ (the various toxic debts, the derivatives and so forth that precipitated the crisis in the first place) to their original ‘book price’ rather than their likely price if sold presently on the open market (‘mark to market’). This has allowed US banks to report a return to solvency. This suits US banks and the US Government but in the long term prevents a full resolution of the crisis that might accompany the kind of wholesale write-down of assets necessary for a reboot of the US financial system.
While the major US banks were bailed out with virtually unlimited funds from the US government earlier in the year, the US banking system as a whole was in a worse state in Q2 than Q1 as banks were hit by a sluggish economy and rising unemployment (Morgenson, 2009). The US housing crisis which sparked the financial crash is still in play. Sub-prime mortgages are faring worse than they were a year ago: 40% are now overdue (Timiraos, 2009). Delinquency rates on prime mortgages, the ‘gold standard’ of the US banking system, have risen from 5.3% to 9% (Timiraos, 2009). Further weighing down the market is the increasing proportion of mortgage holders stuck with ‘negative equity’, that is, they owe more on their mortgage than their house is worth. The figure is already one quarter of the total and is predicted by the Deutsche Bank to rise to one half by 2011 (Pethokoukis, 2009). With no end to the sackings in sight in the US, the housing market is not likely to recover quickly. Thus the banking system will continue to be bogged down with bad debts.

Speculation is rife that there may be a second round of financial failures in the US sparked off by a collapse in commercial real estate (Pristin, 2009). The IMF estimates loss rates of 27% on commercial mortgage securities in the USA, UK and Europe (IMF, 2009). Building values have fallen as much as 50% around the USA and there are dire predictions for refinancing commercial mortgages (Pristin, 2009). Unrealised losses on their holdings of commercial real estate are a deadweight on the banks’ balance books and further hinder their preparedness to lend. Bank credit, generally, is in sharp retreat.

The situation is worse again in Europe where banks have double the leverage of the USA. European banks still need to raise about $380 billion to right their books (IMF, 2009). Bank write-downs in the UK amount to $604bn, of which only one third has thus far been taken (IMF, 2009). Banks in Austria and Sweden are taking heavy hits because of investments in Eastern Europe. During the boom years of 2002-06 Eastern European businesses and householders took out loans denominated in Euros to take advantage of lower interest rates. With the rise of the Euro and the collapse of their own currencies during the current crisis, the repayments are crippling them. Further defaults are likely, threatening a chain reaction in the Western European banking
The flood of foreign investment into Eastern Europe in 2007 and 2008 has now turned into a flight as banks and investors try to get their money out.

**Endemic Excess Capacity in the World Economy**

Although the rate of profit is higher in the major economies than during the 1970s, it is still insufficient to prompt the revival of capital accumulation (Brenner, 2009; Harman, 2009: 195-201; 231-38). This is significant because it exacerbates another systemic problem in the advanced economies, excess capacity. Traditionally, the gap between production and working class consumption is met by business investment. However, business will not invest where the rate of profit is inadequate for its needs. Robert Brenner records that capital accumulation in the major Western economies has been successively lower in every decade since the 1960s (Brenner, 2006: 282). With no sustained recovery in profitability in sight, the capitalists are not going to gamble on investing in production of new goods for sale onto glutted markets. Lower rates of capital accumulation may restrain the rise in the organic composition of capital, and therefore slow down the tendency for the rate of profit to fall, but they do nothing to solve the problem of excess capacity and only hold back long term growth in productivity. In Japan, where excess capacity has been most obvious, the economy stagnated for 14 years, the so-called ‘lost decade’. With the onset of a fresh crisis, the problem of excess capacity in the advanced economies has become more urgent. Manufacturing in the EU and USA is now operating at 70% capacity. In addition, bank lending to business for investment is constrained by the banks’ own underlying solvency problems and the weight of toxic assets on their books.

If business will not step into the breach of inadequate effective demand by expanding investment, what of working class consumption? Here the capitalists are stuck with an inherent contradiction. Governments around the world would like households to spend up to reflate their economies. This is particularly important in the USA where consumption accounts for 70% of the total economy. However, at the same time governments are using the crisis to attack working class wages and living standards.
Working class spending will not be able to contribute to any resolution of the crisis in the short term when workers are on short hours, facing retrenchment, unemployed, suffering negative equity on their homes, or staring at default on their mortgages. Between Q2 2007 and Q1 2009, household net worth in the US fell by 22% (Zimmerman and Murray, 2009). In Q2 2009, net worth rose by 3.8% on the back of a surge in stock prices, but this is not likely to affect the spending plans of working class households (Associated Press, 2009). The result is obvious in the retail sector where sales in July 2009 were 8.3% lower compared to a year previously. Saving and reducing debt is now the priority for US consumers, not spending, even if this holds back economic recovery – the so-called paradox of thrift.

European workers now face the same situation experienced by US workers for the past 30 years: declining real wages as the jobs crisis begins to hit home. In Europe (Germany, France, Belgium and Holland), the rise in unemployment has been delayed by short-time working and government subsidies to cover part of the wages of workers in hard-hit companies. In April 2009, two million German workers were on short-time. Hundreds of thousands of workers have avoided retrenchments due to such arrangements, and this has maintained working class consumer spending. However, government subsidies will run out in 2010, and economists predict that unemployment in Germany will soar from its current 3.5 million (8.3%) to 4.4 million (more than 10%), when this occurs (Taylor, 2009). Wolfgang Franz, the chairman of Chancellor Merkel’s panel of independent economic advisers, told reporters in September 2009 ‘As much as it hurts me to say it, the worst is yet to come for the labor market’ (Anon, 2009a).

In the UK, unemployment is forecast to rise from its current 2.4 million to 3 million by the end of 2009, figures last seen during the early Thatcher years. The chief economist of the Chartered Institute of Personnel and Development in the UK said in August that ‘it was far too soon to rule out another avalanche of private sector redundancies later in the year’ (Hyland, 2009). In France, where the economy has not plunged as far as its neighbours, this fact did not protect workers’ jobs as unemployment rose from 8.9% in Q1 to 9.5% in Q2 2009. Japanese workers, too, face similar pressures. In July 2009, unemployment
reached a record high of 5.7% and average household spending in that month was 2% lower than a year previously (Anon, 2009b). The handouts which were part of many stimulus packages gave a temporary shot in the arm to household spending but the amounts involved were woefully insufficient. Governments rescued the banks but turned a blind eye to the hardship of the working class.

A third possible source of effective demand is world trade. However, with world trade likely to fall by 10% in 2009, there is little potential that the developed countries can reflate on the basis of surging exports. With the US consumers snapping their wallets shut, the Asian economies, which recovered from the ‘Asian crisis’ of 1997-98 by exporting vast quantities of goods to the USA, will also likely remain subdued.

Unsustainable Public Debt and Stimulus Packages

The inability of business, households or world trade to significantly boost demand at present means that government spending is still playing a major role in preventing the freefall from resuming. This fact lies behind the decision of the meeting of the G20 leaders in September 2009 to maintain the stimulus packages. Pressure from the German and French governments to begin to wind back the stimulus was successfully resisted by the British and American governments well aware that the stock market surge of mid 2009 and apparent stabilization of the financial system were dependent on governments keeping a floor under demand and being ready to step in to prop up banks in difficulty. Any withdrawal of the stimulus would threaten to reveal the underlying lack of solvency amongst hundreds of British and US banks.

Nonetheless, the continued use of the stimulus packages has consequences – they are draining the government purse at an alarming rate. Public debt as a share of GDP in the OECD is forecast to rise from 73% in 2007 to 100% in 2010 (OECD, 2009b). In the US the debt will rise from 63% to 98%, in the Euro area from 71% to 89%, and in the UK from 47% to 89%. Japan, where debt already soared from 64% of GDP in 1991 to 167% in 2007, faces the most significant dangers as its public debt is now forecast to rise to 200% of GDP by 2010 (OECD, 2009b).
The amounts involved are staggering. US debt in early 2009 stood at $11 trillion: by 2020 it is forecast to rise by another $9 trillion to $20 trillion.

A series of problems arise from the escalation of US public debt. First, the spectre of a major financial crunch in the US if overseas governments and financial institutions decide to stop amassing US dollar securities. While such precipitate action is unlikely, short of a viable and stable alternative to the dollar emerging, foreign creditors are likely to demand higher interest rates over time to offset the gradual depreciation of the US dollar that has taken place through 2009. Upward pressure on interest rates may in turn choke off any early recovery as it will exacerbate the housing crisis and prevent any recovery in business investment. The interest bill alone on the debt will eat up an ever increasing proportion of US government funds. A rise in the US debt of $9 trillion, with higher interest payable down the track in the order of 5%, means that the interest bill on the US debt alone will rise by $450bn, equivalent to about 3% of GDP. In other words, the US government will have to find another 3% of GDP simply to pay off the additional interest.

Over time, the continuous accumulation of debt and decline in the value of the dollar threatens the US role as the centre of the world financial system and the US dollar as the reserve currency. And while the USA may be able to sustain a gigantic debt, such is the global appetite for US dollar assets, the same is not true of any other government. Governments around the world are therefore under pressure to wind back the stimulus packages. That will mean an immense scaling-back in budget spending or tax hikes.

While most sober-minded capitalists and think tanks advise the continuation of high government spending for the foreseeable future, they are all agreed that governments around the world will need to axe social spending down the track. There has been a long-term propaganda campaign by Western capitalist classes about the alleged unsustainability of current systems of pensions and public healthcare. Even before the crisis, US Democrats and Republicans alike were arguing that Medicaid, Medicare and social security (retiree pensions in particular) had to be wound back. President Obama has announced his intention to reduce the budget deficit to no more than 3% within five to ten years, while the Republicans have already announced a plan to cut spending by $75bn a
year. The re-elected Merkel Government in Germany is threatening severe reductions to government spending, as have both the British Labour and Conservative parties should they win the 2010 general election.

However, winding back public spending presents its own problems. Undertaken quickly and brutally it could spark a fresh collapse as the private sector is incapable of filling the gap left by the withdrawal of Government outlays. Governments are therefore caught in a painful dilemma for which there is no obvious solution.

Contradictions in the Chinese Economy

With the USA, EU and Japan both having fallen into a deep hole in the northern winter of 2008-09 and showing few signs of any substantial real growth since touching bottom, the world’s hopes have rested on China to pull the rest of the world out of recession. This is an unlikely outcome. Understanding why means coming to grips with the key components of the Chinese growth of recent decades.\(^4\)

Chinese growth since the early 1980s has been built on its (until recently) unstoppable export machine. Exports have risen from 20% of GDP in 1997 to 40% today. Domestic consumption, by contrast, is only 35-40%. China’s ‘economic miracle’ has been built by suppressing working class consumption and encouraging very high savings rates.\(^5\) Workers’ savings deposited in the banking system have furnished a large pool of investible funds for the development of export-related infrastructure. Investment as a proportion of Chinese GDP is about 40%, as against 10-20% generally in the OECD countries.

Keeping a lid on wages through direct repression of trade unions has the added advantage of attracting foreign manufacturers eager to set up

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\(^4\) The following analysis of the Chinese economy from boom to bust to recovery draws extensively from Whitehouse (2009).

\(^5\) With the withdrawal of state-provided healthcare, education and pensions and permanent jobs (the ‘iron rice bowl’) since the early 1980s, Chinese workers now save nearly half of their incomes to prepare for sickness, unemployment and retirement and to pay for their children’s education (Whitehouse, 2009: 29).
operations in what has become the new workshop of the world. Low wages have also reduced demand for imports, enabling the Chinese government to amass huge trade surpluses. State control of the banks and industrial enterprises has allowed the government to stimulate or cool down the economy by manipulating lending and investment more effectively than is possible in the OECD.

Left unchecked, China’s export success and enormous trade surpluses would have driven up the yuan and made exports more expensive and imports cheaper. In order to protect the interests of the export-driven economy, the Chinese central bank has bought large quantities of US dollar-denominated assets and printed money to prevent a rapid appreciation of the yuan. The Chinese government now holds $776bn in US Treasury securities and more than $2 trillion in foreign currency reserves in total. The fact that the Chinese government has been willing to hold US debts in US dollars has allowed the Federal Reserve to keep domestic interest rates low and thereby contributed to the further expansion of exports to the US market.

China’s rapid economic growth gave rise to speculative fever. In 2005-07, there was a rapid rise in the Shanghai stock exchange and the real estate market as newly wealthy enterprises and billionaires splashed their cash. The Shanghai stock market shot up five-fold from mid 2005 until October 2007. House prices followed a similar trend, rising fast through 2006-07. Investment also poured into export industries and export-related infrastructure – roads, ports, airports and so forth. The result in China, as elsewhere in the world economy, was the development of massive excess capacity. Even before the crash, when US demand for Chinese goods was running hot, 75% of Chinese industries were plagued with excess capacity. The Chinese auto industry was capable of turning out twice as many cars as could be absorbed (Bello, 2009).

In late 2007 the stock market bubble burst – the Shanghai exchange fell by 65% over the next 12 months. The property market boom came to earth in early 2008 with house prices forecast to fall by anything between 10% and 30% before the bottom is reached. The construction sector was crippled, and ten million construction workers lost their jobs in 2008 (Whitehouse, 2009). The downturn in world trade in the second half of
2008 was therefore only another heavy blow to an economy that was already staggering. China’s export industries fell sharply.

The Chinese government responded quickly in November 2008 with a massive 4 trillion yuan stimulus package which had two elements. One was large-scale government handouts and subsidies to small business to lift domestic consumption in order to provide a market for Chinese businesses. This was largely successful - retail sales were 15% higher in July 2009 than a year previously (Reuters, 2009a). The second was the release of a flood of credit by the state-owned banks to the construction industry for infrastructure development. Investment in urban areas in fixed assets such as roads, rail lines, canals, airports and power plants in the first half of 2009 was up 33% on a year previously (Reuters, 2009a). These initiatives have re-started Chinese industry and growth is back on track for 8% per annum. They have also underpinned strong demand for raw materials and minerals which have helped stave off the worst of the crisis in Australia.

Several contradictions remain, however. First, there are real limits to the degree to which domestic consumption in China can continue to be raised. Government handouts serve a useful purpose in stimulating consumption but, vast though the Chinese government reserves are, the handouts cannot go on forever. The stimulus packages will be exhausted at some stage. Further, the Chinese government is loathe to allow wages to rise significantly. Rising wages in the mid-2000s led to increasing anxiety amongst both local and foreign investors and a preparedness to shift investments to countries with still-lower wages such as Vietnam. Any sustained shift towards an economy based on higher domestic consumption – aside from short-term boosts from state stimuli – is going to be constrained by the fact that higher wages would begin to price Chinese workers out of world markets, assuming there is no significant lift in the skills of the Chinese workforce in the interim. Thus, the kind of structural shift away from a reliance on exports towards domestic consumption is limited by a countervailing force – a tendency by business to shift offshore – that will slow down such a shift. A concern to keep a lid on wages in the context of the crisis is evident in the decisions by the Chinese government in 2008 to rescind a lift in minimum wages
and to defer improvements in labour standards foreshadowed by 2007 labour legislation.

Short of a big surge in strikes capable of pushing up wages substantially, therefore, the Chinese economy is not going to drive the world economy out of its slump. It can help: modest growth in the French, German and Asian economies in Q2 2009 was underpinned by rising exports to China (up by 6.3% in Q2). However, it is nowhere near enough: the Chinese economy is only one-third the size of the US, and the consumer market in the US stands at $9.5 trillion as against only $1.5 trillion in China (Batson, 2009). It is the US consumer market that still matters for any expansion of world trade and that is going to be subdued for the indefinite future.

A second significant contradiction in the Chinese economy is that infrastructure development is only exacerbating excess capacity in world and domestic manufacturing. Jobs in construction have bounced back and industrial output was up 12.3% in August 2009 compared to a year previously (Reuters, 2009b). However, most of the expansion is still aimed at the export sector. And, with domestic consumption limited by the factors discussed above, and with exports hemmed in by depressed markets in the USA and Europe, expansion of Chinese export capacity is simply contributing to further excess capacity in world markets and at home. Despite the surge in domestic spending in the first half of 2009 on the back of the stimulus package, the Chinese steel industry was still operating at only 71% capacity in Q2 2009 (Whitehouse, 2009: 30).

The Chinese government’s determination to maintain stimulus to the export sector will do nothing to alleviate tension in the world trading system. The tyre industry provides a case study. Between 2004 and 2008 Chinese tyre production capacity rose by 152% and is forecast to rise by another 16% by the end of 2010 (Weisman, 2009). Capacity now far exceeds the ability of the domestic economy to absorb it by a ratio of three to one. The result is that Chinese tyre producers have flooded world markets, with US imports rising from 14.6 million tyres in 2004 to 46 million in 2008 (Weisman, 2009). Under pressure from the United Steelworkers union the Obama administration slapped a 35% tariff on imported Chinese tyres in September. Such initiatives only raise the potential for retaliation.
Third, with the resumption of growth in China, billions of yuan poured back into the share market in the first half of 2009 as Chinese investors looked for quick returns. The Shanghai stock exchange, having plunged in 2008, rose by nearly 80% in the first seven months of the year. In August 2009, however, the stock exchange fell back by 20% before steadying. Speculation, underwritten by bank loans, shifted to property. If property prices tumble, therefore, the heavily leveraged Chinese banks are in big trouble. A prominent Chinese economist wrote in August that the Chinese stock and properties markets were over-valued by 50-100% and were like ‘a giant Ponzi scheme’ (Chan, 2009).

Further adding to anxiety about the Chinese economy is concern about the integrity of Chinese economic data (Chan, 2009). Simply put, they are subject to extraordinary manipulation. Perhaps even more than the US, the Chinese government has little interest in revealing the true value of assets that Chinese business corporations have accumulated through speculation because the politicians are frequently executives on the relevant boards and have grown rich from the process. Second, provincial premiers frequently report quite unrealistic growth figures to the central government in order to curry favour and promote their own careers. Thus, China reported growth in industrial production of 7.9% in Q2 2009 compared to a year earlier. However, exports were down 22%, power generation dropped by 2.2% and oil demand fell by 3.5%, suggesting that this growth figure is almost certainly exaggerated (Chan, 2009).

A series of economic and political factors therefore limit any potential for China to act as the new locomotive for the world economy.

**Summary and Prospects**

The fragile ‘green shoots’ that have appeared in the northern summer of 2009 are no indication that the world economy has escaped the crisis into which it fell in the latter half of 2008. In early September 2009, the UN Conference on Trade and Development attacked the ‘green shoots’ hypothesis head on. It is worth quoting at length:
But the real economic winter is far from over; tumbling profits in the real economy, previous overinvestment in real estate and rising unemployment will continue to constrain private consumption and investment for the foreseeable future. As the crisis is global, reliance on exports offers no easy way out, since trade is expected to decline by about 11% in real terms and any new trade expansion requires a recovery of consumption and investment somewhere in the world. Given the weakness in macroeconomic fundamentals, an upturn in financial indicators in the first half of 2009 is more likely to signal a temporary rebound from abnormally low levels of prices of financial assets and commodities following a downward overshooting that was as irrational as the previously bullish exuberance. They are not a reflection of strengthened macroeconomic fundamentals but of a restored ‘risk appetite’ among financial agents. Consequently, they could be reversed at short notice, depending on the pace of recovery and financial market sentiment (UNCTAD, 2009: ii-iii).

UNCTAD is not alone in its sombre perspective. The World Bank said in June 2009: ‘While the global economy is likely to begin expanding again in the second half of 2009, the recovery is expected to be subdued as global demand remains depressed, unemployment remains high, and recession-like conditions continue until 2011’ (World Bank, 2009). The US Federal Reserve anticipates growth in the second half of 2009 but is not at all confident about this being sustained into 2010. The European Central Bank is predicting a meagre 0.2% growth in the euro area in 2010. The news that the British economy contracted by a further 0.4% in Q3 2009 only added to anxiety about the prospect of a double dip recession (King and Gilmore, 2009).

Regardless of any potential economic recovery, the prognosis for workers is more grim. Following the resumption of growth in output at the end of each American recession since World War II, it has taken steadily longer for employment to return to its pre-recession levels (Wall Street Journal, 4 April 2009). The typical lag following the recessions of the 1940s and 1950s was 18-21 months. After the recession of 1974-75, it took 26 months and, following the early 1980s slump, 29 months. Following the 2001 recession, it took a grinding 48 months, or four
years, for employment to recover (Wall Street Journal, 4 April 2009). How long will it take for the US to generate net job growth of seven million jobs, the toll thus far? The Director General of the ILO declared in June that ‘[i]n short, the world is looking at a deep and prolonged jobs crisis’ stretching out over the next six to eight years, with employment not recovering fully for four or five years after output starts to recover (ILO, 2009b).

The crash of late 2008 was not simply the result of a financial meltdown but had its roots in a crisis of profitability and excess capacity that has plagued Western economies since the 1970s (Brenner, 2009; Harman, 2009). The devalorisation of capital that has occurred has been huge but still insufficient to restore vitality to the system. This is why the bailouts, stimulus packages and low interest rates can work for a while, but they cannot end the crisis. It is why unemployment is forecast to keep rising. It is possible that the latter half of 2009 going into 2010 may see positive growth, but it will be relatively anaemic and prone to worse shocks.

Like a sick patient suffering multiple diseases, one ailment might be cured to return the patient to apparent health, only for another disease to break out elsewhere on the body economic. This has been the pattern for years. Fixing up the Asian crisis of 1997-98 involved the US stepping in as the buyer of last resort, sucking in imports that only contributed to its long term indebtedness. Lower interest rates in the late 1990s only spurred on the ‘tech bubble’ of 1998-2000 which brought forth the Enrons, the WorldComs and the eventual crash in 2001.

Still lower interest rates sparked off the US housing boom of 2002-06, which in turn allowed workers to supplement their declining real wages by tapping into the equity on their homes by borrowing more. Working class indebtedness soared, housing prices skyrocketed and the boom ended with the subprime crisis of 2007-08 which shredded house prices, produced millions of foreclosures and brought about the credit crunch in 2008. The stimulus packages are another adrenalin shot in the arm to the sick patient. They may speed things up for a while, but they will not resolve the underlying problem.

Essentially, there are two ways that the systemic crisis in the world economy may be resolved. One is by the capitalist classes undertaking
immense programmes of industrial restructuring and further destruction of capital stock. This means more decades of austerity and attacks on the working class and, potentially, a drive to a fresh inter-imperialist conflagration such as followed the Great Depression of the 1930s. The alternative is the working class solution, of resistance, fight-backs and opening the way to a socialist resolution of the crisis based on democratic planning and production for human need, not the anarchy of the market and the profits of the few which brought us this catastrophe.

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THE IMPACT OF THE GFC ON AUSTRALIA AS A ‘DUAL ECONOMY’

Harry Perlich

The impact of the global financial crisis (GFC) on the Australian economy can be viewed from a ‘dual economy’ perspective, focusing on its four most populous and economically powerful States - NSW, Victoria, Queensland and Western Australia. This perspective emphasises the duality between the ‘resource States’ of Queensland and WA and the ‘manufacturing States’ of NSW and Victoria.

A ‘dual economy’ analysis provides a better understanding of the causes of the strong growth of the Australian economy prior to the GFC and highlights the imbalanced impact of the GFC on the four key States. It shows that a focus on aggregate growth of the Australian economy fails to fully engage with the unbalanced economic impacts that attend upon both periods of growth and crisis. Finally, the emphasis on the dual economy allows further insight into the period following the downturn, with the Australian economy now appearing to recover, but in different directions in the two groups of States.

Stronger for Longer

From 2006 to the dramatic stock market decline of late 2008 a ‘consensus’ view of economic growth predominated, captured by the phrase ‘stronger for longer’. Experts, international banks and economic consultants, argued that there would be a sustained period of global growth into the future. As late as March 2008, Access Economics maintained that the Australian growth rate for 2008/09 might be 3.8%,
while the Australian Treasury itself anticipated growth of 2.75% (Access Economics, 2008).

The basis for the ‘stronger for longer’ thesis was China’s economic development, a surge that came to be symbolised by the huge steel ‘birds-nest’ stadium built for the 2008 Olympics. China was consuming an exponentially increasing quantity of raw materials, including one of Australia’s primary exports, iron ore (ABS: 5368.0). Chinese growth exceeded 10% per annum from 2003 onwards and was anticipated to continue at this pace for years to come. China’s dynamism was nearly matched by India’s, which reached 9.7% GDP growth in 2006 (IMF, 2009). These two economies combined contain more than a third of the world’s population.

The resources consumption of these two growing Asian economies was identified as a primary driver of Australia’s strong GDP growth and its ability to maintain that growth even as the US economy was subject to the evolving sub-prime mortgage crisis. However, putting China at the centre stage of Australia’s export boom is misleading. In the last five years, Japan has had the primary export market position for Australia, until China surpassed this position at the beginning of 2009, notably after the onset of the GFC (ABS: 5368.14). South Korea has been the third most important export market, exceeding the next market, India. It is true however that both China and India have been the source of greatest value growth as export markets for Australia, with China growing 284% from 2004 to 2009, and India growing 180% (Japan 125% and South Korea 103%).

In any case, the buoyancy of the global economy and the Australian export boom contributed to uneven development in the Australian economy. Indeed, economic analysts began to refer to a ‘two-tiered’ economy, separating their analysis of the economic conditions and growth of Queensland and Western Australia (the ‘resource’ States) from that of the other States. This division is pertinent for comprehending the economic and social imbalances that were developing in the Australian economy, with negative impacts increasingly evident.

The characterisation of Australia as a dual economy must be qualified and elaborated. The economic performance of WA and Queensland has
been distinguished over the last five years from that of NSW and Victoria, as manifested in State Final Demand statistics (Figure 1). State Final Demand experienced the greatest expansion in WA in the period from 2004-2009, at 45%. Queensland was also strong. NSW was the weakest, with an increase of 15%; while the rate of growth in Victoria only slightly exceeded that in NSW.

**Figure 1: State Final Demand, Selected States, index, base 2005**

Although NSW and Victoria remain the largest economies (with the largest populations), WA and Queensland had accelerated economic growth. Their accelerated growth received a substantial contribution from investment. For example, although WA has the smallest population of the four States, its private new capital expenditure increased fastest (as shown by Figure 2 on the next page). In the five years to June 2009, WA private new investment increased by over 200%. Queensland’s private new capital expenditure increased by 82%, reaching equivalence with
NSW by mid 2009. New capital expenditure in Victoria increased by only 53%. NSW came last, with a 24% increase.

**Figure 2: Private New Capital Expenditure, All Industries, Selected States, $million per quarter, 4 period rolling average**

Source: ABS 5625.0

The primary source of WA’s investment performance was the mining boom and the rising international demand for raw materials such as iron ore and natural gas. In June 2005, mining investment in WA was equal to the other three States combined (as shown in Figure 3). By June 2006, investment in mining in WA had reached $11 billion annually, increasing at a rate of around 25% per annum. By June 2009 new mining investment in WA was double that of the other States combined, reaching almost $6 billion dollars per quarter.
Queensland mining investment also greatly increased in the same period, peaking at $2 billion dollars per quarter in December 2008, significantly exceeding that of NSW and Victoria.

**Figure 3: Private New Capital Expenditure in Mining, Selected States, $million per quarter, 4 period rolling average**

Total capital expenditure in WA comprised an extraordinary share of total new capital expenditure in Australia over the last five years. In turn, the dominance of mining in this total investment has been significant to the structure of investment in WA. Mining constituted 58% of all private new capital expenditure in WA in June 2005 (as shown in Figure 4 on the next page), peaking at 78% in September 2008. For Queensland, mining investment had constituted 21% of total private new capital investment five years ago. It increased substantially to reach a peak of 36% in March 2009.
Investment, Population Growth and Housing

The total investments in the resource-rich States entailed increasing demand for suitable skilled labour. Consequently, workers streamed to WA and Queensland. Combining immigration from other countries, interstate migration and natural births, Queensland saw the highest population growth of any Australian state, growing at a consistent 2.5% per annum since 2003 (ABS: 3101.0). WA’s population growth was the second highest in 2003 at 1.5%, but has since outpaced that of Queensland.

Source: compiled from ABS 5625.0
Regardless of interstate migration, the primary source of labour (and population growth) for WA in the last several years has been from overseas. An increasing share of Australia’s immigrants has diverted to WA, due to the strong prospects for employment at high wages. This phenomenon has resulted in WA’s annual population growth touching 3% and has contributed to Australia’s rate of overall population growth rivalling that of India (IMF, 2009).

The population surge in WA and Queensland required more housing. The shortage of housing generated dramatic increases in prices for both land and houses. House prices in WA sustained an average growth above 30% in 2006-2007 (REIA, 2008). Indeed, price rises had been so relentless in WA that the average house price surpassed Melbourne’s average level in mid-2006 (Figure 5). News reports indicated that land package buyers were camping at new release sites overnight to be sure of securing one of the limited land allotments available (Sydney Morning Herald, 6.8.2006).

**Figure 5: House Prices, Selected Capital Cities, Residex Resales**

![House Prices Chart](image)

*Source: Residex (2009) Market Wrap*
Rental rates in WA and the other States also rose rapidly, as shown in Figure 6 below. This development exacerbated economic disparities, as the direct beneficiaries of the mining boom (i.e. those on higher wages) were better able to afford the rising rents than those economically removed from the boom.

Figure 6: Median Weekly Rent for 3-bedroom Houses, annual change

![Graph showing median weekly rent changes for Sydney, Melbourne, Brisbane, and Perth from Dec 02 to Dec 07.](source)

Source: REIA, Real Estate Market Facts, December 2007 quarter

Meanwhile, NSW rental rates also started to rise sharply, but for different reasons. This rise can be traced to the house price boom that occurred at the beginning of the decade. By 2003, NSW house prices had peaked temporarily, while affordability hit a record low (HIA/CBA, 2008). There followed a sustained period of house price stagnation, coinciding with sagging land sales for property developers. Increased infrastructure costs and high interest rates were two factors contributing to the ‘malaise’ in the NSW housing market at that time, and slowing the rate of housing construction.
Yet, underlying housing demand was increasing, as NSW continued to have the largest total population growth, in absolute numbers, of any state. The net result was that an increasing number of people were renting, unable to buy their own home. Consequently, vacancy rates in NSW dropped to an unprecedented 1% of total housing stock by the end of 2007 (REIA, 2008). This drove a boom in rental returns. As in WA, dozens of people would line up for newly available rental properties in Sydney, sometimes outbidding each other to gain tenancy.

This scenario is a testimony to the socially disruptive machinations of market forces in a complex sector like housing: prices surge and then stagnate; supply exceeds and then falls short of demand; there is seldom, if ever, a sustained period of balance or predictability.

**Inflation...in Wages, House Prices, Rents, Retail, Petrol**

Despite significant population growth for the ‘resource’ States, the sudden boom still meant that labour remained in short supply. The four large States all had unemployment levels at around 6% at the end of 2003. In both Queensland and WA unemployment then dropped rapidly, with Queensland reaching 3.1% in August 2008 (ABS: 6202.0) and WA dropping to 2.6% in the December quarter of 2008, the lowest rate ever recorded in that state. Figure 7 on the next page illustrates the emerging unemployment differential between the ‘resource’ States and NSW and Victoria.

The chronic shortage of labour, particularly in WA, fuelled the high wages already offered in the mining and related sectors. While it may be apocryphal, there was talk of Sydney doctors leaving their practices to become truck drivers in the Kimberley where they could earn higher incomes.

The rate of increase in ordinary-time wage costs in WA exceeded the Australian average from 2005 onward (as shown in Figure 8 on p. 75). In 2006, the rate for Queensland followed suit, and they continued to exceed NSW and Victoria up to at least June 2009.
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The rate of increase in the cost of wages, as well as rents, housing and retail goods prices contributed to a sharpening rise in consumer prices. The Reserve Bank of Australia (RBA) maintains a benchmark threshold of 3% as an upper limit to ‘optimal’ CPI inflation. The rate for the Australian economy repeatedly exceeded this level, and prompted
increases in the RBA’s target cash rate. The cash rate was raised eight times by 0.25% increments from the beginning of 2005 to early 2008.

**Figure 8: Labour Cost, annual percentage change**

![Labour Cost Chart]

Source: compiled from ABS 6345.0

It appeared that the RBA was justified in increasing its target cash rate, in view of measured aggregate performance of the Australian economy and accelerating inflation. However, from the perspective of the individual States, the rate decisions of this period could be seen to have had detrimental effects, economically and socially. Although the export boom had generated great wealth and high employment in WA and Queensland, there were negative impacts in the ‘manufacturing’ States as a consequence. One of these impacts was the rising Australian dollar. Increasing iron ore and other mineral exports (and associated speculative activity) generated demand for the Australian currency, driving it up against the value of the US dollar, reaching a high of 79 cents to the $US in 2006 (RBA, 2009). The rise of the Australian currency, from its extraordinary low of 48 cents to the $US in 2001, had a negative effect
on exports from Victoria and NSW. The agricultural sector in general, with a strong export focus, was also disadvantaged by the rising exchange rates.

In addition, the boom in China was contributing to an increasing demand for crude oil, generating sharp increases in international prices. Australia was partly shielded from the international price spike, due to its rising currency, but the impact was felt by those least able to afford prices at the pump, which rose to an average in Sydney above $1.40 per litre in early 2008 (Australian Automobile Association, 2009). The rise in oil prices, a natural product of the global economic boom, generated much chest-beating from government Ministers and the usual threats of inquiries into the petroleum refining and retail sectors.

Figure 9 below illustrates the differential in the state-based CPI between the ‘resource’ States and the ‘manufacturing’ States. It is evident that WA and Queensland were the States making the greatest contribution to consumer price inflation.

**Figure 9: CPI for Selected States, index rebased to 2005**

*Source: compiled from ABS 6401.0*
The RBA assessed that aggregate economic activity was generating excessive inflation. The response was a series of hikes in the target cash rate, which the commercial banks closely followed in their mortgage lending rates. The RBA target cash rate had already been increasing since 2001. However, a slow ratcheting of rates, perhaps tolerable in a period of moderate growth, became more rapid as the economy went into hyper-drive. (This latter phrase is not inappropriate, given that WA annual growth had peaked in September 2007 at 13% (greater than China) while Queensland had exceeded 10% the previous quarter (ABS: 5206.0)). The benchmark cash rate was raised to its maximum of 7.25% in March 2008. Although the rate rises had helped to temper the WA and Queensland economies, it was feared as early as 2006 that the rate rises might push NSW or Victoria into recession (ABC, 2006). The concern was reflected in retail sales growth, with NSW slowing significantly, having negative growth in the second half of 2008, as shown below in Figure 10. It became clear that one of the primary instruments of national economic regulation was a blunt stick that punished sectoral and spatial economic weakness while failing to address the primary dimensions of economic imbalance.

**Figure 10: Retail Sales Index, Selected States, rebased to 2005**

![Retail Sales Index Graph](source: compiled from ABS 8501.0)
Another significant impact of the interest rate rises was a further suppression of demand in the NSW housing market, despite the underlying shortage of housing.

Figure 11 illustrates the relative experience of the housing sector in NSW and WA. Despite its much larger population and underlying housing demand, NSW building approvals for private dwellings kept dropping throughout the boom period. One major NSW home builder, Beechwood, went bankrupt in May 2008 (ABC 2008), leaving many people with half-built homes. Another closed its NSW land development division altogether in mid 2008, having an excess supply of land to last many years and few buyers (Dunlevy, 2008). In WA, the pent-up housing need was met, albeit slowly. Subsequent to the boom, building approvals in WA have dropped, though their level remains buoyant compared to those prevailing in NSW.

**Figure 11: House Approvals, Selected States, original, moving annual total**

Source: compiled from ABS 8731.0
In the Eye of the Storm

While the Australian economy – or substantial parts thereof – boomed on the back of China’s resource demands, there was increasingly bad news from the USA. Starting with the collapse of the sub-prime mortgage market, the rest of the economy was adversely affected as it became increasingly evident that a variety of ‘highly reputable’ financial institutions were in difficulty. Although the Australian economy was not directly affected by US economic conditions to any great extent, the question was whether China would be affected by US conditions. Evidently, what is bad for the Chinese economy is bad for the Australian. Initially, there was confidence that the growth of China, though export led, contained a substantial and sustainable internally generated component. However, economic analysts began to revise their Chinese growth forecasts downward.

Despite these ominous signs, it is notable that the view of Australia’s circumstances among economists was still benign. This optimistic view was held not so long ago; but it is easy to forget the crucial details of economic sentiment that helped to push economic policy in particular directions at this time. For example, in this very journal, Stephen Bell and John Quiggin (2008) suggested that:

The pattern of boom and bust that characterised the Australian economy from the early 1970s to the early 1990s currently seems to be a thing of the past as Australia enters its sixteenth year of uninterrupted expansion.

A complex series of factors would ensure that, technically, Australia would not actually enter a recession as several other economies had done. However, the positive attitude about Australia’s economic resilience would be tested.

‘Weaker for Longer’?

The performance of the Australian stock market during the GFC is an important barometer of overall sentiment about the Australian and world
economies during this period. The stock market was both a symbol and a manifestation of the economic downturn.

The All Ordinaries Index reached its highest point of 6,873 on the first of November 2007. A year later, the index had halved, involving a nominal one trillion dollars in value lost (Digitallook, 2009). The downturn in the stock market appeared relentless, with previous optimism being matched by a comparable pessimism. The loss in value of stocks affected the general population in several ways. First, with stocks favoured by some as a form of savings, a reduction of the financial reserves in this sector meant less potential cash available for investment or spending. In addition, superannuation funds are dependent on stock market performance. The collapse of the stock market after 2007 saw some retirement savings slashed by up to 50%. News reports in 2008, not surprisingly, cited many people delaying their retirement and being forced to continue working (Mercer, 2008).

Figure 12: All Ordinaries Stock Market Index and RBA Cash Rate

Sources: Yahoo (2009), RBA (2009b)
The magnitude of the 2008 stock market collapse (both in Australia and internationally) drew repeated comparisons with the Great Depression of the 1930s. This comparison encouraged a potentially misleading interpretation of current events. The stock market collapse of the 1930s was accompanied by very high unemployment and social upheaval; and it involved uncompromising beggar-my-neighbour moves by the major players of the world economy. Economic stimulus measures in the US after 1929 were implemented late and occurred in an era when the concepts behind ‘Keynesian’ economics had not yet been popularised. This recent economic downturn saw some quick state stimuli implemented. Governments worldwide pumped billions of dollars into their economies to stimulate economic activity.

In the US, the ‘Cash for Clunkers’ program, provided subsidies for consumers to buy new cars. In Australia, the government quickly implemented measures to stimulate the economy, including increased grants to first home buyers at the end of 2008 (Office of State Revenue, 2009). A prominent effort was the one-off general stimulus to the retail sector, providing a $900 grant to taxpayers to spend at the supermarket and stores such as Harvey Norman (The Australian, 3.4.2009). The Keynesian stimulus measures were justified by the characterisation of this downturn as cataclysmic, summed up by Kevin Rudd (2009):

> From time to time in human history there occur events of a truly seismic significance, events that mark a turning point between one epoch and the next. There is a sense that we are now living through just such a time.

Several months after Rudd’s essay appeared, the stock market witnessed a substantial bounce back from its absolute lows. Figure 12 illustrates the movements in the Australian stock market, while Figure 13 (on the next page) benchmarks several high-profile companies against the All Ordinaries Index. BHP initially defied the downturn, but its share price did fall and has recovered somewhat this year. It is notable that, since the beginning of 2009, the value of shares in the banking sector has also been more buoyant, exemplified by the performance of Commonwealth bank stocks. Other companies, such as Qantas, took a beating and have only slowly started to recover.
Figure 13: Index of Selected Australian Stock Market Indicators, Sept 2007–Sept 2009

Note: Base of 100 for all indices set for November 2007
Sources: Yahoo (2009), ASX (2009)

There was a sharp rise in unemployment during the downturn, but it appears to have peaked nationally at 6.3% in February 2009 (based on a 4 quarter average). This figure remains substantially below the rate of unemployment that followed the 1990s recession, when it had peaked at 10.5% in February 1993 (ABS: 6202.0).

Despite signs of reasonable economic health, the return of more positive consumer sentiment and China’s resumption of rapid economic growth, economic analysts initially continued to anticipate hard times. In May 2009, Econtech, a forecasting firm, anticipated a contraction in GDP of 1.2% for 2009 (KPMG Econtech, 2009). NAB, in its June 2009 Quarterly Business Survey & Forecasts, still anticipated unemployment to exceed 7% in 2009 and rise above 8% in 2010.
Narrowly Averting a Recession

That the pessimistic comparison with the Great Depression was not fully justified, at least for the Australian economy, became clear when GDP figures were released for the March quarter of 2009, confirming a slight quarterly downturn in December 2008, but with annualised growth remaining positive (ABS 5206.0). This showed that Australia had narrowly dodged a ‘technical’ recession, unlike many of the G20 nations.

In the medium term, there are grounds for believing in the continuing good health of the Australian economy. Indeed, given resurgent economic conditions, the RBA determined in early October 2009 that the ‘life-support’ provided by historically low interest rate levels should be scaled back. The target cash rate was therefore raised from its historic low of 3% by 0.25%. The first RBA target rate rise in October 2009 also drew international attention. Australia was seen, symbolically, to be leading the advanced G20 economies out of the downturn.

The RBA’s decision, based on the latest economic indicators, caught several analysts by surprise – with Westpac, for example, scrambling to forecast interest rate rises being higher and sooner in response to improved economic indicators (Evans 2009). Regardless of greater optimism about economic recovery, the Australian economy has long-term structural problems. The imbalance of economic performance (across the four main States as well as nationally) is persistent and the possibility of increasing social disadvantage is developing. As the economy as a whole improves in the next year, the RBA is likely to raise the cash rate again. This may continue to have adverse effects on both the weakest States and the weakest social groups.

The Conditions and Prospects of Individual States

The Australian economy is facing economic conditions and policies, following the GFC, that will have different impacts in different States. Again, a useful focus is on the division between the ‘resource’ States of WA and Queensland and the other two populous States, NSW and Victoria.
The overall Australian economy avoided recession in part because of strong export figures, reflecting the significant contribution from the ‘resource’ States, particularly WA. The Chinese economy did not fall into recession, with economic growth reviving to near 8% in 2009 (Forbes, 2009). This result has contributed to the sustained export performance of WA and this, in turn, has contributed to the high value of the Australian currency. Mining investment in WA remained strong in 2009 (Figure 3) and high population growth ensures a ready supply of labour for the WA economy. House price growth in WA has become more subdued (Figure 5), with lack of affordability also easing as a consequence of the interest rate cuts that occurred in 2008-9. However, it is possible that the strength of the WA economy will again see bottlenecks in housing supply from 2010 onwards, as demand for housing surges on the back of population growth. In addition, resource demand from economies currently in recession will add to demand pressures in the near future. As the RBA raises the target cash rate, affordability of housing in WA is likely to slip backwards again.

Although Queensland is also identified as a ‘resource’ State, its economy is more balanced than that of WA. For example, Queensland has a significant manufacturing base and investment (ABS: 5625.0). The Queensland economy boomed on the back of the resources boom, in which the economy also benefited from the initially highest population growth among the selected States. Since the GFC, the level of private investment in Queensland has been more subdued. Unemployment also rose sharply in Queensland following the GFC. The new economic conditions have led to significantly less buoyant retail spending in Queensland. Also, the rate of home building has sharply reduced. Building approvals in Queensland in September 2009 were down to 63% of their peak at the end of 2007 (Figure 11). Strong population growth is likely to increase housing demand in the longer term, with the possibility of rising house prices if demand exceeds supply. Housing rental rates are also likely to rise. This will adversely affect affordability for the poorest sectors of society in Queensland.

While the Australian currency remains high relative to the US currency, Queensland’s manufacturing and agricultural sectors will be impacted negatively, with constraint on growth and employment in these sectors.
Economic growth in Victoria before and during the GFC was lower than of the ‘resource’ States. Manufacturing investment particularly declined from the beginning of 2006 and has remained flat since (ABS: 5625.0). A significant portion of this condition can be attributed to the high market value of the Australian currency, which has made Australian goods more expensive overseas, while encouraging imports of foreign manufactured goods. The most recent aggregated economic indicators suggest that the Australian currency will remain high at least until the US economy begins to recover, with an associated stronger US currency. The Victorian economy will therefore continue to experience subdued conditions in the manufacturing sector. Unemployment can be expected to remain higher than it might otherwise be, at 5%, and remains higher than the ‘resource’ States (Figure 7).

Victoria has experienced relatively strong residential building activity throughout the economic boom and subsequent to the GFC. This may be attributed to the combination of relatively strong population growth and affordable housing, compared to NSW. The median house price for Melbourne is $100,000 lower than Sydney (Residex, 2009, Figure 5). With interest rates at a record low, there is the likelihood of increased building activity in Victoria. Housing finance commitments have risen significantly at the end of 2009, boosted particularly by first home buyer activity (ABS: 5609.0). This will result in increased residential construction activity into 2010 and a boost to State employment.

NSW has been the weakest State among those analysed over the last five years, while being the State with the largest economy and largest population. Weakness has manifested in State Final Demand (Figure 1) as well as unemployment levels (Figure 7) and retail consumption (Figure 10). Like Victoria, NSW manufacturing investment was subdued during the economic boom, partially due to the high Australian currency. Going into the boom, NSW housing affordability had been low, due to high house prices and infrastructure costs on new developments on urban fringes. This problem was exacerbated as the boom developed, with rising interest rates suppressing recovery in residential building activity in NSW. Consequently, despite high population growth, NSW building activity reached record lows in 2008. The decline in demand was correlated with economic stress for people paying home loans, with
NSW having 12 of the 20 highest mortgage delinquency areas in Australia (Chong, 2008).

In late 2009, NSW residential building activity shows signs of an upswing, subsequent to the economic stimulus measures targeting first home buyers and a return to low interest rates. It is therefore likely that building activity will make an important contribution to NSW economic growth into 2010. However, this upsurge will be tempered by impending interest rate rises. Already, there are signs of tension emerging between the need for more housing and reducing affordability as house prices rise (Residex, 2009) and interest rates begin their upward cycle.

The NSW economy continues to be adversely affected by the dual character of the Australian economy, with the strength of WA causing the RBA to raise aggregate interest rates, despite economic vulnerability in NSW. As the world economy recovers, the current conditions will be exacerbated. Action by the RBA to temper economic activity at the aggregate level is likely to negatively impact on NSW, as occurred before the GFC. In addition, there may be a return to the chronic issues of lack of housing affordability, as well as high mortgage defaults, as occurred in NSW in the last two years (ABC, 2008b).

**The Importance of Labour Supply**

Prior to the GFC, the Australian economy had developed an acute labour shortage, losing its ‘reserve army of labour’, particularly in WA, where unemployment had fallen below 3% in late 2008 (ABS: 6202.0). Although this did not lead to wage breakouts that would challenge the share of value going to ‘capital’ or profits, there did emerge bottlenecks in the capital accumulation process. Some bottlenecks were exacerbated by the high mobility of some workers – neophytes in property development headed off to Dubai, for example. Demographers identified the phenomenon of ‘Gen-Y’ being more fickle and mobile than previous generations of workers. Gen-Y was alleged to have a freer attitude to work and career commitments (News.com.au, 2007). Regardless of generational stereotypes, this meant the inconvenience of high staff turnover and training costs for companies. It appears that this period has
now ended, with Gen-Y workers being disciplined by higher unemployment levels (Ambition, 2009).

Although the rate of unemployment has not lifted much in absolute terms in any of the States, the amount is significant from the perspective of business confidence. Wage inflation has moderated, though not dramatically (ABS: 6345.0) and, perhaps more importantly, skilled labour is easier to find (and probably keep). The ACCI-Westpac Survey of Industrial Trends for September 2009 revealed that the difficulty of finding suitable labour had eased significantly. Furthermore, expectations of profitability have returned to normal. As the latest ACCI-Westpac survey claims:

...recovery in profit expectations has coincided with better actual conditions, significantly stronger activity expectations, easing unit cost pressures (ACCI, 2009: 6).

It is a rather paradoxical feature of the Australian labour market that only a small increase in unemployment appears to have significantly eased labour market tightness. It remains to be seen how significant this development will be. It is conceivable that the current economic recovery will again stimulate employment growth and reduce unemployment levels, even perhaps into record territory for recent years.

The Australian economy overall has maintained positive economic growth on the back of the soft downturn in Asian economies and China. With recovery in other developed economies, including the USA and Japan, Australian economic growth could accelerate, with consequent renewed shortages in labour supply. The condition is likely to again impact the non-resource States more significantly if the policy response from the RBA is a higher target cash rate, designed to temper economic activity and inflationary pressures.

**Conclusion**

The Australian economy has gone through stormy times in the last five years. The period started with analysts anticipating a sustained period of strong growth, though this anticipation turned out to be misinformed.
The cyclical nature of capitalist growth meant that the ‘stronger for longer’ thesis was undermined by the emergence of the GFC. Although several leading economies did go into recession, Australia was in a unique historic and economic position. The extraordinary growth of China in the last decade helped to shield the Australian economy from the worst effects of the GFC. Despite this, pessimism eventually resounded through the Australian economy, reaching the top of the political hierarchy. The sentiment can be characterised as ‘weaker for longer’. Yet a number of features of the current economy have helped maintain its strength, at least in macroeconomic terms. Continued strong export markets have supported the resource States and their contribution to GDP, particularly WA. Government economic stimulus and low interest rates provided the basis for a pick-up in growth in the non-resource States. A significant portion in the rebound in non-resource States is likely to be housing. NSW in particular has accumulated underlying demand that should receive greater response from supply in 2010.

Total economic activity in the Australian economy will also be stimulated by an unprecedented level of population growth. This will also contribute to the housing boom, in the context of favourable interest rates, generating jobs and promoting positive GDP figures. It is, therefore, likely that the pessimism of the recent past will soon pass, despite the impact of the export boom on the fate of the manufacturing sectors.

There remains, however, a danger that the economic and social imbalances that emerged prior to the GFC will return, perhaps fairly soon. The continuing strong demand for raw materials, particularly from WA continues to underpin the high Australian currency. Strengthening economic activity, whether in WA or in all the States, will tend to have an uneven effect on both the States and on their respective economic and social conditions. Housing affordability, as one primary example, remains relatively low in all States. Although this has improved in the context of the low interest rate environment, the direction of interest rate movements in the near future will be up, with affordability therefore likely to deteriorate.
The conditions for a cycle of boom and bust in the Australian economy are building again. In the nature of free market dynamics, and belated government responses, there will be those that gain and those that experience disadvantage. The divide of advantage and disadvantage crosses the State regions as well as the social groups within them.

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*The author thanks the anonymous referees and the editor for their helpful comments and suggestions.*

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ABS 5206.0 Australian Bureau of Statistics - *State Final Demand.*


THE CRISIS AND THE AUSTRALIAN FINANCIAL SECTOR

Evan Jones

Much material has been published on the ‘global financial crisis’, especially on its US roots. In Australia, there is a peculiar tension in the commentary that remains unarticulated. There co-exists a general complacency or optimism, especially in official circles, with documentation of a string of financially linked failures. The latter have been mostly treated in isolation (and mostly by journalists).¹

This article summarises a representative range of business failures. The boom years facilitated widespread bravado, incompetence and unconscionability in Australian businesses that the finance sector has fostered and nurtured. A new class of unsophisticated investors has become victim of the rosy promises of ‘shareholder capitalism’. One perverse byproduct has been the further consolidation in the Australian banking sector itself. The financial regulatory agencies are found to be inadequate. Recent mooted regulatory changes reflect the need felt for action by the Rudd Government, but the changes are piecemeal and have been contested by the relevant vested interests. The article concludes with the view that no deep inroads will be made into dysfunctional elements in Australian business culture, that the Australian financial sector will continue to abuse the public interest in the service of private

¹ There is an atypical dependence in what follows on journalistic accounts, essentially for detail. Academic commentary has been meagre and generally sanguine, comparable to the literature emanating from the regulatory agencies. Hawtrey (2009) is representative – a technically admirable coverage of nation-specific data, but which fails to delve into the murky depths that generate dissonance from the official happy story.
profit, and that the structure and culture of the financial regulatory agencies will continue to be inadequate.

**Broad Dimensions of the Crisis**

At the macroeconomic level, the finance sector in Australia has been less badly hit than has been the case in the US or the UK (or Iceland). There have been no Lehmann Brothers / Bear Stearns / Merrill Lynch, and no Northern Rock / Royal Bank of Scotland / Halifax Bank of Scotland (HBOS). There have been claims that the lesser financial fallout is a product of a superior regulatory framework, and of greater self-discipline by the lending institutions.

Both these claims have merit but are over-stated. The disastrous practices and poisonous portfolios of Wall Street investment banks are a reflection of the centrality of investment banks on Wall Street.\(^2\) The more subdued adverse experience in the Australian finance sector is partly due to its predominant domestic orientation, and the concentration of power at the top. Simply, there was too much easy revenue to be made on the home turf (c/f Verrender, 2009c).

The overseas failure that bears the closest resemblance to Australian conditions is that of HBOS. HBOS expanded rapidly its business loan book with inattention to quality, especially in the graveyard that is property development. As a consequence, HBOS accumulated £19 billion of bad debt charges in 2008-09, 8% of its relevant business loan book (Peston, 2009).

Australian banks did not succumb to that degree of excess, but they are guilty of similar practices, and locally unique ones as well (margin lending in particular). For example, the NAB had a significant portfolio of US-sourced collateralised debt obligations, and wrote down the bulk (over $1 billion) of their book value for 2007-08.

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\(^2\) Given that character, it is true that the 1999 abolition of commercial bank / investment bank separation and the 2000 entrenchment of an unregulated derivatives market, both resulting from industry lobbying pressure, facilitated the ensuing crisis.
Analyst estimates of total loan losses by the big four banks for calendar year 2009 range from $12 billion (KPMG) to $16 billion (UBS), with UBS expecting comparable pro rata losses through the first half of 2010. Australian Prudential Regulatory Authority figures highlight that, at end of June quarter 2009, bank ‘impaired assets’ stood at $28.3 billion, 1.08% of total assets. Two years previously, the comparable figures were $4.0 billion, 0.20% of total assets. At June 2009, the banks had made provision for bad and doubtful debts of $20.4 billion, up from $7.8 billion two years previously.

Large corporate exposures were the major culprit. The big four banks all had exposures to ABC Learning and Allco Finance Group. The CBA and NAB had additional exposure to Babcock and Brown, and the CBA (the predominant ‘loose lender’) had exposure to Lehman Brothers. Westpac, CBA and NAB had $400 million total exposure to Commander Communications.

Journalist Stephen Bartholomeusz has claimed that banks had moved commercial property loans off their books through securitisation to listed property trusts which have borne the brunt of falling property values (Bartholomeusz, 2009a). Yet the commercial property impaired asset ratio was at 4.5 per cent as at June 2009, having soared from trivial levels over the previous 2 years (Reserve Bank of Australia, 2009: 20). In December 2008, domestic banks held 86% of a $190 billion commercial property exposure (Cummins, 2009).

Listed property trusts did lose heavily. The top 16 trusts on the S&P/ASX A-REIT index produced losses over 2008-09 totaling $13.6 billion, with property assets being devalued by over $10 billion (Nicholls, 2009). REIT management has responded merely by engaging

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3 RBA, Statistics: Banks – Consolidated Group Impaired Assets – B5. Accessed 2 October. Comparable figures (impaired assets as percentage of total assets) for the early 1990s recession are 3.46% as at June 1990 (the first consistent data available), rising to a maximum of 6.91% by March 1992 (data obtained from the RBA).

4 In the two year period to June 2009, the quarterly changes in impaired assets totalled $24.3 billion, comprising $42.4 billion in new impaired assets, minus $10.1 billion in impaired assets write-offs, minus $7.9 billion in ‘cured’ loans removed from impaired asset status.
in a ‘capital-raising frenzy’, and promising industry consolidation to head off future market pressures.

All the banks have substantial exposure to the failed shopping centre owner/manager Centro (the CBA’s exposure is a rumoured $1 billion). With major exposure to the US property market, Centro was a fragile entity. Yet the major banks readily provided the debt. The ANZ CEO, Mike Smith, referred to it as an ‘emblematic exposure’, with the banks having to support it or face a general commercial property wipeout (Bartholomeusz, 2008). Atypically, bank lenders have decided to support Centro’s rehabilitation.

There is also the ‘pub’ sector, to which the banks have a massive exposure ($7 billion in NSW alone), having seen it as a milch cow built on poker machine revenue. Hotel valuations, on which the major banks readily expanded credit, were ludicrously inflated. Specialist vehicles, owning securitised hotel assets, have been major casualties.5

There are grim stories in the residential mortgage domain. By June 2009, loans in arrears (by loan value) on bank balance sheets reached 0.62% of such loans (0.9% for securitised loans), rising steadily since 2004 (Reserve Bank of Australia, 2009: 47).6 An estimated 25,000 households were 90 or more days in arrears on their housing loans (ibid: 48), up from 13,000 eighteen months previously. Home mortgage difficulties arrived several years earlier than difficulties of business loans, reflecting the peak of the respective bubbles.

Dry statistics come to life with home repossessions. Supreme Court figures show a dramatic rise in claims for possession in New South Wales to almost 5,500 in 2006 (significantly higher than during the early 1990s recession), falling to 4,000 in 2007; in Victoria there was a continuous rise to 3,000 in 2007 (Berry, et. al., 2009). National figures are not readily available for claims or repossessions. South-western Sydney is known to be a particular problem area. However, the media has regularly reported on widespread distress elsewhere – particularly in the Illawarra and the Hunter in New South Wales, and in South-eastern

5 For example, the ING Real Estate Entertainment Fund (Carson, 2009).
6 Non-bank mortgage brokers have a higher arrears rate, whereas building societies and credit unions have significantly lower arrears rates.
Queensland. Claims and foreclosures across the country have climbed again in 2008, and persist into 2009, not least in Western Australia. This second surge, given lower interest rates, appears to be the result of rising unemployment.

The pain of household financial crisis centred on housing mortgage costs is reflected in a header from a provincial newspaper – ‘1/4 % Such a small figure, such a HUGE effect’ (Farrington, 2007). Intolerably high base housing prices coupled with a succession of RBA-induced interest rate rises (see below) put many mortgage holders at or over the threshold of payment sustainability. The scandal, as the article highlights, is that not only are there no figures on home repossessions, but the figure of forced house sales is certainly a multiple of court-registered figures. The terms on which failed mortgagors relinquish their homes remains unknown and unexamined. Substantial administrative costs are incurred in Supreme Court foreclosure action.

Several Disasters Deserving of Selective Attention

Three failed investment schemes deserve special emphasis – Lehman Brothers Australia, Opes Prime, Storm Financial – because they highlight the adverse effects of the cynical marketing of ‘innovative’ financial products to unsophisticated investors.

In early 2007, the American investment bank Lehman Brothers bought a local funds manager, Grange Securities. Grange Securities immediately started peddling the sort of toxic assets that helped bring down its parent in September 2008. Collaterised Debt Obligation packages were aggressively marketed to municipal councils (especially in NSW and WA) and non-profit organisations. Over 40 councils placed about $625 million in such instruments. The CDOs were in turn linked to Credit Default Swaps, whose returns were dependent on the health of American corporate and mortgage markets. These bizarrely complex instruments were sold as ‘safe as houses’, with favourable ratings from the ratings agencies. This unconscionable phenomenon was compounded by the administrators of Lehman Brothers Australia which forged a ‘deed of company arrangement’ in May 2009 – the major creditors (Lehman
affiliates) and staff of the Australian operations extracted close to 100% of their claims, whereas the councils (‘contingent creditors’) were shut out, receiving anything between 2c and 13c in the dollar on their purportedly ‘plain vanilla’ investments.7

From 2003 onwards, the ANZ bank lent hundreds of millions of dollars to ‘stockbroking’ firms that were in reality firms dealing in margin loans for speculative share purchases and in share borrowing/lending with hedge funds. The most significant of these firms was Opes Prime, to which the ANZ committed $650 million (and Merrill Lynch $350 million). The share portfolios included some listed stocks, but were replete with ‘hundreds of tin-pot stocks’ (West, 2008) generating no revenue. The innately flawed Opes’ business model was premised on a permanently rising stock market – more, on dealing only in shares of well-managed firms. With Opes in trouble, the ANZ ‘advanced’ Opes $95 million on 20 March 1998 in return for Opes directors granting the ANZ belated security over Opes’ assets.8 Opes was put into receivership a week later. The ANZ then appropriated $1.6 billion worth of Opes’ clients shares (including those of clients in good standing), and offloaded them at significant discounts. Opes was lending its own clients’ shares for short selling, the drop in share prices triggering the margin calls, which brought down Opes itself. A subsequent deal forged by the Australian Securities & Investments Commission between bank lenders and Opes’ administrators had the banks agreeing to pay out $253 million in return for closing off all potential suits from disgruntled clients. It is estimated that Opes’ clients will receive little more than 30c in the dollar from the fiasco.

7 Remarkably, on 25 September the Federal Court of Appeal overturned the deed, holding that the attempt to release the Lehman group from liability was invalid under the Corporations Act. The litigating Councils had assistance from litigation funder IMF and opinion from the Australian Securities & Investments Commission. The Lehman group and administrator are expected to seek redress in the High Court (Yeates, 2009b).

8 This phenomenon of banks attempting to appropriate security over assets of a failing business, given that the initial loan(s) were made with limited or no security, is a regular practice. A comparable phenomenon occurred with the failing Babcock & Brown, with shareholders left cocooned in a worthless holding company (John, 2009).
Storm Financial collapsed in January 2009. Storm, formally a financial advisory firm, aggressively sold a one product package – the use of debt to speculate on the permanent upward movement of share prices. The package comprised a home mortgage loan taken on the client’s residence (occasionally investment properties), complemented by a margin loan, the total to be placed into an indexed fund designated by Storm, with the loan quantum to be further enhanced if the nominal share value increased or if any slack appeared in the loan to valuation ratio. The customers were perennially low income, retirees, on a disability pension or unemployed; they were generally ill-informed as to the details of their ‘investment’. Necessary information was supplanted by the mesmerising charm of Storm principals, Emmanuel and Julie Cassimatis.

Emmanuel Cassimatis had been a long-time financial advisor and agent, located in Townsville, North Queensland. The transformation of a conventional business into a fantasy operation headed for certain failure and irredeemable suffering for many clients appears to be based on two factors. First, roughly between 2003 and 2007, a large number of previously independent advisory businesses brought themselves under the Storm umbrella, with the resulting operation run in a highly centralised fashion.

The second factor was Storm’s close relationship with the CBA. The bank had been involved with Storm since 1994, but the transformed Storm was evidently viewed within the bank as a profit bonanza. The CBA fuelled Storm’s fantasy – home loans, margin loans through subsidiary Colonial Geared Investments, and ‘wealth management’ of the loans into index funds through Colonial First State. The CBA-Storm relationship encompassed between 4-5,000 clients. The CBA’s desktop ‘VAS’ remote valuation system, introduced in March 2008, gave increasingly generous valuations of client property, readily leveraged into a higher margin loan and more fees for Storm. The CBA extended Storm clients’ loan to valuation ratio to an unprecedented 80% plus 10% ‘buffer’, and a unique office outlet was established in Townsville to service Storm business (countering competition from the Bank of Queensland). The Colonial arms even paid for a ‘gala ball’ in Italy in 2008 for the smooching of clients. Such was the success that the CBA yearly raised sales targets of the Storm-servicing cell, including for 2008-
09. The complacency was smashed with the falling share market in late September 2008.

Storm advisers and staff independently claimed that CGI’s software failed in the mayhem that ensured in October and November, with Storm and clients incorrectly advised or uninformed of developments. In early December, the CBA declined a Cassimatis request for a tide-over loan to assist clients with margin calls. On 10 December the bank unilaterally shut down all Storm-badged products, closing off without consultation all client investments, and effectively defaulting Storm from that time.

Upon examination of some client records, the CBA has subsequently claimed responsibility for some ‘irregularities’, nature unspecified, with promises to make amends, details unspecified. The bank has scapegoated local staff, when clearly the entire model had senior level approval. Its senior representatives dissembled before the Parliamentary inquiry hearings in Sydney on 4 September 2009.9 journalist Alan Kohler (2009) astutely summarised the unholy alliance between the CBA and Storm:

Storm Financial in Townsville was not so much a Ponzi scheme, where new money finances the returns on old money, as a scandalous partnership between spivs and a bank, that should have known better, to place ordinary people in harm’s way.

A Wider Panoply of Unsavoury Practices

The crisis has left exposed a wide range of unsavoury practices whose essential character deserves summary.10 The collapse of several sizeable ‘managed investment schemes’ (Timbercorp and Great Southern) has exposed their dysfunctional character. The MISs oversaw the planting of large-scale plantations of agricultural and forestry commodities. But tax avoidance was the dominant motif. Management structures were neglected; capital planning non-existent, short-termism prevailed in

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9 The author was present at these hearings.
10 Schwab (2009b) conveniently lists a large number of failed companies and the sources of their demise, some of which are treated below.
sectors where long term planning was paramount; fees were gouged. In the case of Great Southern, the ‘advisers’ to potential clients were all paid agents for the company. Stupidly, Bendigo and Adelaide Bank has an exposure of $550-600 million to Great Southern ‘investors’.

On Queensland’s Gold Coast, City Pacific Limited was a combined funds manager and property developer. Its life span (1997-2009) encapsulates the fragile species – built on easy credit for boom times only. City Pacific gouged fees from its First Mortgage Fund, but lost control of the Fund in July 2009. The intrinsic non-viability of its Martha Cove project in the sober climate of Victoria’s Mornington Peninsula highlights that City Pacific was built not to last. The CBA, with a $100 million exposure to the company, evidently thought otherwise.

Also notable is the collapse of the Gold Coast-based large-scale MFS funds manager and holding company. MFS, with myriad satellites, was a complex entity attracting investors through commission-based ‘advisers’. High risk investments and fee extraction brought a major subsidiary, with 10,000 investors, to freeze redemptions in January 2008. The entire group, having changed its name to Octaviar, was forced into administration in October 2008, with unknown losses (one estimate at $1.6 billion) to hapless investors.

Chartwell Enterprises was a small-scale investment company located in the hapless provincial town of Geelong. One man brought in savings from ‘Mum and Dad’ investors on the strength of personal charm alone. A second placed the savings in extremely high risk outlets, mostly sophisticated futures contracts – save for sums siphoned off into the salesman’s extravagant lifestyle and sums unknown siphoned into tax havens. The game was up by September 2006, but the duo delayed the inevitable for another 18 months by bringing in new investors to prevent immediate collapse. Approximately $70 million of hard-earned savings has disappeared with the collapse of Chartwell.

Perhaps exemplary of the extravagance of the boom years was the attempted private equity buyout of Qantas Airways by a consortium that included Macquarie Bank and Alco Finance. The bid was premised on indefinitely cheap debt financing costs, and indefinitely expanding air
travel. The bid collapsed, albeit by a whisker, in May 2007. A successful takeover would have burdened Qantas with intolerable debt financing commitments (an $11 billion takeover based on $10 billion of debt), with subsequent bankruptcy a certainty (Schwab, 2009a).

BrisConnections was a trust floated in July 2008 by joint underwriters Macquarie and Deutsche Bank at the behest of the Queensland Labor Government. Its function is to preside over the building of three arterial roads out of Brisbane, particularly an airport link. BrisConnections is an exemplar of cynical and dysfunctional financial imperatives in the provision of infrastructure. The largest float of the year, at $1.2 billion, failed spectacularly, predictable given the adverse environment. 400 units were offered at $3, spread over three instalments. The $1 listing immediately fell to 41c. Macquarie, which had extracted $110 million in fees for the listing, ended up with 26% through various vehicles, which it proceeded to sell down, with the units tumbling to 1c. Ill-informed scavengers picked up truckloads of the 1c. units, ignorant of the further two calls at $1 in the fine print. Chaos has ensured, with attempts to wind up the company, an attempt by Macquarie to cancel the small fry’s obligations, and attempts to pursue the small fry to the last drop of their blood. The conflicted Chairman of BrisConnections was also Chairman of BrisConnections equity holder (about 10%) Queensland Investment Corporation, until pressured to quit the latter role in September. Rowe had made improbable revenue projections. Dividends were to be initially paid out of borrowings. Meanwhile, big name banks were lined up to provide $3 billion in debt; but, having been hit by the crisis, many want out. The Queensland government refuses to bail out the project. In short, it has been a debacle.

Finally, there is the fault line in that major buttress of the Australian finance sector, the superannuation industry. The crisis-driven decline in returns has amplified longstanding criticism of the fees rort that permeates the compulsory superannuation regime in Australia. The central problem is that fees have been appropriated as a percentage of the client’s assets. There is no necessary relation between fees and quality of service and client returns. Large funds have performed more poorly than smaller funds, in spite of presumed scale economies. For-profit retail funds charge generally in the range of 1-2% of assets, whereas industry
(i.e. union-sponsored) funds charge generally in the range of 0.5-1% of
assets. Moreover, the former have performed worse than the latter;
nevertheless, both systems have in common an asset-based fee structure.
There is a round-robin relationship between lower return for-profit retail
funds, the large banks and insurers as dominant owners of the funds,
commission-based advisers, and the direction of clients by such advisers
to in-house funds (Keane, 2009). There is a marked lack of transparency
of the total fee cost to clients of their superannuation assets. The
regulators’ sole concern to date has been to enhance transparency of
information rather than to address the scale and character of fees per se.11

Behind this series of misfortunes are key dimensions of the Australian
financial environment. The abundant pool in which predators flourish is
fed by at least three factors. The first factor is the compulsory
superannuation scheme. As at June 2009, superannuation funds stood at
an estimated $1,076.7 billion.12 The figure reached $1.2 trillion by June
2007,13 so the crisis has knocked over $100 billion off the total, but the
pile grows inexorably – an estimated $70 billion each year, amongst the
fastest in the world.14 Neglected is the nature of the outlets for this
endless flow. Are there sufficient materially productive investments to
absorb the capital? The answer clearly is no, with expanding capital
serving to inflate asset prices, not least of share prices and real
property.15 The super funds thus exacerbate the financial sector’s
contribution to booms and busts.

11 Two other issues mar the integrity and efficiency of the superannuation regime.
First is the widespread practice of ‘flipping’, whereby an employee previously in a
corporate super fund who loses his/her job or moves employment is automatically
moved into accounts with higher fees (Johnston, 2009). Second, the fragmentation
of superannuation payments associated with high job mobility has resulted in
escalating billions sunk into ‘eligible rollover funds’, with small sums being
subject to fees in the range of 3-7% (Anon, 2008).
12 APRA Statistics, Quarterly Superannuation Performance, June 2009.
14 Longtime superannuation journalist Barrie Dunstan, reflecting a recent survey,
remarkably claims that growth per se is an indication of the strength of the
Australian financial sector (Dunstan, 2009). The survey does not distinguish the
separate impact on funds’ asset growth of investment returns and capital inflow.
15 ABS figures, at June 2009, have an estimated $200 billion of Australian managed
funds allocated overseas (down from $275 billion at December 2007), the bulk of
which would be superannuation assets. ABS, cat. no. 5655.0, Managed Funds.
The second and third factors are the pervasive fear (fuelled by propaganda, as in Storm) of the potential inadequacy of personal retirement provision, and the marketing of the so-called democratisation of capital in the neoliberal age (compounded by the privatisation and listing of public infrastructure). These factors have generated waves of financially unsophisticated lemmings as prey to potential and real predation. The series of misfortunes in aggregate point to the spectacular failure of ‘shareholder capitalism’ that has been sold to the public in the last twenty years as the inclusive vehicle both for the security of individual families and the regeneration of the domestic economy in general.

Byproducts of the Financial Crisis

A hardline view of economic crisis is that it desirably ‘cleans out’ the system, with the inefficient falling by the wayside. Rather, crises generally eradicate the less powerful rather than the less efficient. But in this case there have been some worthy corporate deaths. Notable and deserving failures were ABC Learning, Allco Finance and Babcock and Brown (B&B). Only Allco, as representative, will be summarised here.

Allco was a financial engineer, with B&B a would-be Macquarie Bank copy-cat. Allco and B&B had in common labyrinthine structures of investment trusts, extravagant gearing premised on permanently low interest rates, fee gouging from these satellites, and executives living in opulence. Apart from leasing operations of aircraft and shipping. Allco delved into sub-prime and loc-doc mortgages. Three Allco principals complemented the insouciance of the attempted Qantas buyout with the late 2007 sale of their predominantly privately-held Rubicon Holdings (property trusts operating in Japan, Europe and the US) to Allco itself at the vastly inflated sum of $277 million; $64 million in cash was extracted by the threesome. Rubicon had previously been inflated with debt for the purchase of over-valued real estate, from which the same

(Footnote 15 continued): Note that ABS figures understate superannuation assets compared to APRA figures. Capital invested overseas, in the face of competition with global superannuation capital in pursuit of finite productive outlets, also tends to push up asset prices and compound the boom/bust cycle.

Macquarie Bank itself survives and is reinventing itself. Its share price has recovered from $15 in early March 2009 to safely over $50 in September, not least because it was saved from hedge fund predation by the banning of short selling by ASIC in September 2008 and it raised almost $12 billion (to mid-September 2009) in capital under the Government’s bank guarantee. But the model by which it became the fabled ‘fee factory’ or ‘millionaire’s factory’ is dead. Macquarie bought infrastructure assets, loaded them into satellites with substantial debt acquired at historically low rates, from which were appropriated a full range of fees. Assets were revalued upwards, and fees increased for ‘enhanced’ management performance. With revenues delayed, dividends were often paid from new investors’ capital.16

The model had its built-in use-by date. Revenues started to fall, and the bank faced ‘a mass exodus of investors from the debt-laden vehicles’ (Verrender, 2009d). Some satellite share prices had fallen dramatically, facing increasingly critical analyst ratings. There followed share buybacks, asset sales (albeit some early sales were to related parties) and asset devaluations, with both Head Office and satellite management opting for separation. Even a jewel in the crown, Macquarie Airports, is to be separated. But Macquarie is extracting a spectacular pound of flesh in the form of a $345 million payment for the buyout of management rights – this after pulling out over $520 million in management and performance fees since MAp’s listing in 2002, part of a total estimated fee extraction of $940 million (Verrender, 2009f). The majority non-Macquarie security holders apparently felt blackmailed with the need to avoid a hostile dissolution of the complex relationship (Bartholomeusz, 2009b). The payment was approved at a 30 September meeting, albeit against a strong protest vote – a rich nightcap sayonara to the Macquarie model.

16 In late June 2009, Macquarie ‘… announced it no longer would be paying dividends from debt, and made the radical suggestion that in future it would be a better idea if dividends reflected earnings’ (Verrender, 2009d).
In terms of the financial dimension, the most substantial adverse effect of the crisis has been the concentration of power in the banking sector. The dominance of the ‘big four’ banks in Australia is without precedent. The big four monopolised new mortgage issuance during 2009 (Drummond & Bührer, 2009). Starting life as (specialist) trading banks, the now allfinanz institutions have swallowed up finance companies and savings banks, and their reach now extends to investment banking, insurance, wealth management and stock broking.

The spectacular rise of mortgage brokers on debt funding and asset securitisation was perhaps destined to be checked. Unexpected was the extent to which the Rudd Government and the regulators were prepared to foster greater big four dominance. The Government early proposed (following NAB pressure) creation of an Australian Business Investment Partnership to subsidise the big four’s ongoing exposure to the overblown commercial property sector – a proposal fortunately rejected in the Senate.17.

The Government introduced a bank deposits and capital raising guarantee in October 2008. The big four banks, with AA ratings, have to pay an extra 70 basis points (i.e. 0.7%) for access to guaranteed capital, but the second tier (and credit unions, etc.), with lower ratings, have to pay an extra 100 to 150 basis points. To mid-September, the big four plus Macquarie Bank had raised $94 billion in debt under the guarantee. The smaller banks have been complaining about the unlevel playing field without effect. A recent Parliamentary inquiry and report has recommended that the Government redress the imbalance (Senate Economics References Committee, 2009). However, the biggest sop to the big four has been the regulatory support of takeovers and the subsequent consolidation of market power. The ACCC under Chairman Allan Fels tolerated Westpac’s takeover of Western Australia’s Challenge Bank in 1995 and the Bank of Melbourne in 1997 (both ex-Building Societies), and the privatised CBA’s takeover

17 The federal government’s public sector superannuation Future Fund has also plunged significantly into bank debt securities, enhancing bank liquidity (Yeates, 2009a). This development may be strictly commercially-driven, but it is not improbable that it is a strategic backdoor mechanism of further propping up major bank balance sheets.
of Colonial in 2000. In late 2008, the ACCC under Chairman Graeme Samuel and the federal Treasurer, Wayne Swan, approved Westpac’s takeover of St. George and the CBA’s takeover of BankWest. Swan talked of the need for stability and the ACCC maintained that competition would not suffer. The claims were fatuous (Jones, 2009). The loss of an independent St George, in particular, is a scandal. St George, partly by the takeover of fellow ex-building society Advance Bank in 1997, had transcended its second tier status, and was threatening the cosy world of the big four, especially in small business lending (Jones, 2008a).

Market power has been readily translated into higher margins. The market power not sighted by the competition regulator has been explicitly flagged by analysts and explicitly welcomed by the banks themselves. UBS analyst Mark Rider recommended buying (big) bank stocks because of the ‘structural change’ going on: ‘What they are doing is they are getting pricing power; they are widening margins’ (Washington, 2009; Gluyas, 2009). Bank executives talk about the necessity to re-price risk, but profitable companies talk about arbitrary hikes in their conditions. Small and medium enterprises have been hard hit in terms of access to credit and its pricing (Fenton-Jones, 2009). In effect, the big four banks are now utilising ‘administered pricing’, available only to those with unrequited market power, in which a desired profit rate or mass is determined, and products are priced accordingly. Return on equity might fall, as in 2007-08, but the retreat is minor. The rest of the economy, heavily dependent on the big four, pays the price.

Several vignettes highlight the asymmetry of the banking relationship. In February 2009, the (mostly) clothing manufacturer Pacific Brands announced seven plant closures in Australia and New Zealand, and the retrenchment of 1850 and almost 100 workers respectively. Reports were clouded by questions regarding sustainability of the company’s product diversity, and why any company was manufacturing anything in Australia. But the immediate force behind the retrenchments was Pacific Brands’ banking cabal, which wanted rapid repayment of debt, higher

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18 Colonial was, in turn, the product of a giant insurer, Colonial Mutual, turned bank, and its subsequent takeover of the State Bank of NSW.
rates and tightened covenants. The normally priggish journalist Elizabeth Knight commented (Knight, 2009):

Being subject to this trifecta of onerous bank conditions suggest pretty clearly that the banks are calling the shots. … Banks now have legions of operatives calling the shots behind the scenes, taking control of corporate strategies in order to avoid having even larger bad debt provisioning.

An even more striking manifestation of the same phenomenon is the forced sale of prime assets by Australia’s third largest mining company OZMinerals. The equally conservative journalist Robert Gottliebsen was appalled (Gottliebsen, 2009):

… Australian superannuation funds and other investors in OZ Minerals are being taken to the cleaners. They are being asked to approve the sale of prime, highly profitable mineral assets to the Chinese owned Minmetals group at a fraction of their worth. …

The 2009 OZ Minerals disaster is simply about deplorable banking. … OZ Minerals owes local and foreign banks about $A1.2 billion and the company is generating cash in excess of $300 million a year. The total value of the OZ Minerals assets is several times the amount owing to the banks so these are loans covered by cash flow and asset values. However, the bank chief executives are effectively telling OZ Minerals shareholders that unless they sell key OZ Minerals mining assets to the Chinese at a fraction of their worth then "we will pull the plug on the company and effectively ruin you by flogging the assets off at low prices". … We are handing the Chinese an immediate paper profit of $US400 million simply because of bad banking.

Both Pacific Brands and OzMinerals have complex histories, and they had expanded debt by acquisitions. But the banks were supportive parties to these acquisitions and debt expansion, and have shown that the relationship, presumed to display mutual concern for long term viability,

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19 A similar process occurred at PaperlinX with the company forced by its bank to divest paper manufacturing assets at under value to Nippon Paper (McIlwraith, 2009).
is merely one of expediency. The lesson is clearly that he who sups with the devil must have a long spoon. Australian banks simply cannot be trusted.

**Weaknesses in the Regulatory Agencies**

The regulatory agencies each have their own problems. The Reserve Bank has been reduced to a single policy instrument – the overnight cash rate. The RBA raised the cash rate by 0.25% on 12 successive occasions, between May 2002 and March 2008, the rate rising from 4.25% to 7.25%. The most sustained rises were in the 3-year period from March 2005, the rate rising from 5.25% to 7.25%. By the standards of the appallingly high rates of the 1980s, these rises seem relatively benign. Yet the country was facing asset price inflation, and the cash rate is unsuitable to the task. Variation of the cash rate has no positive impact on asset bubbles – indeed, it may even exacerbate them (Jones, 2007). Housing price rises are a complex story in their own right, not least because owner occupation has such a strong impulsion. Myriad desperate home-owners have been pincered by intolerable house prices, rising interest costs and subsequent under- or unemployment.

Recently, with enhanced bank debt sourced globally, even bank lending rates have become detached from the cash rate. There seems little chance of the RBA acquiring additional instruments to offset the current dysfunctionality of monetary policy. The elaborate research output of RBA staff points to mere hiccups, emphasising overall stability. The RBA’s herculean indifference, embodied in its biannual *Financial Stability Review*, is based on its benchmarks for ‘genuine’ crisis being the calamities of the early 1990s recession in Australia and current calamities overseas.

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20 The RBA’s previous Governor, Ian Macfarlane, had made subdued statements along these lines, but both he and his successor (since September 2006), Glenn Stevens, have carried on with the blunt cash rate mechanism regardless. Curiously, Macfarlane is quoted as claiming that giving the RBA powers to target asset prices “… was unlikely to be accepted by the community and therefore would not be achievable at least for the next decade.” (Kehoe, 2009). The first part of this claim is spurious.
The Australian Prudential & Regulatory Authority essentially administers Bank of International Settlements standards on prudential capital holdings – the primary product of the ‘hands off’ ersatz regulation at the centre of the globally deregulated financial system. APRA has received much credit for the mildness of the Australian crisis. Yet much of the substantial capital raised by the big four under the government’s guarantee scheme, and at unsavoury haste (offered at discount and privileging the institutions over individual shareholders) highlights the unsatisfactory character of the BIS/APRA regime. APRA also formally monitors bank bad debts but declines to intervene in bank practices (in spite of formal powers) to redress the culture that generates them.

The real failure of APRA (and of the BIS model) has been with regard to bank wholesale debt (and equity/debt hybrid capital). As at June 2009, deposits constituted only 60% of the liabilities of Australian-based banks associated with domestic operations (totaling $2,272 billion). 15.2% ($346 billion) of such liabilities were due to non-residents. The debt erected on customer deposits is a natural consequence of the transformation of Australia’s core banks from trading banks to allfinanz institutions. Timely re-financing of this debt (and on reasonable terms) is fundamental to Australian bank liquidity, in turn more fundamental to systemic stability than are capital ratios. Bank liquidity risk was precisely why the Government established the bank guarantee while hiding the reason – the guarantee provides prima facie proof that the APRA monitoring structure is inadequate.

21 APRA was created in 1998 when the prudential monitoring role for Deposit Taking Institutions was carved out of the RBA.
22 In particular, APRA has been praised for several ‘stress tests’ of ADI’s, especially in raising the capital requirements for higher risk housing loans in 2004 (Reserve Bank of Australia, 2009: 21).
23 The NAB, in particular, was under-capitalised. It raised $11 billion in the 12 months to September 2009, roughly one-third of its then capitalisation. Although some of this capital has been fuel for further acquisitions, the NAB was forced by the UK Financial Services Authority to allocate £1.4 billion pounds in extra capital to its UK subsidiaries (over three tranches in October 2008 and February and May 2009). The NAB has consistently misled the market on the extent of its bad debts and on its capital raisings.
The Australian Securities & Investments Commission is the predominant financial services regulator. The ASIC Act requires the Commission to ‘promote confident and informed participation by investors and consumers in the financial system’. Australia does not enjoy such a situation, so who or what is to blame? Reasonably, ASIC can only investigate a small proportion of the thousands of complaints it receives each year. The scale of the problems is an issue, even with 1,200 staff, and the expense of major actions is prohibitive. For example, in late 2007 ASIC initiated action against principals, financial advisers and KPMG auditors associated with the property empire Westpoint and its collapse in late 2005. ASIC finally achieved a ban on auditors in August 2009 and compensation against one advising firm in September. After four years ASIC is still dealing with earlier malpractice in the financial products sector, and with none of the penalised parties admitting culpability. But how was Westpoint (and its comparators Fincorp and Australian Capital Reserve) able to achieve the scale and wreak such damage in the first place?

ASIC had previously had complaints about Storm’s founder, Emmanuel Cassimatis, and Storm Financial, but it claims (minor) problems were resolved following ‘routine ASIC surveillance in Queensland on financial planners’ (Australian Securities & Investments Commission, 2009: 14). ASIC decided to investigate Storm only in late December 2008 after it had collapsed. ASIC ought to have scrutinised the Storm model when Storm submitted operational details in November 2007 preparatory to a proposed public listing, a proposal that could find no underwriting brokers. Everything about the Storm model oozes fraudulence. The ASIC submission to the Parliamentary Storm inquiry simultaneously denies regulatory failure, insists that ASIC has been vigilant, yet claims that it has been dramatically restricted by an inadequate legislative brief.

ASIC’s difficulties demand to be seen in the light of its treatment of its legislative responsibilities for unconscionable conduct in financial services. ASIC acquired such responsibility with respect to retail clients in July 1998 and small business clients in August 2001, operative in March 2002. A decade of research and advocacy by this author has highlighted that unconscionable conduct by major banks against small
business clients is endemic. Admittedly, the hurdle in the courts to winning a business to business unconscionability suit is formidable. Nevertheless, ASIC has mounted no case in this domain, nor has it lobbied regarding surmounting of the presumed judicial hurdles. Rather, it has variously denied responsibility, and responded to small business complainants that it will not pursue the matter, misrepresenting to them that it has examined closely their situation (Jones, 2008b).

ASIC, as with its institutional predecessors, was born with a regulatory emphasis on enhancing disclosure and transparency in the financial marketplace, and has acquired a dominant culture that underpins that emphasis. ASIC has yet to acquire a culture commensurate with the cowboy frontier environment that it is expected to regulate.

Finally, the Australian Securities Exchange as a profit-oriented publicly-listed monopoly is structurally incapable of adequately enforcing its formal responsibility for stock listing probity. In September, ASIC’s ‘annual report card’ to the ASX listed 13 areas where enforcement procedures had been inadequate (Williams, 2009). ASIC queried whether the ASX’s listing criteria was too lenient, asking whether ‘particular business models are suitable for listing on the ASX’s market’. ASIC was particularly critical of ASX’s neglected gate keeping over the BrisConnection listing debacle.

ASIC’s concerns are valid, but the ASX’s failings are linked to the weaknesses of the accuser itself. Journalist Ian Verrender makes the point (Verrender, 2009e):

ASIC has hardly covered itself in glory in recent years. It is slow to react, if it bothers to react at all. It has an appalling record on charging miscreants, let alone getting convictions. And it always goes for the easy target – individuals, and not-so-powerful individuals at that. Investigations of corporate collapses are now left to receivers and liquidators. Litigation funders such as IMF are more effective than our corporate watchdog in extracting penalties from the big end of town … Last year, the ASX handed ASIC 31 referrals on insider trading and 14 cases of market manipulation. Whatever happened to them? Or the ones that were referred to ASIC the
previous year? ASIC is a mixed metaphor lover's dream – a lame-duck watchdog.

In short, we have a massively staffed but fragmented regulatory apparatus – partly steeped in automaton-like application of narrowly devised rules, partly mired in passivity punctuated by belated action to clear up the mess.

Crisis-Induced Regulatory Changes

The crisis has induced some changes and the promise of others. In mid-September 2009, APRA recommended stronger liquidity provisions for banks, in effect a revamping of the 1960s ‘liquid and government securities’ requirement. The measures include a narrowing of what assets can be so classified, and the lengthening of the liquidity coverage period from 5 to 30 days (Glynn, 2009).

In August 2009, the Government foreshadowed removal of the ASX’s regulation of market traders to ASIC and has given ASIC powers to directly investigation insider trading (Verrender, 2009e). In October, the Government foreshadowed a disclosure regime for stock short selling, to be monitored by ASIC.

Of substantial formal importance is the Government’s attempt to move all regulation of consumer credit to the federal level. Formerly the States and Territories’ Uniform Consumer Credit Code regulated consumer credit but not credit for investment purposes. Under the National Consumer Credit Protection Bill, introduced into Parliament on 25 June 2009 and pending its delayed implementation in July 2010, all credit providers will be subject to a consistent licensing regime (although it is not clear how this differs to the present), and lending for investment in residential property will be regulated.25 The Corporations Legislation Amendment (Financial Services Modernisation) Bill 2009 will ensure coverage of margin loans under the Corporations Act as a financial product.

25 Subsequent amendments will generalise regulation of consumer borrowing for investment purposes.
This legislation will bring new formal responsibilities within ASIC’s purview, but will there be a qualitative regulatory transformation? ASIC has claimed that margin loans as credit were already covered under the ASIC Act (Australian Securities & Investments Commission, 2009: 88), but it does not explain why its coverage of this innately dangerous facility remained inoperative.

There is a pervasive ambivalent tone to the ASIC submission to the Storm inquiry. It tacitly acknowledges the retail investments sector as corrupted, yet it refers merely to ‘potential [my emphasis] systemic issues that have arisen in relation to the role played by lending institutions in recent retail investor losses’ (p.87), and generalises early ‘that the current standards in the advice industry are adequate’ (p.37). ASIC only weakly recommends that the government consider legislating for fiduciary duty, while noting its existence in jurisdictions overseas that Australia regularly takes as models. The new legislation will not impose a fiduciary duty of care on financial advisers, a major weakness.

The scale and character of the Storm debacle was fundamentally dependent on intimate CBA involvement. But the prospect is that ASIC will fail to include the CBA in any culpability and compensation in the case against Storm Financial being pursued in the Federal Court. Late in a large submission ASIC summarises the reigning ethos (p.181):

However, the basic philosophy of the Australian financial services regime is that any product can be sold to any investor provided the nature of the risks, fees, etc. are disclosed. In this context, ASIC’s role is to oversee and enforce compliance with the conduct and disclosure rules enacted in the Corporations Act. The regime relies on market participants to comply with the law and places the onus for assessing risk on the investor.

ASIC does make straightforward recommendations to eradicate the corrupted financial ‘advisory’ remuneration structures (p.53). The Government has established an inquiry (under previous ASIC Deputy Director Jeremy Cooper) into superannuation funds management. But Cooper’s record at ASIC has not been illustrious, and the forces mitigating against substantial change are powerful. The industry ‘professional’ associations, essentially lobby groups, have been
unrepentant in defense of the status quo – the Investment and Financial Services Association26, the Association of Superannuation Funds of Australia27, the Financial Planning Association28, and the Association of Financial Advisers.

A qualitative regulatory transformation requires not merely statutes but aggressive enforcement and cultural change. ASIC Chairman, Tony D’Aloisio, is gradually assuming a more interventionist stance.29 D’Aloisio has attacked the systematic failure of ‘intermediaries’ – auditors and credit rating agencies as well as financial advisers. Delay is inevitable, partly because of the need for international cooperation, but partly because of the complexity of prospective reform of deeply compromised institutions whose member companies remain belligerent in the face of their own crucial contribution to the crisis (Drummond, 2009). The prospect is for a long wait for a transformation of substance beyond rhetoric.

Conclusion

A rational examination of the evolving forces leads one to conclude that regulatory reform in the financial services sector will be substantively marginal. The new dominance of the big four banks as allfinanz conglomerates has been legitimised in the political and regulatory arenas. The banks’ leverage to extract booty from their customers has been enhanced. The dimensions of their operations that embody recklessness, incompetence and unconscionability will go unchecked. At the other end of the spectrum, the bottom feeders will continue to spawn and wreak

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26 An IFSA sponsored report in late September by Deloitte notes higher costs for funds under management in Australia than overseas, but claims that the costs are due predominantly to more active and higher-return oriented management than comparators overseas, and to regulatory compliance costs.
27 ASFA has recently lobbied to deter government support for retirement savings options other than the superannuation system (Patten, 2009).
28 Under pressure, the FPA announced in October a recommendation to members that commission-based payments end after July 2012.
29 D’Aloisio was appointed Chairman in May 2007 to replace his do-nothing predecessor, Jeffrey Lucy.
havoc on the gullible. Every reform proposal has been opposed by the vested interests, with proposals delayed, compromised or abandoned.30

In the not too distant future, a new generation of independent parliamentarians will force Parliamentary committees of inquiry, whose recommendations will be watered down or not acted upon. And the cycle will continue, with previous crises and their cast of villains lost to memory.

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30 ASIC attempted in July 2008 to raise the monetary limit to $280,000 for compensation against financial planners, but retracted following an industry backlash – ASIC is now trying again (Yeow, 2009). Big business and its supportive law firms are engaged in ongoing lobbying to emasculate consumer credit reform, their first success being the excision of any inclusion of small business concerns from consideration.


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WOMEN'S EARNINGS SECURITY IN A CONTEXT OF ECONOMIC CRISIS

Therese Jefferson and Alison Preston

There are likely to be important gender differences in both the short and long term effects of economic downturns (ILO, 2009; Tutnjevic, 2002). Typically the differences are attributable to three contrasts between the working lives of men and women. Firstly, women are traditionally over represented in casualised workforce sectors that are relatively less regulated and susceptible to changes in working hours and employment conditions. Secondly, men and women are concentrated in different industries and occupations and therefore the gender effects of a change in economic conditions differ according to the effects on specific sectors of the economy. Thirdly, women in Australia and many other societies undertake a disproportionately large amount of unpaid household work. Economic conditions which result in reduced public expenditure on service provision can increase the demands on household unpaid labour to make up the shortfall. These contrasts mean that government policies aimed at stimulating the economy can have different implications for men’s and women’s employment, depending on which sectors are targeted for government expenditure and support. Policies focused on physical infrastructure such as buildings may have a more positive effect in traditionally male industries (Richardson, 2009).

The conventional wisdom, backed by a large and growing research literature suggests that part-time workers in low paid industries are likely to be among the first casualties in an economic downturn (Seguino, 2009). Not only are they likely to lack negotiating power; they are also likely to have relatively low levels of accumulated assets to draw upon if they lose their jobs. These general patterns can differ, however, depending on specific combinations of social, industry, occupational and
government policy responses to an economic downturn. The sudden and steep economic crisis in Australia since September 2008 is a good example of the way in which actual developments in women’s employment and official data may differ from the experiences of past recessions.

In this article we review official Australian data on women’s employment, earnings and wealth immediately preceding and after September 2008. The data show that, while patterns of employment and earnings appear, superficially, to demonstrate that women are faring comparatively well there are also indications that there are serious short and long term challenges for women in the Australian labour market. This has serious implications for policy and for the growing number of men who are facing patterns of employment that were once more strongly associated with feminised workforces.

**Employment Patterns Preceding September 2008**

At July the 2008 labour market participation reached 65.4 per cent, comprised of a female participation rate of 58.6 per cent and a male participation rate of 72.5 per cent (ABS, 2009d, trend estimates). Strong participation rates were partly driven by increasing demand for labour, but were also underpinned by demographic effects such as changed social norms and an ageing population (Austen and Seymour, 2006). At October 2008, for example, of all women in the labour force aged 20 plus, women aged 45 or more accounted for 39.8 per cent. In 1991 the corresponding share had been 24 per cent. The majority of women in this age group are engaged in part-time employment.

During the years prior to September 2008 there also was a sustained trend towards growth in the part-time labour market. This appears to reflect an employer preference for more flexible forms of labour and a growing use of non-standard forms of employment (part-time, temporary, casual). In the eight years to October 2008 part-time employment grew by 26 per cent. By October 2008 more than two million women were employed part-time and more than 73 per cent of all part-time jobs were held by women (ABS, 2009d). This is closely linked
with the varying concentrations of men and women in different industries. Retail trade, accommodation, cafes and restaurants and cultural and recreational services are relatively feminised industry sectors and have high rates of part-time employment. Employees in these sectors also receive relatively low pay.

**Employment Patterns since September 2008**

The key labour market indicators since September 2008 are consistent with the patterns expected during an economic downturn. There has been an increase in the unemployment rate from 4.3 per cent in September 2008 to 5.8 per cent in September 2009 and a growth in part-time employment (up by approximately 159,000) compared to a drop in full-time employment by approximately 175,700. However, while unemployment has increased, labour market participation does not appear to have changed significantly. Total labour force participation was 65.4 per cent in September 2008 and the latest figures, for September 2009, are 65.1 per cent. Female participation initially rose during this period, reaching a new high of 58.8 at February 2009. By September 2009 it had fallen to 58.4 per cent, while male participation declined from 72.4 to 72.1 per cent (see Tables 1a and 1b on the following two pages).

Throughout 2008 the unemployment rate among women was higher than men. However, if we focus firstly on unemployment among those looking for full-time work, in column 5 (Table 1a and 1b), there are two key features. Since September 2008, unemployment among men looking for full-time work has grown by 2.3 percentage points, from 3.6 per cent to 5.9 per cent per cent, a faster rate than among women (which increased by 1.7 percentage points from 5.0 per cent to 6.7 per cent). However, men’s full-time unemployment rate has not yet overtaken women’s. In terms of the overall unemployment rate (which includes those looking for either full-time or part-time work, as shown in column 6), a somewhat different pattern is observable: women had a higher rate of unemployment before the downturn. Higher rates of growth in unemployment among men mean that men are now experiencing higher levels of unemployment.
Secondly, labour force participation rates among men and women are moving in opposite directions. Men’s participation rates have been falling from 72.4 per cent in September 2008 to 72.1 per cent in September 2009. A decline in participation rates might be attributed to people discontinuing their job search as they become discouraged in a labour market with relatively fewer opportunities; this is known as the ‘discouraged worker effect’. For example, people may decide to retire early or return to education rather than seek employment. This type of pattern is typically associated with a downturn in the labour market. However, it is noteworthy that women’s participation rates rose during 2009, reaching a new peak at 58.8 per cent during the May 2009 quarter.

Table 1a: Selected Indicators of Male Labour Force Status: September 2008 – September 2009, Australia

<table>
<thead>
<tr>
<th>Month/Year</th>
<th>Employed full time ‘000</th>
<th>Employed part time ‘000</th>
<th>Employed total ‘000</th>
<th>Unemployment rate looking for full-time work %</th>
<th>Unemployment rate %</th>
<th>Participation rate %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sep-08</td>
<td>5041.4</td>
<td>871.5</td>
<td>5913.0</td>
<td>3.6</td>
<td>4.0</td>
<td>72.4</td>
</tr>
<tr>
<td>Oct-08</td>
<td>5035.2</td>
<td>875.7</td>
<td>5911.0</td>
<td>3.8</td>
<td>4.1</td>
<td>72.4</td>
</tr>
<tr>
<td>Nov-08</td>
<td>5022.0</td>
<td>883.1</td>
<td>5905.0</td>
<td>4.0</td>
<td>4.3</td>
<td>72.3</td>
</tr>
<tr>
<td>Dec-08</td>
<td>5003.6</td>
<td>892.4</td>
<td>5896.0</td>
<td>4.3</td>
<td>4.6</td>
<td>72.3</td>
</tr>
<tr>
<td>Jan-09</td>
<td>4983.1</td>
<td>901.8</td>
<td>5884.8</td>
<td>4.6</td>
<td>4.9</td>
<td>72.3</td>
</tr>
<tr>
<td>Feb-09</td>
<td>4961.8</td>
<td>910.7</td>
<td>5872.5</td>
<td>5.0</td>
<td>5.2</td>
<td>72.3</td>
</tr>
<tr>
<td>Mar-09</td>
<td>4941.5</td>
<td>919.7</td>
<td>5861.2</td>
<td>5.3</td>
<td>5.5</td>
<td>72.2</td>
</tr>
<tr>
<td>Apr-09</td>
<td>4925.2</td>
<td>928.8</td>
<td>5854.0</td>
<td>5.6</td>
<td>5.8</td>
<td>72.2</td>
</tr>
<tr>
<td>May-09</td>
<td>4914.9</td>
<td>937.1</td>
<td>5852.0</td>
<td>5.7</td>
<td>5.9</td>
<td>72.2</td>
</tr>
<tr>
<td>Jun-09</td>
<td>4909.1</td>
<td>945.1</td>
<td>5854.3</td>
<td>5.8</td>
<td>6.0</td>
<td>72.2</td>
</tr>
<tr>
<td>Jul-09</td>
<td>4905.9</td>
<td>953.1</td>
<td>5859.0</td>
<td>5.9</td>
<td>6.0</td>
<td>72.1</td>
</tr>
<tr>
<td>Aug-09</td>
<td>4904.6</td>
<td>960.6</td>
<td>5865.2</td>
<td>5.9</td>
<td>6.0</td>
<td>72.1</td>
</tr>
<tr>
<td>Sep-09</td>
<td>4905.8</td>
<td>966.4</td>
<td>5872.1</td>
<td>5.9</td>
<td>6.0</td>
<td>72.1</td>
</tr>
</tbody>
</table>

Table 1b: Selected Indicators of Female Labour Force Status: September 2008 – September 2009, Australia

<table>
<thead>
<tr>
<th>Month/ year</th>
<th>Employed full time ‘000</th>
<th>Employed part time ‘000</th>
<th>Employed total ‘000</th>
<th>Unemployment rate- looking for full-time work %</th>
<th>Unemployment rate %</th>
<th>Participation rate %</th>
</tr>
</thead>
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<tr>
<td>Sep-08</td>
<td>2705.5</td>
<td>2184.1</td>
<td>4889.6</td>
<td>5.0</td>
<td>4.6</td>
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<tr>
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<td>4895.5</td>
<td>5.1</td>
<td>4.7</td>
<td>58.5</td>
</tr>
<tr>
<td>Nov-08</td>
<td>2694.5</td>
<td>2207.4</td>
<td>4901.9</td>
<td>5.2</td>
<td>4.7</td>
<td>58.5</td>
</tr>
<tr>
<td>Dec-08</td>
<td>2693.3</td>
<td>2215.2</td>
<td>4908.5</td>
<td>5.3</td>
<td>4.8</td>
<td>58.6</td>
</tr>
<tr>
<td>Jan-09</td>
<td>2696.8</td>
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<td>5.5</td>
<td>5.0</td>
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</tr>
<tr>
<td>Feb-09</td>
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<td>4921.8</td>
<td>5.7</td>
<td>5.2</td>
<td>58.8</td>
</tr>
<tr>
<td>Mar-09</td>
<td>2709.3</td>
<td>2216.9</td>
<td>4926.2</td>
<td>5.9</td>
<td>5.3</td>
<td>58.8</td>
</tr>
<tr>
<td>Apr-09</td>
<td>2710.0</td>
<td>2217.6</td>
<td>4927.6</td>
<td>6.1</td>
<td>5.4</td>
<td>58.8</td>
</tr>
<tr>
<td>May-09</td>
<td>2704.9</td>
<td>2221.3</td>
<td>4926.2</td>
<td>6.3</td>
<td>5.5</td>
<td>58.8</td>
</tr>
<tr>
<td>Jun-09</td>
<td>2695.5</td>
<td>2227.5</td>
<td>4923.1</td>
<td>6.4</td>
<td>5.5</td>
<td>58.7</td>
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<tr>
<td>Jul-09</td>
<td>2685.0</td>
<td>2234.6</td>
<td>4919.6</td>
<td>6.5</td>
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<tr>
<td>Aug-09</td>
<td>2675.1</td>
<td>2241.1</td>
<td>4916.2</td>
<td>6.6</td>
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<tr>
<td>Sep-09</td>
<td>2665.5</td>
<td>2248.4</td>
<td>4913.9</td>
<td>6.7</td>
<td>5.5</td>
<td>58.4</td>
</tr>
</tbody>
</table>


By September 2009 the female participation rate had again declined to 58.4 per cent (as shown in Table 1b above). These trends are worthy of further comment.

Mainstream economic theory predicts that individual labour supply is largely determined by market wages. Higher market incomes are expected to motivate individuals to enter the labour market or to increase the number of hours in which they participate in paid work. However, it has long been recognised that the issue of women’s labour supply is more complex than this simple model would imply. Women’s unpaid work within households and the influence of a partner’s earnings on her
labour market participation decisions contribute to relatively complicated models and empirical research with ambiguous findings and predictions (Birch, 2005). However, rising participation rates are an outcome that contradicts the discouraged worker effect in a declining job market and at this stage we can only speculate on the possible causes. One possible reason is that women are entering the labour market in an attempt to add to household incomes as men’s labour market opportunities falter – labelled the ‘added worker effect’. In addition, historically high household debt levels and the need to meet ongoing commitments, such as mortgage and credit card repayments, comprise one possibility that is consistent with previous research linking women’s labour market participation with mortgage repayments (Birch, 2005: 72). Reserve Bank of Australia data show that declining asset values also increased households’ debt to asset ratios after September 2008 and household debt to income ratios remained relatively high, falling from a peak of 159.3 percent in March 2008 to 155.6 percent in June 2009 (RBA 2009).

Rapidly falling asset values – and women’s lower average levels of accumulated assets – may also mean that women have less opportunity to choose retirement as an option in the current climate (ABS, 2008b). It is also possible that there may be linkages between procedures and entitlement provisions for access to social security and labour force participation decisions. In particular, the receipt of redundancy payments and holding of liquid assets are linked with waiting periods for entitlement to social security benefit tests which might also increase the motivation for women to increase their employment to maintain incomes in households where a partner has lost employment.

However, there is little in the existing literature that provides insight into this issue (Birch, 2005). The outcome is that, despite lower interest rates and a lower ratio of interest repayments to household income, the added worker effect appears to have negated any expected discouraged worker effect among women workforce participants.

Table 2 on the following page shows the trends in full-time, part-time and total employment and monthly percentage changes, by gender. The percentage changes provide a ready guide to the shift away from full-time work to part-time work since late 2008. Amongst men this shift peaked, in particular, during the early part of 2009.
### Table 2: Monthly Change in Full-time and Part-time Employment by Gender, September 2008- September 2009, Australia

<table>
<thead>
<tr>
<th>Month/ year</th>
<th>Monthly change in full time employment %</th>
<th>Monthly Change in part time employment %</th>
<th>Monthly Change in total employment %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Males</td>
<td>Females</td>
<td>Males</td>
<td>Females</td>
</tr>
<tr>
<td>Aug-08 to Sep-08</td>
<td>0.03</td>
<td>0.02</td>
<td>0.03</td>
</tr>
<tr>
<td>Oct-08</td>
<td>-0.12</td>
<td>0.48</td>
<td>-0.03</td>
</tr>
<tr>
<td>Nov-08</td>
<td>-0.26</td>
<td>0.84</td>
<td>-0.10</td>
</tr>
<tr>
<td>Dec-08</td>
<td>-0.37</td>
<td>1.06</td>
<td>-0.15</td>
</tr>
<tr>
<td>Jan-09</td>
<td>-0.41</td>
<td>1.05</td>
<td>-0.19</td>
</tr>
<tr>
<td>Feb-09</td>
<td>-0.43</td>
<td>0.98</td>
<td>-0.21</td>
</tr>
<tr>
<td>Mar-09</td>
<td>-0.41</td>
<td>0.99</td>
<td>-0.19</td>
</tr>
<tr>
<td>Apr-09</td>
<td>-0.33</td>
<td>0.98</td>
<td>-0.12</td>
</tr>
<tr>
<td>May-09</td>
<td>-0.21</td>
<td>0.90</td>
<td>-0.03</td>
</tr>
<tr>
<td>Jun-09</td>
<td>-0.12</td>
<td>0.86</td>
<td>0.04</td>
</tr>
<tr>
<td>Jul-09</td>
<td>-0.07</td>
<td>0.85</td>
<td>0.08</td>
</tr>
<tr>
<td>Aug-09</td>
<td>-0.03</td>
<td>0.78</td>
<td>0.10</td>
</tr>
<tr>
<td>Sep-09</td>
<td>0.02</td>
<td>0.61</td>
<td>0.12</td>
</tr>
</tbody>
</table>

Source: ABS 2009d, Trend series.

The patterns of full-time and part-time work differ considerably between different industries. The latest official release of employment data for specific industries is for the August quarter 2009. Table 3 (on the next page) provides a summary of the composition of the workforce in different industry sectors, by gender and part-time/full-time employment status. It shows the relatively high levels of part-time work occur in relatively feminised industries including retail trade, accommodation and food services, health and social assistance and art recreation services.

Only three industry sectors have above average level of female employment and above average levels of full-time work: financial and insurance services; administrative support and services; and public administration and safety. The remaining industry sectors have relatively male, full-time workforces. There are no industry sectors that have both above average levels of male employment and above average levels of part-time employment, a reflection of the traditional and continuing concentration of part-time work among women.
The significance of part-time employment among women and specific industries imposes important limitations on our understanding of changes in earnings. As will become apparent in the discussion below, available data are more suited to understanding patterns of earning and employment in the full-time workforce.

### Table 3: Composition of Employment by Industry, Gender and Full-time/Part-time Employment Status, Australia, August 2009

<table>
<thead>
<tr>
<th>Industry</th>
<th>Male F-T%</th>
<th>Male P-T%</th>
<th>Female F-T%</th>
<th>Female P-T%</th>
<th>All persons ('000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture, forestry and fishing</td>
<td>59.1</td>
<td>14.8</td>
<td>10.4</td>
<td>15.7</td>
<td>360.3</td>
</tr>
<tr>
<td>Mining</td>
<td>85.2</td>
<td>11.8</td>
<td>1.7</td>
<td>1.4</td>
<td>161.6</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>67.4</td>
<td>18.7</td>
<td>4.6</td>
<td>9.3</td>
<td>1,014.3</td>
</tr>
<tr>
<td>Electricity, gas and water supply</td>
<td>74.9</td>
<td>16.0</td>
<td>5.0</td>
<td>4.1</td>
<td>124.1</td>
</tr>
<tr>
<td>Construction</td>
<td>79.2</td>
<td>5.3</td>
<td>9.3</td>
<td>6.2</td>
<td>967.3</td>
</tr>
<tr>
<td>Wholesale trade</td>
<td>63.8</td>
<td>19.8</td>
<td>5.2</td>
<td>11.3</td>
<td>408.3</td>
</tr>
<tr>
<td>Retail trade</td>
<td>29.4</td>
<td>22.2</td>
<td>14.6</td>
<td>33.8</td>
<td>1,150.2</td>
</tr>
<tr>
<td>Accommodation and food services</td>
<td>23.1</td>
<td>17.9</td>
<td>21.0</td>
<td>38.0</td>
<td>739.6</td>
</tr>
<tr>
<td>Transport, postal and warehousing</td>
<td>65.0</td>
<td>14.3</td>
<td>11.2</td>
<td>9.5</td>
<td>572.3</td>
</tr>
<tr>
<td>Information media and telecommunications</td>
<td>49.7</td>
<td>29.9</td>
<td>9.4</td>
<td>11.0</td>
<td>208</td>
</tr>
<tr>
<td>Financial and insurance services</td>
<td>45.2</td>
<td>37.9</td>
<td>3.8</td>
<td>13.2</td>
<td>390.2</td>
</tr>
<tr>
<td>Rental, hiring and real estate services</td>
<td>39.9</td>
<td>29.9</td>
<td>8.2</td>
<td>22.0</td>
<td>189.5</td>
</tr>
<tr>
<td>Professional, scientific and technical services</td>
<td>49.8</td>
<td>27.7</td>
<td>6.9</td>
<td>15.6</td>
<td>779.3</td>
</tr>
<tr>
<td>Administrative and support services</td>
<td>32.4</td>
<td>28.4</td>
<td>13.9</td>
<td>25.4</td>
<td>350.7</td>
</tr>
<tr>
<td>Public administration and safety</td>
<td>51.3</td>
<td>33.4</td>
<td>3.9</td>
<td>11.4</td>
<td>638.7</td>
</tr>
<tr>
<td>Education and training</td>
<td>23.8</td>
<td>39.2</td>
<td>7.1</td>
<td>29.9</td>
<td>818.5</td>
</tr>
<tr>
<td>Health care and social assistance</td>
<td>16.3</td>
<td>40.0</td>
<td>4.8</td>
<td>38.9</td>
<td>1,212.6</td>
</tr>
<tr>
<td>Arts and recreation services</td>
<td>31.5</td>
<td>20.2</td>
<td>17.4</td>
<td>30.9</td>
<td>192</td>
</tr>
<tr>
<td>Other services</td>
<td>47.3</td>
<td>21.0</td>
<td>9.2</td>
<td>22.5</td>
<td>429.2</td>
</tr>
<tr>
<td>Total</td>
<td>45.5</td>
<td>24.4</td>
<td>9.0</td>
<td>21.1</td>
<td>10,706.7</td>
</tr>
</tbody>
</table>

*Source: ABS, 2009a, Table 2.4 Original Series*
Underutilisation

Growing rates of casualisation mean that unemployment rates do not tell the full story of reduced opportunities in the labour market and labour underutilisation needs to be considered. There are two readily available estimates of labour underutilisation in Australia. One is produced by the Australian Bureau of Statistics. This is a quarterly series providing estimates of labour underutilisation that includes unemployment and part-time workers seeking more hours of work and full-time workers on reduced hours of work. Table 4 shows that these official statistics record reductions in labour underutilisation in the years leading up to August 2008 and sharp increases in the period thereafter.

Table 4: Labour Underutilisation – Australian Bureau of Statistics estimates

<table>
<thead>
<tr>
<th>All persons %</th>
<th>Males %</th>
<th>Females %</th>
</tr>
</thead>
<tbody>
<tr>
<td>August 2004</td>
<td>12.4</td>
<td>10.3</td>
</tr>
<tr>
<td>August 2005</td>
<td>11.3</td>
<td>9.9</td>
</tr>
<tr>
<td>August 2006</td>
<td>11.3</td>
<td>9.5</td>
</tr>
<tr>
<td>August 2007</td>
<td>10.7</td>
<td>8.6</td>
</tr>
<tr>
<td>August 2008</td>
<td>10.3</td>
<td>8.2</td>
</tr>
<tr>
<td>November 2008</td>
<td>11.2</td>
<td>9.2</td>
</tr>
<tr>
<td>February 2009</td>
<td>12.3</td>
<td>10.7</td>
</tr>
<tr>
<td>May 2009</td>
<td>13.3</td>
<td>11.8</td>
</tr>
<tr>
<td>August 2009</td>
<td>13.9</td>
<td>12.6</td>
</tr>
</tbody>
</table>

Source: ABS, 2009a, Catalogue 6105.0 Table 4.1, Trend estimates.

The other data source is the Centre for Full Employment and Equity (CofFEE) at the University of Newcastle which publishes indicators of the degree of labour underutilisation in Australia. In this series, labour underutilisation includes and estimate of potential hours not worked not only by those unemployed, but also part-time workers who wish to work more hours and discouraged workers who wish to work but are not actively seeking employment (the ‘hidden unemployed’). Table 5 (on the next page) reports CofFEE’s most comprehensive labour underutilisation indicator, labelled CU8.
Table 5: CU8 Labour Underutilisation Measures, November 2007 – August 2009, Australia

<table>
<thead>
<tr>
<th></th>
<th>CoFEE U8 %</th>
<th>CoFEE U8 – males %</th>
<th>CoFEE U8 – females %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nov 2007</td>
<td>9.4</td>
<td>7.5</td>
<td>13.6</td>
</tr>
<tr>
<td>Feb 2008</td>
<td>8.7</td>
<td>7.0</td>
<td>12.8</td>
</tr>
<tr>
<td>May 2008</td>
<td>8.9</td>
<td>7.2</td>
<td>13.2</td>
</tr>
<tr>
<td>Aug 2008</td>
<td>9.0</td>
<td>7.2</td>
<td>13.5</td>
</tr>
<tr>
<td>Nov 2008</td>
<td>9.7</td>
<td>7.7</td>
<td>14.1</td>
</tr>
<tr>
<td>Feb 2009</td>
<td>11.3</td>
<td>9.6</td>
<td>15.9</td>
</tr>
<tr>
<td>May 2008</td>
<td>12.2</td>
<td>10.9</td>
<td>16.0</td>
</tr>
<tr>
<td>Aug 2008</td>
<td>12.6</td>
<td>11.2</td>
<td>16.8</td>
</tr>
</tbody>
</table>


Note: Data is seasonally adjusted and rounded to one decimal place.

The CU8 indicator gives a dramatic picture of the extent to which there is a gendered pattern of labour utilisation. While men’s rate of unemployment is growing relatively faster than women’s, high and growing underutilisation rates indicate that many more women than men are working fewer hours of work than they would prefer. This can occur through full-time jobs being converted to part-time jobs or the number of part-time hours being reduced, or through unemployment. An additional factor in the large and growing gender gap in labour underutilisation is that women are more likely to be among the ‘hidden unemployed’. Women undertake the majority of household caring work and are often not entitled to unemployment benefits and therefore not recorded as officially unemployed.

Patterns of Working Hours

Further estimates that provide insights into patterns of employment and working hours are available through the Australian Bureau of Statistics Labour Force Survey data on actual working hours. These data complement and add some detail relevant to underutilisation by showing a reduction in both the number of people employed and the average
number of hours they worked between August 2008 and August 2009. The data show an increase in the percentage of the workforce who recorded working no working hours, from 5.0 to 5.7 per cent for men and 6.0 to 6.4 per cent for women. Similarly, there were increases in the share of the workforce working relatively low numbers of hours, particularly among women working between 1 and 15 hours. At the other end of the scale there was a slight fall in the proportions working 40 or more hours per week, with the reductions more pronounced amongst the male workforce. By August 2009 54.6 per cent of men worked 40 or more hours per week (down from 57.1 per cent at August 2008); amongst women 27.4 per cent worked 40 hours or more per week (down from 28.4 per cent at August 2008) (see Figure 1 below). These estimates reinforce the indicators on underutilisation with more people working fewer average weekly hours, particularly among those who work less than 40 hours per week.

Figure 1: Actual Hours Worked, by Gender (%), August 2008 and August 2009

Source: ABS 2009a, Catalogue 6105.0 Table 2.7
Earnings Preceding September 2008

Figure 2 displays trends in the wage price index (WPI) for Australia disaggregated by sector. The WPI captures changes in wages attached to particular ‘jobs’ (rather than people) and, in so doing, overcomes some of the skill and compositional problems that plague efforts to monitor earnings over time.

Between March 2000 and June 2008 the annual pace of wage growth (ordinary time hourly rates of pay excluding bonuses) was equal to 3.7 per cent, with wage growth in the public sector tending to outstrip that of the private sector (see Figure 2 below). In the public sector total hourly rates of pay (excluding bonuses) grew by 32.4 per cent between June 2000 and June 2008. In the private sector the corresponding wage growth was 30.0 per cent.

Figure 2: Wage Price Index, Australia

Source: ABS, 2009e, Catalogue 634501 Tables 3b, 4b and 8b

Note: Wage price index excludes consideration of bonus payments.
Observed differences in public and private sector wage growth rates reflect, in part, different methods of wage setting between these two sectors. Relative to the private sector, the public sector is more likely to set wages using registered collective agreements.

Table 6 (on the next page) shows award and agreement coverage by sector and sex for Australia at August 2008. Across all public sector employees, 96 per cent of all employees were covered by a collective agreement; 1.1 per cent had a registered individual agreement and a further 2.0 per cent were covered by an unregistered individual agreement. In contrast, of all private sector employees at August 2008 only 25.6 per cent were covered by a collective agreement, 2.4 per cent by a registered individual agreement and 44.7 per cent by an unregistered individual agreement. As shown in Figure 2 (opposite), the outcome is that, while annual changes in WPI in the private sector exceeded those in the public sector immediately before September 2008, this situation has reversed in recent months. This suggests that private sector employers have responded to the economic context by restricting labour costs.

These wage setting patterns have also varied by sex. Women, for example, were more likely to have their pay set by the award or a pay scale (19.9 per cent vis-à-vis 13.3 per cent). In the private sector males were more likely to be on an unregistered individual agreement (47.5 per cent) compared to women (41.5 per cent).

Research elsewhere has documented the differing wage outcomes arising from various approaches to pay setting. In the federal jurisdiction wage growth (measured in terms of median earnings) has, on average, been stronger for workers employed under collective registered agreements than under federally registered individual agreements (or Australian Workplace Agreements as they were more commonly known) (Peetz and Preston, 2009). The shortfalls are particularly pronounced in smaller organisations. In 2006 Victorian employees in small firms (with less than 20 employees) on AWAs earned 43 per cent less than their counterparts on registered collective agreements (Peetz and Preston, 2007).
Table 6: Methods of Wage Setting – Australia, August 2008

<table>
<thead>
<tr>
<th></th>
<th>COLLECTIVE AGREEMENT</th>
<th>INDIVIDUAL AGREEMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Award or pay scale</td>
<td>Registered</td>
</tr>
<tr>
<td>Males</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private</td>
<td>15.7</td>
<td>25.2</td>
</tr>
<tr>
<td>Public</td>
<td>*0.3</td>
<td>94.5</td>
</tr>
<tr>
<td>All sectors</td>
<td>13.3</td>
<td>35.9</td>
</tr>
<tr>
<td>Females</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private</td>
<td>25.8</td>
<td>26.1</td>
</tr>
<tr>
<td>Public</td>
<td>*0.5</td>
<td>97.0</td>
</tr>
<tr>
<td>All sectors</td>
<td>19.9</td>
<td>42.6</td>
</tr>
<tr>
<td>Persons</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private</td>
<td>20.4</td>
<td>25.6</td>
</tr>
<tr>
<td>Public</td>
<td>*0.4</td>
<td>96.0</td>
</tr>
<tr>
<td>All sectors</td>
<td>16.5</td>
<td>39.2</td>
</tr>
</tbody>
</table>

Source: ABS, 2008a, Catalogue 6303.0, Table 12.

The relatively high representation of women in specific areas of public employment such as health and education could be expected to ensure a greater level of earnings for this section of the workforce and to contribute to a reduction in the gender pay gap. However, as shown below, this is not reflected in post September 2008 earnings data.

**Earnings Since September 2008**

Table 7 summarises changes in the wage price index since September 2008 (the changes are also shown graphically in Figure 2 on p. 128). Two indicators are provided: quarterly changes and the changes on the corresponding quarter in the previous year. The data are disaggregated by sector. Across Australia there was relatively strong wages growth in the public sector in the latter part of 2008. Nationally, quarterly changes peaked in the December quarter with the public sector quarterly increase being 1.7 per cent and the private sector increase being 1.4 per cent.
Table 7: Wage Price Index, Total Hourly Earnings, Excluding Bonuses, Australia, December 2007 to June 2009

<table>
<thead>
<tr>
<th></th>
<th>Dec-07</th>
<th>Mar-08</th>
<th>Jun-08</th>
<th>Sep-08</th>
<th>Dec-08</th>
<th>Mar-09</th>
<th>Jun-09</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public</td>
<td>1.0</td>
<td>1.0</td>
<td>0.6</td>
<td>1.6</td>
<td>1.7</td>
<td>1.3</td>
<td>0.8</td>
</tr>
<tr>
<td>Private</td>
<td>1.2</td>
<td>1.1</td>
<td>1.2</td>
<td>1.3</td>
<td>1.4</td>
<td>0.8</td>
<td>0.7</td>
</tr>
<tr>
<td>Change on corresponding quarter in previous year (%)</td>
<td>4.1</td>
<td>3.9</td>
<td>3.8</td>
<td>3.6</td>
<td>4.2</td>
<td>4.4</td>
<td>4.5</td>
</tr>
<tr>
<td>Public</td>
<td>4.3</td>
<td>4.2</td>
<td>4.3</td>
<td>4.2</td>
<td>4.3</td>
<td>4.0</td>
<td>3.5</td>
</tr>
<tr>
<td>Private</td>
<td>4.3</td>
<td>4.2</td>
<td>4.3</td>
<td>4.2</td>
<td>4.3</td>
<td>4.0</td>
<td>3.5</td>
</tr>
</tbody>
</table>

Source: ABS 2009e, Catalogue 634503b and 634504b

Since the peak at December 2008 there has been a sharp decline in wages growth, particularly in the private sector (see Figure 2). Sectors with below average rates of growth included many low paid sectors such as cultural and recreational services, cafes accommodation and restaurants, retail trade and manufacturing.

Table 8 (on the following page) lists the changes in earnings estimates for three quarters of data since August 2008 for men and women employed full-time in different industry sectors. The comparisons of earnings data through time are subject to complexities associated with possible compositional changes in the workforce, which may be particularly important in a context where older, higher earning employees might be leaving the workforce. However, in this case we are comparing earnings patterns between different groups of employees and, assuming that compositional changes are relatively constant across the workforce, the comparisons can provide some insights. The wage price index for the June 2009 quarter has been included in Table 8 to provide point of comparison between average earnings data (which is subject to compositional change) and average wage costs.

Two general patterns are evident. Across all industries, increases in women’s earnings are lower than men’s and, for both men and women, total earnings are growing more slowly than ordinary time earnings. The latter is likely to be due to less hours being worked, with implications for the amount of overtime or other penalty payments that affect total earnings. There are seven industries in which women working full-time
received comparatively higher increases in weekly earnings than men: electricity, gas and water supply, retail trade, finance and insurance, property and business services, education, health and community services and cultural and recreational services.

Table 8: Change in Average Weekly Earnings for Full-time Employees (%), Australia, August 2008 – May 2009

<table>
<thead>
<tr>
<th>Industry</th>
<th>Males</th>
<th>Females</th>
<th>Average Weekly Earnings (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>% change in</td>
<td>% change in</td>
<td>Industry Wage</td>
</tr>
<tr>
<td></td>
<td>earnings</td>
<td>earnings</td>
<td>Price Index*</td>
</tr>
<tr>
<td></td>
<td>Ordinary</td>
<td>Total</td>
<td>($)</td>
</tr>
<tr>
<td>Mining</td>
<td>6.4</td>
<td>6.4</td>
<td>2,140.00</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>0.6</td>
<td>-1.0</td>
<td>1,128.50</td>
</tr>
<tr>
<td>Electricity gas and water supply</td>
<td>2.9</td>
<td>2.5</td>
<td>1,435.70</td>
</tr>
<tr>
<td>Construction</td>
<td>7.4</td>
<td>6.4</td>
<td>1,262.40</td>
</tr>
<tr>
<td>Wholesale trade</td>
<td>2.3</td>
<td>0.9</td>
<td>1,157.80</td>
</tr>
<tr>
<td>Retail trade</td>
<td>4.8</td>
<td>3.6</td>
<td>939.20</td>
</tr>
<tr>
<td>Accommodation, cafes and restaurants</td>
<td>2.7</td>
<td>2.7</td>
<td>902.90</td>
</tr>
<tr>
<td>Transport and storage</td>
<td>2.7</td>
<td>2.3</td>
<td>1,192.10</td>
</tr>
<tr>
<td>Communication services</td>
<td>5.4</td>
<td>5.3</td>
<td>1,278.60</td>
</tr>
<tr>
<td>Finance and insurance</td>
<td>-0.1</td>
<td>0.1</td>
<td>1,697.80</td>
</tr>
<tr>
<td>Property and business services</td>
<td>3.2</td>
<td>2.9</td>
<td>1,455.40</td>
</tr>
<tr>
<td>Government administration and defence</td>
<td>3.6</td>
<td>3.6</td>
<td>1,287.60</td>
</tr>
<tr>
<td>Education</td>
<td>3.3</td>
<td>3.2</td>
<td>1,343.40</td>
</tr>
<tr>
<td>Health and community services</td>
<td>5.5</td>
<td>5.1</td>
<td>1,434.10</td>
</tr>
<tr>
<td>Cultural and recreational services</td>
<td>4.8</td>
<td>4.5</td>
<td>1,309.60</td>
</tr>
<tr>
<td>Personal and other services</td>
<td>6.9</td>
<td>6.1</td>
<td>1,276.50</td>
</tr>
<tr>
<td>All industries</td>
<td>4.3</td>
<td>3.7</td>
<td>1,280.40</td>
</tr>
</tbody>
</table>

Source: ABS, 2009e Catalogue 6302.0, * hourly wage excluding bonuses; 2009e Catalogue 6345.0 original estimates.
In three of these industries, full-time women workers comprise less than 20 percent of the workforce (electricity gas and water supply; retail trade; cultural and recreational services).

Perhaps buoyed by the economic stimulus package, including infrastructure investment and the first home owners grant, construction wages for men grew at a comparatively high rate. Despite widely reported job losses in the mining industry, earnings for those who have retained employment appear to remain relatively high. There was also comparatively stronger growth in industries with a relatively strong public sector presence, including education, health and community services, cultural and recreational services and personal and other services.

Figure 3: Percentage Growth in Total Hourly Rates of Pay, Excluding Bonuses (Wage Price Index)
December 2008 – June 2009

Source: ABS 634505b
The high levels of gender segmentation in the labour market, together with these marked differences in the inter-industry wages growth, have affected the size of the estimated gender wage gap. Since August 2008 the gender wage ratio in the full-time labour market (measured using average weekly ordinary time earnings (trend series) has fallen by 0.7 percentage points to 82.6 per cent (at May 2009). The gender wage gap of 17.4 per cent at May 2009 equates to an average pay differential of $224 per week. However, the use of full-time wage rates to determine a gender pay gap has some disadvantages. As illustrated in Figure 3 (on the preceding page), the growth in hourly wage rates has been highest in Education, a sector with a relatively high percentage of women workers. An obvious question is why this relatively high rate of wage growth has not reduced the gender pay gap. One answer is that the Education has a high rate of part-time employment (see Table 3 on p. 124) and thus many of the women employed in this sector and potentially benefiting from improved wages are not included in gender wage gap estimates. In contrast, other high wage growth sectors, such as mining and construction, employ relatively large percentages of full-time men and are, therefore, included in gender pay gap estimates.

The obvious solution is to base gender earnings comparisons on hourly wage rates. However, the wage price index does not provide data disaggregated by gender, making it inappropriate for estimating gender wage gaps. Hourly wage estimates available from data collected in the ABS Survey of Employee Earnings and Hours also focus on full-time (ABS 2009f, Catalogue 6306.0). The lack of regular, timely data for hourly wage rates and hours worked by gender provides a significant limit to monitoring and understanding gendered aspects of employment and wages in Australia. Unless improvements in women’s earnings are reflected in the full-time workforce they have a limited impact on measured gender wage gaps.

**So How are Women Faring? Gaps in our Understanding of Women’s Economic Security**

The data give us some tentative indications about women’s earnings security since September 2008. The expectation that women’s over-
representation in the casual or part-time workforce will lead to disproportionate job losses seems to over simplify the current picture of Australia’s work patterns. Neither job losses nor the discouraged worker effect appear to be dominating women’s patterns of working and earnings. Women’s workforce participation has slightly increased or been relatively steady since September 2008 and there has been a shift towards part-time work rather than a large scale loss of part-time employment. While women remain over-represented among those looking for full-time work, they have fared comparatively well in finding part-time work. This appears to have had mixed results in terms of economic security. While part-time work has cushioned women’s unemployment rates, women have higher rates of labour underutilisation, suggesting that many are working fewer hours than they require or want. Simultaneously, there has been a shift toward part-time employment and growing underutilisation among men. Rather than women’s patterns of work being reduced during the economic downturn through a reduction in the employment of women part-time workers, women’s patterns of work have expanded to a larger proportion of men.

The implications for earnings security and gender wage gaps are ambiguous. For part-time workers, earnings vary considerably with hours worked as well as their hourly wage rate. In relatively low paying, part-time industries such as retail trade and accommodation, cafes and restaurants, it is likely that a lack of earnings security arises from both fewer hours and relatively low wages. However, it is difficult to gain an adequate picture of earnings security by industry due to the lack of data on hours worked by industry. Further, in the absence of appropriate data for part-time workers, the gender pay gap is estimated using wages for full-time workers. This limits the potential effect on the gender wage gap of the relatively favourable wage increases in the feminised sector of education which employs a large proportion of part-time workers.

Prior to September 2008 there was growth in the gender wage gap and this was linked with pay setting arrangements with women on individual agreements achieving more modest pay increases compared with those on collective agreements (Peetz and Preston 2009; Peetz and Preston 2007). This was consistent with the argument that centralised wage fixing is particularly important to women’s prospects in the labour
market. Austen et al. (2008) show that minimum wage adjustments between 1995 and 2000 reduced the gender wage gap by 1.2 percentage points.

As illustrated above, the estimated gender wage ratio has continued to fall since September 2008, although possibly for different reasons. The decision by the Australian Fair Pay Commission to leave the 2009 federal minimum wage unchanged at $543.73 per week may further contribute to rising wage inequality and gender wage gaps in Australia. Legislated minimum wages play an important role in raising the bottom of the pay distribution and in protecting the earnings of women (Austen et al. 2008).

The lack of a detailed data severely limits our understanding of changes in wages, hours and working conditions of part-time workers. Fifty-three per cent of employed women currently work less than 35 hours per week (i.e. work part-time). Amongst men the comparable share is 25 per cent (ABS, 2009a). The lack of available data to monitor the earnings and employment conditions of part-time employees has been an ongoing concern for the Australian Human Rights Commission for several years, a concern confirmed by previously commissioned research (Preston, Jefferson, and Seymour, 2006). A lack of appropriate, timely data can be considered a particularly important omission within a context of individual, confidential agreements and the need for evidence as a key input for implementing and monitoring economic policy reform (Leigh, 2009; Wilkie and Grant, 2009).

Analysis by Access Economics suggests that shifts between part-time and full-time work have implications for Australia’s output and productivity. It has been suggested that changes in the percentage of women in the workforce, along with the number of hours they work, will significantly affect Australia’s capacity to meet the challenges of an ageing population. If women’s workforce participation remains at current levels and there is growth in the percentage of women employed part-time, national income per capita is predicted to be 2.8 per cent less than the $76,000 predicted in the Commonwealth’s intergenerational report. On the other hand, if women’s participation increases and the percentage of women in full-time employment increases, then national income per capita is predicted to increase by 4.4 per cent. For the predicted per
There are strong arguments that major policy changes should be accompanied by data collection that systematically monitors the costs and benefits of the policy. This has not occurred in the area of labour market policy; data collection has declined in both scope and regularity during a period of major legislative change. We have little idea how the large number of part-time women workers and ever increasing number of part-time men workers are faring in a rapidly changing labour market. Economists are among the first to admit that efficient markets rely on good information – an issue that appears to have been overlooked in debates about labour market reform.

In the absence of timely and comprehensive data, we are left to rely on newspaper reports, other informal sources and past studies from which to infer outcomes for labour market sectors. Predictions for the future of specific industries and their employees are mixed. In recent months, there has been significant press coverage given to the downturn and job losses in traditionally male industries such as mining and heavy manufacturing.

Data on retail sales has received considerable media attention due to the effects of the federal government’s fiscal stimulus package at the end of 2008. Increased turnover of 1.3 percent in the June quarter 2009 suggests some success in maintaining consumer spending, although the increased turnover was accompanied by a decline of 1.4 percent in trend estimates at current prices (ABS, 2009g). At the same time, however, turnover is volatile within specific areas of the retail industry, with a 2.9 percent increase in turnover in the household good sector occurring alongside an 8.8 percent decline in department stores turnover (ABS, 2009g, table 2, seasonally adjusted).

Conclusions

Available data indicates that patterns of employment and earnings among Australian women are not following a predictable pattern. In addition,
the effects have varied between men and women, industries and occupations. Part-time employment and labour underutilisation are growing features of the labour market and suggest an expansion, rather than a contraction of traditionally feminised work arrangements. While many of the estimates discussed in this article cover a short period at the very start of the downturn, they reveal an important issue – namely that the timing and sources of changes in employment are likely to be very different for men and women and these differences have important policy implications. Women are over represented in industries in which discretionary spending is an important driver of employment, such as retail trade, accommodation, cafes and restaurants and personal and other services. The workforces in these industries are also heavily casualised, making reductions in working hours relatively easy to implement.

However, our capacity to monitor these changes is limited. Notwithstanding the significance of women’s labour market participation and the growth of part-time employment there remains a lack of comprehensive data to monitor their employment experiences. This has serious implications for policy analysis and development.

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The authors would like to express their appreciation of helpful suggestions received from Frank Stilwell and an anonymous reviewer. The usual disclaimer applies.

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EUROPE’S CRISIS MANAGEMENT: MISSp OPPORTUNITIES

Heribert Dieter

The financial crisis that affected the global economy in 2008 and 2009 originated from the USA, but it affected most economies, including of course the European Union. The 27 member countries were hit hard: Capital exporters like Germany had considerable direct exposure to sub-prime lending in the US, whilst Eastern European economies like Hungary were suffering from the deteriorating conditions on credit markets and the inability of borrowers to roll over existing debt. Above all the crisis has exposed the weakness of European cooperation and may have damaged the prospects for European integration for a considerable period of time.

When the crisis hit Europe with increased force in September/October 2008, the response continued to be limited to national economic policy. Whilst there has been a token European recovery program, in essence Europeans returned to the national level for rescue packages. Of course, this was particularly so for banks, who – as one observer quipped – grow abroad but die at home. Consequently, bailout packages were organized by national governments. ING turned to the Dutch authorities, Northern Rock and the Royal Bank of Scotland to Downing Street, and IKB to the German government. Cross-border banks turned out to pose a problem: Fortis, a Belgian-Dutch finance group, had to be dismantled into ‘national’ entities before governments came to the rescue.

For all the praise the European Union has received for overcoming conflict and tension, the group turned out to be unable to implement a joint response to the crisis. The lack of a common financial policy became an issue. Finance ministers from the 27 countries tended to
express as many opinions and the group was and continues to be unable to express a common position on financial reform at home and abroad.

Moreover, the old split between Britain and Continental Europe became more pronounced in the crisis. In the first part of the crisis, from the collapse of Northern Rock in September 2007 to the collapse of Lehman Brothers about one year later, many continental Europeans viewed the crisis as a phenomenon limited to the USA and the United Kingdom. The failure of the liberalized financial sectors in the USA and the United Kingdom was observed with a touch of *schadenfreude*, until policy makers and citizens in Germany, Holland and France realized that those that lent to the USA often came from continental Europe.

With hindsight, this phase of satisfaction and self-approval was wasted time. Instead of preparing Europe for what was to come, many policy makers in Germany, France and other countries were far too complacent and reacted belatedly. Moreover, when they realized that the crisis would not spare them, the reactions were frequently hastily implemented and lacked a coherent strategy. A particular nasty example is the German guarantee for deposits of October 2008, which I will discuss in greater detail below. But in general, all member countries of the European Union were reacting in panic, and this represents an astounding contrast to the Chinese crisis management, which appears to have been implemented in a much more strategic manner. Effectively, European integration may emerge from the American-made crisis as the biggest casualty.

**Crisis Management at the National Level**

The European Union is the most successful regional integration project in the world, or at least it has been in the past. The question is whether European governments have been reacting appropriately to the crisis. For Europe, the crisis could have represented a unique opportunity to promote a reform of international financial markets and institutions of global governance, given that the Anglo-American model of financial markets has been discredited. The crisis provided the EU with an unprecedented opportunity to demonstrate its collective ability to manage and master a crisis of enormous dimensions, but the EU has failed this
litmus test. Whilst there was a lot of rhetoric on the need to cooperate in the crisis, in reality the more powerful member countries have chosen to pursue their own national agendas and have continued to do so since.

The national responses have been implemented against a background of limited cooperation before the crisis. It should be noted that the regulation of the financial sector in the European Union continued to escape efforts to develop a uniform approach. One factor here is that the European Union has at least three distinct levels of cooperation in financial affairs. The core is the eurozone. Whilst monetary policy is run by the European Central Bank, the ECB’s mandate is limited. It is responsible for price stability, not for the much broader concept of financial stability. Thus, even within the eurozone there has not been any significant supranational financial supervision. Denmark represents the second level of cooperation: it continues to have its own currency, the krone, which is tied to the euro at a fixed rate and is part of the old European Monetary System. The third group is neither having any cooperation on exchange rate stability nor any meaningful cooperation with regard to the regulation of financial markets. The United Kingdom is, of course, the most important country in this category. In contrast to many other policy areas, e.g. agriculture or foreign trade, the European Union continues to be characterised by an impoverished infrastructure in finance.

Against this background, it is not surprising that Europe has not presented itself as a model of good behaviour in a crisis. The problems started in early 2007 when European governments did not take sufficient note of the first hints of the crisis and failed to respond accordingly. As a result, one comparatively hastily designed programme followed the next, conveying the impression of hectic and uninformed politics and hence exacerbating the crisis. In Europe government policies have often not been contributing to restoring confidence, but have occasionally contributed to the already emerging fears in their population. In particular, the continuous repetition of the inevitability of doom and gloom, prominent especially after the collapse of Lehman Brothers in September 2008, dented the expectations of even the most ardent optimists.
Government officials in many European economies have fuelled the crisis with their negative comments. This requires an explanation. Why have they collectively done this? Either the situation was as bleak as they portrayed it, which is possible, or policy makers were trying to shore up public support for their bailout packages, which appears more likely. Without the negative sentiment that appeared to be the consensus amongst political parties in many European economies, and certainly in Germany, the large rescue operations of 2008 would have been discussed much more critically and the call for limits to the bailout operations would have been more widespread.

But why were policy makers so keen on spending billions of euros on private institutions that obviously did not fully understand their business? Why were politicians eager to dismantle one of the characteristics of the capitalist system, the principle that market participants that fail have to exit the markets and go into bankruptcy? Again, there are two potential answers to that question. The explanation given in public was that all banks that were at risk in 2008 were so important to the future functioning of the financial system that they had to be bailed out at almost any cost. Governments were, so they argued, not willing to risk the collapse of the financial system. However, in Europe all banks were considered systemically important, even small institutions that no one outside the trading floors had heard of prior to their calamities.

Representative of this extended coverage is the ‘Deutsche Industriebank’ (IKB) in Germany, a small bank specialised in providing finance to small- and medium-sized companies in Germany.\(^1\) IKB had been founded in 1924 and had weathered the turbulent 20\(^{th}\) century, but not the subprime crisis. IKB was small: total assets of euro 50 billion and 1,800 employees do not constitute a large bank and, given the business of IKB, it is impossible to consider it systemically relevant. Nevertheless, IKB was rescued with about euro 10 billion of public money (German Ministry of Finance 2009). Subsequently, IKB was quickly re-privatised to the American Investor ‘Lone Star’, a private equity institution. Whilst there has not been an official confirmation for the value of the

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\(^1\) Of course, the bank’s core activity did not cause trouble, but rather its engagement in the US, for which IKB was ill equipped.
transaction, newspapers have estimated the price that Lone Star paid at euro 137 million (Handelsblatt, 19 June 2009, p. 1).

Of course, the question arises why IKB and, later on, other larger banks, such as Hypo Real Estate in Germany or Fortis in Belgium and the Netherlands, were rescued. Indeed, there appears to be a significant difference from the crisis management of the USA, which permitted the bankruptcy of least one investment bank, Lehman Brothers. By contrast, virtually all banks were rescued in Europe.

In essence, there are four potential explanations. First, and least convincing, is the idea that all banks have indeed become too big to fail. Whilst this is certainly the case for large financial conglomerates such as Deutsche Bank or the Royal Bank of Scotland, not all banks, least of all IKB, were so large that they could disrupt the entire financial sector.

Second, policy makers may have thought that all banks had to be rescued and may have been afraid to be the first that did not rescue a bank. Historical evidence would have given them some support for their arguments. In previous financial crises, e.g. in the 1930s or 1970s, individual bank collapses were identified as at least the trigger, if not the cause of severe turbulence. In July 1931, the collapse of the ‘Darmstädter und Nationalbank – Danat Bank’ triggered a crisis that not only deepened the already two-year old depression, but also had international repercussions. The United Kingdom, which had lent to Germany and the ‘Danat Bank’, the second-largest German bank at the time, was facing severe liquidity shortages and the Bank of England had to take Britain off the gold standard in September 1931. The collapse of ‘Herstatt Bank’ in 1974, caused by a bunch of inexperienced young currency traders, sent shockwaves through the financial markets of Europe and the United States. Consequently, the assumption that policy makers were unable to differentiate between systemically relevant banks and those that may be sent into liquidation has a certain appeal.

Third, policy makers may have been concerned about the short- and long-term consequences of bank collapses. This idea is reflected on the website of the German Ministry of Finance, where the rescue operations are justified with an interesting explanation: any collapse of a bank would have destroyed confidence in the German banking system. Whilst
related to the second explanation, there is an additional dimension: the future competitiveness of the banking system may have been at risk, and therefore policy makers decided to risk taxpayers’ money for bailout operations.

However, these explanations are not fully satisfying. An additional fourth factor is the close network of interests between policy makers and the financial sector that has been developed over the years. Whilst this development has long been criticised in the United States, for example in Jagdish Bhagwati’s 1998 article on the ‘Wall Street Treasury Complex’, published in the respected journal *Foreign Affairs*, there has not been a debate on the close links between politics and finance in continental Europe (Bhagwati 1998). Yet there are very close links. In the case of IKB, Jörg Asmussen, who was promoted to the position of German Deputy Minister of Finance in July 2008, sat on the board in the years before the crisis. Thus, the government not only bailed out the bank, but also tried to safeguard its own reputation. The issue of networks in German finance will be revisited later in this article.

**The Unilateral German Guarantee and Uncoordinated Stimulus Packages**

The most striking example of national crisis management is provided by Germany, the EU’s largest economy. After the collapse of Lehman Brothers in mid-September 2008, a period of unprecedented turbulence in financial markets followed. Liquidity in interbank markets dried up completely, and panic crept into the thinking of managers and citizens alike. There was an obvious need for leadership and guidance, which private markets were unable to provide. In essence, the weeks after the crash of Lehman would have required the joint effort of political leaders and their finance ministers. They could and should have demonstrated that they will be able to handle the crisis collectively. Unfortunately, that

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2 In spring 2009, Asmussen received some public criticism about his role in the run–up to the crisis, but without consequences. See, for example, a report on him on German television at [http://www.br-online.de/das-erste/report-muenchen/report-krisenmanager-asmussen-ID1246612708714.xhtml](http://www.br-online.de/das-erste/report-muenchen/report-krisenmanager-asmussen-ID1246612708714.xhtml).
was not happening. Instead, policy makers in virtually all European countries acted individually. In Germany, the government announced on 5 October 2008 a guarantee for all deposits in banks operating in the country, regardless of the size of the deposit. This unilateral measure may represent one of the worst mistakes of German post-war foreign policy.

That claim requires substantiation. What is wrong with a government guaranteeing the savings of its citizens, in particular when the economic history of Germany is considered? In the 20th century, Germans had lost most of their savings twice: in the hyperinflation of 1923 and in the post-war currency reform of 1948. These two events have shaped the preference of German citizens for safe investments and have contributed to the monetary policy of the Bundesbank, which was always characterized by a preference for stability over economic growth or high employment.

Against this background, it is understandable that the German government was concerned about a potential panic amongst German citizens. However, until the government announced its unilateral guarantee, there had not been any obvious sign of nervousness amongst savers. Yes, people were discussing the stability of the financial system, but there were no widespread withdrawals. Bundesbank personnel are said to have admitted unofficially that they had difficulty in restocking cash dispensers in the week before the guarantee, but there is no more evidence than that.

However, Germany’s unilateral guarantee created severe problems for other economies. More advanced ones, including Australia, were also having to guarantee deposits because capital was seeking safe havens and OECD-countries that had issued government guarantees were considered the safest of all. Unfortunately, economies whose governments were not able to issue credible guarantees were the main victims. Capital was withdrawn from economies in Eastern Europe and from developing economies. Effectively, the uncoordinated and probably unnecessary German guarantee deepened the global crisis rather than containing it. Nobel laureate Paul Krugman has also been criticizing the German crisis management in general and Finance Minister Peer Steinbrück in particular, emphasising the drawbacks of the national crisis management.
in Europe’s biggest economy. Krugman saw a negative multiplier effect arising from Germany’s policies (Krugman 2008).

Thereafter, European economies continued to implement national, rather than European, crisis management. The stimulus packages were an important element in that process. Each member country of the EU implemented a tailor-made program. Of course, the individual measures were influenced by each country’s specific preferences and in many countries a lot of money went to the building industry, which is a sector with limited competition from abroad. Effectively, national governments were trying to make sure that taxpayers’ money would not stimulate the economies of other countries. Whilst this is not surprising, it nevertheless constitutes a partial departure from the European project, which was characterized by collective problem-solving. The country that should have withstood that trend was Germany, which is both Europe’s largest and most competitive economy. More than any other single country, Germany benefits from both European integration and a liberal global trade regime, and the failure of German politicians to realize their specific responsibility in the European and global economy attracted harsh criticism (See, for example, Collignon 2009). 3 A comment of Germany’s then Minister of Economics in November 2008 didn’t help: he indicated his hope that ‘… the measures taken by other countries … will help our export economy’ (quoted in Münchau 2008).

No Difference to Wall Street – The Quiet Networks in European Finance

Networks between finance and politics help to explain some dimensions of the crisis management, both in the USA and in Europe. In the USA, the crisis has shed light on the significant linkages between Wall Street and Treasury. Three recent American Secretaries of the Treasury – Robert Rubin, John Snow and Hank Paulson – came from Wall Street or went there after their time in office. Alan Greenspan has become an advisor to PIMCO, an important player in international bond markets. The former chief economist of the International Monetary Fund, Simon

3 See also The Economist, Miss World goes missing, 22.11.2008, pp. 35-36.
Johnson, has argued that the financial industry has effectively captured the American government. Comparing the American financial sector to Russian Oligarchs, he has recommended a tough medicine:

The second problem the U.S. faces—the power of the oligarchy—is just as important as the immediate crisis of lending. And the advice from the IMF on this front would again be simple: break the oligarchy (Johnson 2009).

The linkages between the government and the financial sector are well known and well-documented in the USA, but Europe, and Germany in particular, is not structurally different. As mentioned above, a key figure in German has been the Deputy Finance Minister Jörg Asmussen, a Social Democrat. Asmussen joined the Ministry of Finance in 1996 at the age of 30. Quickly promoted, he became Head of Department VII – financial markets and their regulation – in 2003. Asmussen pushed innovation in German finance, securitization in particular, in subsequent years. In an article in a finance journal in 2006, Asmussen praised the benefits that asset backed securities would have. Besides, he explicitly indicated that the German Ministry of Finance will not insist on ‘unnecessary testing and documentation requirements’ (Asmussen 2006). As mentioned above, he sat on the board of the failed IKB and was thus partly responsible for this bank failure.

Some observers had expected that Asmussen, following the IKB debacle, would have been sent into early retirement. Instead, he was promoted in July 2008 to the position of Deputy Minister of Finance and became responsible for the bailout measures – a classic case of ‘poacher turned gamekeeper’. The very person that had been pushing deregulation and lax banking supervision in Germany became the most important person in the rescue operation. Ironically, or perhaps rather a confirmation of Asmussen’s good networks, he has been one of the very few senior officials from the Social Democrats that remained in office after the change of government in autumn 2009.4

4 The German newspaper Frankfurter Allgemeine Zeitung characterized Asmussen’s remaining in office as a big surprise. Gerhard Schick, Green Member of Parliament, expressed criticism and suggested that the policies of the previous coalition would probably be continued (29.10.2009, p. 17).
In addition, Asmussen has strong private links with German finance. His partner, Henriette Peuker, is the chief lobbyist of the German Stock Exchange in Berlin (Afhüppe 2009). Asmussen studied at Bonn University, and one of his fellow students was Jens Weidmann, who has been Angela Merkel’s main economic advisor since 2005. These two were taught at Bonn by the economist Axel Weber, who was promoted to the presidency of the Bundesbank in 2004, following a proposal of Asmussen (Fietz 2009). The regulation and supervision of German financial markets, as well as the subsequent rescue operation, was in the hands of a social circle that shared not only their academic background but also their market-friendly economic orientation.

The existence of links between the government and the financial sector is not astonishing, but their intensity is remarkable. As in the United States a regular exchange of personnel can be observed. One of Asmussen’s predecessors, Caio Koch-Weser, left the Ministry of Finance for a lucrative position at Deutsche Bank in 2006. Another Deputy Minister of Finance, Axel Nawrath, left the government in 2009 to take up a position in the Government-owned KfW-Bank. The scale of the links between finance and the government may not be the same as in the USA, but the trend and effects appear similar.

The drift towards less regulation for the financial sector in Germany has been implemented under the auspices of Social Democratic Ministers of Finance, who held this office since the change of government in 1998. Whilst the previous conservative coalition, led by Helmut Kohl, was not hostile to the interests of the financial sector, it was their Social Democratic successors that deregulated financial markets. The parallels to other countries are quite striking: In Australia, financial markets were deregulated by the Hawke/Keating government following its election in 1983. In the USA, important regulatory restrictions, for instance the separation of investment and commercial banking required by the Glass-Steagall Act of 1933, were scrapped by the Clinton administration in 1999. And in the United Kingdom, Tony Blair’s Labour government championed ‘light-touch regulation’, the term being coined by Gordon Brown. In all those cases, including Germany, the interests of finance industry were accommodated by ostensibly left-leaning governments.
Of course, the importance of the small group of economists at the German Ministry of Finance and the Bundesbank rose dramatically during the financial crisis. Effectively, the crisis was managed by half a dozen men in Germany – Finance Minister Peer Steinbrück, Axel Weber from the Bundesbank, Josef Ackermann from Deutsche Bank and Jochen Sanio from BAFIN, the agency supervising financial markets, Jörg Asmussen and Jens Weidmann coordinating the rescue operations in the background. Given the great importance of Asmussen in particular, there has been a substantial amount of criticism, both in the political sphere and in the media (See, for example, Ramthun 2009, Stern 2009, Zeit 2009). As mentioned above, this criticism has not destabilized his position.

As in other countries, the preferences of the private sector have changed over the last two decades, and at the centre of this change is Deutsche Bank, Germany’s only global player in finance. Josef Ackermann, the chief executive of Deutsche Bank, is the by far most important representative of the banking industry in Germany. He has continued and eventually championed the transformation of Deutsche Bank from a national player into a globally operating investment bank. Since 2005, Ackermann has been frequently consulted by Chancellor Angela Merkel and has been a prominent figure in German crisis management.

The contrast to previous decades is striking. In the first four decades after World War II, Deutsche Bank was very closely intertwined with German industry. Since the early 1950s, for example, Deutsche Bank owned 25 percent of the shares of Daimler-Benz, one of the largest and probably most prestigious industrial producers in Germany. The close relationship between German Banks and the manufacturing sector – labeled ‘Deutschland AG’ or Germany Inc. – came under intense pressure in the 1990s. Again, it was the Social Democrats who facilitated change. Deutsche Bank, to take the example from above, had acquired Daimler-Benz shares at a share price that was of course a fraction of their valuation decades later. Had they sold the shares under the old tax regime, Deutsche Bank would have been forced to pay billions in taxes on their capital gains. However, a change of the tax regime introduced by

the Social Democratic Finance Minister Hans Eichel in the late 1990s enabled German Banks to sever their ties with German industry and realize enormous tax-free gains (Maiisch 2005). Since then, the interests of German banks have of course changed fundamentally. Whilst prior to the late 1990s, German banks regularly were advocates of German industry, since then industry and finance often have diverging positions.

Silence on Imbalances

At the macroeconomic level, the crisis has exposed the vulnerability of capital exporters. In recent years China, Japan, Russia, Saudi Arabia, and Germany have exported huge amounts of capital and contributed to speculative excesses in other countries. But the role of the capital exporters plays a minor role both in the analysis of the crisis and in the debate on crisis prevention. This is surprising.

There are good reasons to give more thought to these imbalances. The whole business was a rotten deal. Germany sold machines and high-quality cars and received Lehman derivatives in return. Germany’s enormous surpluses landed back in the United States where they helped fuel the dubious dealings of the US financial sector. This is not a model to emulate. However, at the international level there is still no earnest discussion about getting rid of the imbalances. There are reasons for the silence.

For the economies involved, the existing model has offered advantages and satisfied particular preferences. That claim applies especially to the United States and China. The former is the economy with the biggest appetite for capital, whereas the latter is already the world’s most important manufacturer of consumer goods of all kinds. A specific division of labour has emerged over the past decade: China manufactures goods and supplies the credit for their purchase; while the United States buys Chinese goods and accumulates debt. Back in 2003, the Basle Bank for International Settlements was already describing this arrangement as ‘vendor finance’.

China is not the only surplus country, however. In Europe, Germany’s enormous surpluses have led to tensions within the EU. Without the
common European currency, the large German current account surplus (more than 260 billion US dollars in 2007) would have driven up the exchange rate of the deutschmark. In the absence of an external stability pact, this drives a dangerous wedge into the European Union (Dullien & Schwarzer 2009). Ultimately, German capital exports helped to finance the bubbles in Spain, Ireland and a number of Eastern European countries. German capital exports were a poor deal for Germans anyway. Despite their preference for safe investments, risk-shy German savers have been left carrying the can all the same – through the state budget – for the risks taken by financial intermediaries.

Of course, given the risk-adverse preferences of German savers, there had to be a transformation of savings into high-risk investment. This transformation was often facilitated by state-owned ‘Landesbanken’. Typically, these government-owned and government-guaranteed banks were engaged in financing investment in Germany. Their particular legal construction, especially their explicit government guarantees, came under pressure from the European Commission, which considered the government-guarantees to be an illegal subsidy and a competitive disadvantage for other European banks. Since the government guarantees had to be scrapped, the Landesbanken perceived a need to expand their activities and engage in new, potentially more risky activities. Many of them, for example Sachsen LB, Westdeutsche LB and Bayerische Landesbank, were aggressively expanding their activities in the current decade. Unfortunately, they did not know their new trade well, and most of them needed big bailout packages from the German taxpayer. German policy makers, some of whom oversaw these ventures, have been criticising the greed of investment banks, but were at the same time much more reluctant to disapprove of those banks which have been under their direct influence.

Surprisingly, both the contribution of German savers to the fuelling of bubbles elsewhere and the involvement of German federal and state governments in financial adventures abroad are hardly discussed in Germany. With regard to the production of surpluses, most Germans appear eager to return to successful exporting and appear not concerned that this eventuality could lead to yet another financial calamity.
Model Endorsed – Gains Wasted

The global financial crisis represented an opportunity for Europe, but that opportunity has been wasted. Continental Europe, without the United Kingdom and Ireland, has not had financial sectors that had grown out of proportion and had continued to place emphasis on a more sustainable economic development. In the crisis, continental European economies – in particular Germany, France, Italy and Spain – could have both led the group out of crisis and re-emphasized their political preference for a sound and more comprehensively regulated financial sector. Neither happened. Crisis management was primarily organised at the national, not the regional level; and a member country of the EU, Hungary, had to call the International Monetary Fund to the rescue.

In the subsequent reform debate, continental Europe is as silent as ever, whilst the discussion is led by British politicians, who have lately suggested rather dramatic measures. Adair Turner, head of the Financial Services Authority FSA, categorized the City of London as having grown ‘beyond a socially reasonable size’ and has been advocating a transaction or Tobin tax, hitherto anathema for the British establishment.6 Mervyn King, Governor of the Bank of England, has even called for the break up of banks into government-protected commercial banks and investment banks, with the latter free to gamble but not to be rescued if they fail.7

Whilst China appears to benefit from the crisis in OECD countries, the countries of the European Union have failed to utilize the historic opportunity that the crisis provided. Contributing to the failure have been mediocre crisis management driven by national rather than European priorities, structural weaknesses in regional economic governance and the inability of European governments to develop joint positions on financial governance.

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The author thanks the anonymous referees and the editor for their helpful comments and suggestions.

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...AND IN ABOUT TWO YEARS, I PREDICT A VERY STRONG RECOVERY FROM THE RECESSION I DIDN'T PREDICT UNTIL LAST WEEK.
A Great Financial Crisis can only occur as a surprise. If it is anticipated by the financial players, there may be a series of little financial crises as the players adjust their expectations but the imbalances which cause great crises will not build up. Great crises are therefore consequences of selective blindness. They result from disregard of the first and perhaps only worthwhile lesson in economics, which is that everything depends on everything else.

Despite the plague of dishonest accounting (itself a sign of trouble), in the boom which begat the current GFC the selective blindness was not due to lack of data – throughout the boom the national accounts of the Anglophone countries documented an unsustainable reliance on growing consumer debt as a source of demand. The blinkers were imposed by neo-liberal economics, that legacy of European intellectual turmoil and American Cold War evangelism which became the hegemonic economic theory following the end of full employment. This was ultimately an economics of process: provided all economic decisions were subject to demand and supply in competitive markets, the invisible hand would guarantee economic efficiency and the optimum use of resources. This being the case, there was no perceived need to check the macroeconomic balance sheets for signs of impending trouble. With honourable exceptions, faith in competition brought blindness, and this ingrained faith still hinders an appreciation of what went wrong. For a full appreciation of present problems, it is necessary to examine the macroeconomic balance sheets (ABS 2008).
What Went Wrong?

From an Australian urban point of view, the place to begin is the urban balance sheet. There is no official version of this, but we know the major trends. From 1994 or thereabouts Australian cities went through a land boom. Site values increased faster than improved values; location value rose as a proportion of total urban assets (NIEIR: 2006 Ch.2). The capital gain was shared by the business and household sectors.

Why did site values rise? One clue is the steepening of the centre-fringe rent gradient, which broadly reflected changes in the accessibility of work. During the boom it was frequently claimed that the increase in employment in the CBDs and inner suburbs reflected the growth of the knowledge economy, and there was certainly an element of this. However, the bloating of the finance sector added to CBD employment growth while the decline of the manufacturing sector reduced employment growth on the urban periphery. The rent gradient also steepened as a result of the full exploitation of motoring technology. In the 1950s the adoption of universal motoring had allowed the decentralisation of employment and the infilling of green wedges. By the 1970s the wedges had been filled and readily-decentralised employment had been spread around. Inner urban streets had become congested as cross-town traffic was added to traffic with local origins and destinations. The simple engineering solution to falling road speeds – increased road space – proved to be highly expensive, particularly when externalities were taken into account. The combination of the centralisation of work and falling road speeds increased the relative accessibility of work from the inner suburbs. Inner urban site values rose, precipitating both gentrification and redevelopment.

However, this was not the whole story of the land boom. An essential ingredient was bank promotion of residential mortgages. To the neo-classically blinkered this was no problem – after all, the mortgages were contracted between private parties assumed to be fully aware of all risks. From a bank point of view, residential mortgagees could be charged higher interest rates than other borrowers (big business had direct access to financial markets) yet mortgage lending seemed secure since there was land as collateral and if all else failed the borrowing household could
repay upon retirement from lump sum superannuation payouts. From the household point of view, the established advantages of entry into home ownership via mortgage borrowing were compounded by the discovery that extra consumption could be financed by extending the mortgage, not to speak of the joys of capital gains financed by negative gearing. As in booms more generally, selective blindness set in. The rising claim of debt servicing on household income increased the riskiness of mortgage loans, but this was ignored. Similarly the falling affordability of residential land to new market entrants put in question the sustainability of land prices, and hence the value of collateral, but this was also ignored.

A major increase in mortgage lending to households was the main change on the asset side of bank balance sheets during the boom. The corresponding increase on the liability side was borrowing from overseas. All of this seemed profit-maximising when it was undertaken but has landed the banks with two major exposures: exposure to household loan default and exposure to overseas financial markets and the costs and uncertainties of refinancing overseas debt.

The macroeconomic balance sheets thus document three problems – overvalued urban land, over-indebted households and a banking system over-exposed to overseas borrowing. Cries of alarm, including those from the National Institute of Economic and Industry Research in its State of the Regions Reports, were hushed by the neo-liberal establishment with the claim that competitive markets guarantee optimum and equilibrium.

**Market Failures**

Why have the macroeconomic balance sheets become financially unsustainable?

For Australia, looking at the balance of payments is a good place to start. Imports and debt servicing have persistently exceeded exports, financed largely by further accumulation of overseas borrowing by the banks. In neo-liberal theory free trade in currencies guarantees equilibrium in the balance of payments, but in practice the price responses are completely unhelpful. In particular, correction of a balance of payments deficit
requires the deficit country to invest in the industries producing tradeable goods, but a fluctuating exchange rate discourages such investment by adding to the risk that the exchange rate will be high and so kill the profitability of investment at the crucial time when profit is needed for cash flow.

Market forces are also supposed to guarantee that overseas borrowings are invested in ways which generate flows of foreign exchange with which to service the debt. However, under the market forces prevailing during the boom the banks found it more profitable to lend to households on mortgage than to lend to trade-exposed business. Not only did this lending fail to strengthen the trade-exposed sector; because of the limitations to the supply of accessible urban land it even failed to generate much of an increase in dwelling supply, instead spilling over into land value increases on the asset side and consumption increases on the expenditure side.

As regards the household sector income and expenditure account, land boom borrowing more than negated compulsory saving through national superannuation. Via the financial sector, overseas borrowing had a counterpart in the disappearance of household saving, crowded out by consumption.

Apart from the disappearance of saving, a remarkable element in the household sector income and expenditure account (compared to the decades before deregulation) was persistent heavy reliance on social security income. The data required to disaggregate the drivers of Commonwealth social security expenditures were suppressed as part of the overhaul of the public accounts in 1998, but take-up rates testify that the end of full employment continues to account for much social security receipt. This is partly a matter of geography – social security take-up is high in regions which suffer from failed industries and in general combine poor employment opportunities with affordable housing. Take-up is also high in the ‘lifestyle’ regions, whose populations have increased as land-boom capital gains encouraged retirees from the city to sell-up and shift to the beach, always carefully arranging their finances to come in under the means test. More fundamentally, the under-utilisation of labour reflected in high social security take-up disproves the neo-liberal faith that full employment can be guaranteed by movements in
real wages. There is, for a start, the strong complementarity between particular skills and particular types of equipment – and both the skills and the equipment commonly take decades to acquire. Again, work is a social activity, and lack of attention to the social aspect of work can result in both wasted resources and in over-utilised resources.

Despite the accumulation of warning signs in Australia, the GFC was triggered in the USA. Its main immediate effect in Australia was psychological – a reassessment of financial asset values – but it was plain that exports would soon be affected and that the refinancing of overseas debt was likely to become difficult. The banks had already had a foretaste of the latter problem (from 2007 they were unable to offload securitised mortgages) and were poised to implement a credit squeeze.

Governments across the OECD, including many governments which were already heavily in debt, reacted by borrowing and spending, in the hope that a Keynesian stimulus would bring a return to business as usual. In a volte-face compared to its behaviour during the Asian crisis, the IMF approved of stimulation. Comforted by the implied promise that the IMF would help with the resulting increases in the balance of payments deficit, the Commonwealth of Australia felt confident to join the stimulators. But herein, for Australia (and the USA), lies the weakness of stimulation: the boom was doomed because of its dependence on overseas savings. Stimulation in deficit countries which does not include measures to reduce overseas borrowing is liable (at best) to peter out as more and more domestic income is absorbed in debt servicing and (at worst) to end convulsively with a collapse in the exchange rate.

This is but one facet of the exquisite policy quandary which is the Commonwealth’s inheritance from neo-liberalism. Addressing the balance of payments constraint requires an increase in saving, but increased saving is the opposite of stimulus. Worse than this, the market mechanism to address the balance of payments deficit is depreciation in the exchange rate, but this would bankrupt the banks and negate the policy of stimulus. Addressing housing affordability requires deflation of land prices, but that is also the opposite of stimulus. Add climate change to all this and it is no wonder that confusion is widespread in a policy elite schooled to think in neo-liberal terms. The only certainty is that unemployment will increase.
The certainty of rising unemployment arises not only from the limits to stimulus, but from the need for an economic restructuring much more drastic than the neo-liberal restructuring of the 1980s and 1990s. Economic restructurings involve reductions in output in some industries, counterbalanced by increases in others. At best this precipitates frictional unemployment. In the 1980s, through inattention to retraining and similar inattention to investment complementary to the skills on offer, it generated a lost cohort of deskilled workers. This time round, the worry is more that the transition requires a rapid change in both producer and consumer expectations. Needless to say, economic restructuring is resisted by the losing parties, as for example the fierce resistance of the carbon lobby to greenhouse gas emission abatement policies (Hamilton 2007, Pearse 2007). The need for financial arrangements to underpin the restructuring provides the losers with opportunities for resistance which increase the ultimate cost – whether expressed in unemployment or in reduced incomes. Where one of the losers is the finance sector itself these opportunities are magnified.

Beyond Market Measures

Given the seriousness of the quandary, governments which genuinely wish to minimise the increase in unemployment (and the waste of resources which this implies) have no option but to go beyond market measures. An example where we can learn from Australian history is the balance of payments, where as we have seen the market nostrum of exchange rate depreciation is simply not feasible in the present condition of bank balance sheets, and would not work anyway since business is understandably wary of fluctuating exchange rates. Far better to control the exchange rate at a believable level – preferably on the low side, with controls over capital flows if necessary – and apply alternative policies. Australia has long if not always highly successful experience with the support of tradeable production. Industry policy can be revisited, ideally at the expense of non-tradeable activity such as the finance sector rather than by transfer of resources from the more successful tradeable industries to the less. The balance of payments also benefits if consumer demand switches from import-intensive purchases to domestic purchases.
For example, an increase in taxation, spent to household benefit on education and health services, would benefit not only the balance of payments but would reduce carbon emissions (education and health services being two of the least carbon-intensive of Australia’s industries).

A second example where reliance on market solutions is bound to fail is greenhouse gas emission abatement. The proposed market measure is emissions trading which is expected to generate price incentives to reduce the carbon intensity of production (especially electricity production). The danger is that the abatement target will be met by shutting down emissions-intensive production with nothing to replace it – in other words, by reducing economic activity and increasing unemployment. The decarbonisation of electricity requires active government investment. Once it is under way, a further important step will be the electrification of transport (battery cars, electric railways), a step which will have the further benefit of reducing imports, particularly if the electrical equipment can be manufactured locally.

And what of that most difficult imbalance of all, the imbalance that was at the heart of the boom – the urban land market? Is there an alternative to the deflation method of bringing land prices back to affordable levels? Theoretically, land prices can be brought back into line by holding them in nominal value while other prices and incomes are inflated, but it may turn out that the answer is a combination of CPI-inflation and land price deflation, both at manageable rates. Meanwhile the challenge is to address the underlying accessibility patterns, both from the land use and from the transport side.

These three examples testify to the major adjustments asked of all sectors of society. If aspirational consumers are unable to increase savings and switch consumption patterns, the result will be delayed adjustment and high unemployment. If the carbon and finance lobbies postpone adjustment, the eventual changes will be cataclysmic and will generate high unemployment. If commentators, politicians and governments insist on continuing to apply neoliberal economics, the result will be delayed adjustment and high unemployment.
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The world faces a twin threat from simultaneous economic and environmental crises. Human society, now heavily urbanised, will mostly encounter these threats in cities and large human settlements. The crisis of financial capital is a crisis of financial capitals, the urban hubs of neoliberal global order. In an era of globalised interdependency, the pain of the wealthy metropolitan centres will likely be the agonies of the world’s poorer peripheries. David Harvey (2009) writes:

My guess is that half of the financial crises over the last 30 years are urban property based. The origins of this crisis in the United States came from something called the sub prime mortgage crises. I call this not a sub prime mortgage crisis but an urban crisis.

Australia and its cities remain on the margins of the crisis. We don’t yet feel the searing pain that is so apparent in global pivots, like New York, or aspiring tigers like Dublin, where unemployment soars as public finances plummet. And yet our cities are already on the edge of social and environmental defaults that widened during the era of neoliberal rule (McManus, 2004). Australian author and social commentator, John Birmingham (2009) depicts ‘The Coming Storm’ whose advance clouds are already engulfing those in vulnerable employment sectors, like mining, business services and manufacturing, where retrenchment and reduced hours are the norm.

The tempests of global warming and resource (especially oil) volatility threaten the fundamental circulation and health of an urban process that produced ever higher velocities. This process pushed continuously...
against the constraints of time. Time is the agent of delay, decay and debility which reminds us that we exist in nature not outside it. In doing so, as Harvey (1982) reminds us, the urban process in capitalism seeks ways of overcoming barriers to the realisation of value and profit. The city is a means for overcoming ‘the limits to capital’ presented by the time-space dimensions of nature. As capitalism has evolved – and suffered and survived crises – it has sought new pathways to the realisation of value in city processes. A key instance of this in the twentieth-century was the motorisation of urban mobility to reduce spatial frictions of the labour process.

Crisis Tendencies in the Neoliberal City

In general, in the neoliberal city we observed an urban process that sought to overcome nature and natural barriers through the annihilation of time by space – in this case, the space of the city. This is to reverse the formulation of Marx who a century and a half ago observed that capitalism was a volatile expansive force that deployed technological advance (railways, machines, etc.) to overcome all barriers, including topography and distance. In Marx’s era, through the expansion and improvement of steam shipping, railways, and telegraphic communication, technology was used to accelerate commercial time and overcome spatial barriers – overcoming the tyranny of economic distance.

This process has continued since and with increasing force. Consider economic globalisation and the air travel and telecommunications that have driven it forward. The internet, like nothing before it, is ‘instant time’ that annihilates spatial frictions and links communities and people in a great web of simultaneity. Of course, geography still matters – as geographers like to say – because even the internet cannot overcome political geography. Consider the filtering that many countries like China (and perhaps soon Australia) apply to the web.

Nested within this global crunching of space by time, we see, at the urban level during neoliberalism, the reverse – the use of urban space to speed governance, the economy and everyday life. Cities are spaces of
control, governed by governments and powerful corporations, who often act together to exert authority over change (Harvey, 2008). In the Australian system this view implicates State Governments, corporations and powerful development industry lobbies as the titans in an ‘urban game’. They can form cross-sectoral ensembles to wield power and protect mutual interests. Key examples are the road building coalitions who, with the States, have used devices like Public Private Partnerships to force through unplanned and unpopular changes to our cities: the tollways and tunnels that have torn up urban fabric and cost enormous sums of money.

Sydney’s tunnel debacles in the last few years only partly managed to expose what may be termed a ‘tollway industrial complex’ that has exerted enormous undemocratic power over our cities during the phase of neoliberalism. Brisbane is presently embroiled in a tunnel and tollway construction scheme of epic proportions. This ‘TransApex’ scheme will ultimately prove a very costly and unpopular act of folly. And yet, decades after broad acceptance of the danger and damage of car dependency, the production of road space in Australian cities continues unstoppable, and seemingly unstoppable (Mees, 2000). It remains a deeply embedded, if increasingly faulted, strategy for overcoming mobility barriers to the realisation of value.

Arguably, metropolitan space, and the urban process generally, has been governed in the interests of those wishing to ‘speed things up’. Such interests wish to keep decision making – about infrastructure, about planning, about basic urban priorities – ahead of public comprehension, beyond the ordinary politics of democracy which neoliberal advocates tend to despise as a brake on the things that matter to them: growth and profit, narrowly conceived. In this way space – especially city space – is used to annihilate time, the time of democracy. As Harvey explains in his *A Brief History of Neoliberalism* (2008), neoliberals see democracy as a hoarding behind which lurk deliberation and dissent. These are regarded as infuriating societal tendencies that delay the supremely significant work of production and gratification.

Economic velocity was axiomatic to neoliberalism – it was as if we needed ‘chronic activity’ to keep us busy, the system furiously humming to forestall any awareness and discussion of the mounting balance sheet
of social and environmental debt. This was achieved in an urban process – an urban space – that was sanguine of time. Cities were fortresses of speed, of youth, of debt deferred. By contrast, in many rural and regional areas time could not be vanquished as depopulation, decay and decline set in.

Recall the slogans and language of the neoliberal urban process: boundless mobility, frictionless exchange, easy credit, ‘can do’ governance, policy ‘going forward’, big build infrastructure. Its most memorable emblem was the Kennett Government’s (1992-99) slogan ‘Victoria on the Move’, emblazoned on everything for a time, including number plates and exits to Melbourne’s Tullamarine Airport. The State-wide claim proved misleading. It was ultimately shown to mean Melbourne on the Move as increasingly disaffected country folk watched rural services slow and decline. Meanwhile, back in the city it was ‘all go’: tollways and ring roads were rammed through the urban fabric, the sudden raising of a new city consumption palace, the Crown Casino, and the imposition of corporate events like the Formula 1 Grand Prix on inner urban communities. On the Move: this was not time for consultation and contemplation of alternatives. The ‘urban’, in short, was a space where time was refused. Williamson (2002) essayed and summarised the many deleterious consequences for urban democracy of the Kennett reform era:

The Kennett government’s economic liberal reform ensured that broad political participation in democratic government, social equity and community participation was subservient to the domination of public choice theory, competition and economic progress (2002:18).

This was an order that spoke much of time but did not value it. And yet ultimately time caught up with this space. The Global Financial Crisis is a temporal crisis, of flighty, fictitious wealth at last brought to ground by the claims of the ‘real economy’. The neoliberal order was also deeply Promethean, believing itself free of ecological limits. Resources, the stock of Nature, could be cheerfully priced and somehow thereby conserved sufficiently. This faulted assumption has been exposed by a series of resources crises (notably ‘peak oil’) and natural disasters which can at least partly be laid at the feet of freewheeling growth (see the
article by Dodson and Sipe later in this volume). The horizon of environmental threat has at last been reached: climate change stalks our cities and regions, perhaps as witnessed in the continuing great drought of south-eastern Australia and in the tragic Black Saturday fires that reached the edges of Melbourne in February 2009. The infinite resource time of neoliberal urbanism now looks unexpectedly morbid. A stop clock has been set above the oil pump. Metropolitan planning asserts boundaries and land rationing (or tries to). Water is more strictly allocated. By one means or another, energy is asserting its ‘real price’.

A Crisis of Overconsumption?

The election of the Rudd federal government in 2007 marked political recognition of the increasingly apparent contradictions of the neoliberal model. In 2009, the new Prime Minister published an essay in a national journal declaring the end of neoliberalism (Rudd, 2009). The new wisdom is that financial meltdown and the economic recession which emerged from its wings are crises of indebtedness: of over-consumption and under-saving. The environmental crises are even more straightforwardly the spawn of excess consumption. And yet, these assessments are missing something fundamental. Arguably, both forms of failure are crises of production, not consumption. This is not a minor point of language or economic emphasis. Claims of overconsumption may miss the origins of economic and environmental malaise and overlook the underconsumption of necessities, especially social values, under neoliberalism. Moreover, of deeper consequence than the immediate problem of consumption are two crises of production that intersect in the contemporary global failure: of social reproduction under neoliberalism and of overproduction under longer run ‘carbon capitalism’.

Neoliberal consumption was surely problematical for economic resilience but of less consequence for environmental crises, notably global warming, driven by two centuries of ‘carbon capitalism’. The latter betokens a political economy whose forces of production were assumed to be freed from nature via access to an infinitely abundant carbon legacy (Altavter, 1993). If the claim of ‘infinity’ was resisted in
some dismal quarters, there was always the promise of technical improvement which would ultimately render a finite source boundless. The result was always the same: nature assumed away to the margins of economic consciousness; and time refused.

There exists a looming default in the processes that reproduce the social conditions for production, and of the economy in general. As Harvey (2009) points out, ‘since the 1970s the policies of neoliberalism have been about wage repression’. This has helped to effect the process of ‘accumulation by dispossession’ which Harvey (2005) earlier described as central to the neoliberal project. Since 1975 in Australia, labour’s wage share of national income has decreased by over 12 per cent, whilst the share to profits has increased by nearly 50 per cent (Pusey 2003: 201, calculated from Table C.4).

This shift, reinforced by reforms that directly or indirectly effect wealth transfers (e.g., privatisation of public assets, deregulation of labour), has been reflected in a new urban geography of polarisation (residential segregation) and disadvantage (homelessness) in the neoliberal Australian city. Fresh ruptures in the social fabric of reproduction have manifested as poverty sinkholes, ‘crime hotspots’, and rising social and health morbidities in poorer communities. Around 100,000 Australians are homeless, while over 700,000 have been consigned to the netherworld of the Disability Support Pension (Australian Government, 2008).

The current GFC is revealing a more generalised legacy of social vulnerability under neoliberalism. Mortgage failure is spreading amongst the suburban middle class, especially the lower ‘aspirational’ echelons who were encouraged into high levels of household debt. In September 2009 it was reported that nearly one-third of Australia – 33 per cent of postcodes – had fallen into a ‘high-risk’ category of financial distress, meaning they faced the highest risk of defaulting on debts (Ferguson, 2009). In the United States, one in five homeowners now has negative equity in their property (Rundle 2008).

A failure of planning will, and of public fiscal provision, has left middle and outer suburban regions without public transport in the face of soaring petrol and energy costs (Dodson & Sipe, 2008). The progressive
dislocation of urban and housing submarkets that was endemic to neoliberal urbanism, and based on the supposition of boundless mobility, has greatly intensified the consequences of this planning failure.

Ostensibly, the neoliberal project was to rescue the individual from long slumber in the twilight of the Welfare State. And yet, it did everything but that. An age of radical ‘individualisation’ (Bauman, 2000) denied human dependency only to reproduce it massively at the social scale. This scale is glimpsed in the vexed remarks of one neoliberal advocate, Des Moore (Director of the ‘Institute of Private Enterprise’):

It is absurd to have 2.7 million, or 20 per cent of the working-age population, receiving income support compared with only 15 per cent at the end of the 1980s, and 4 per cent in 1969. Social assistance benefits now contribute 14.3 per cent of gross household disposable income. This compares with just 8 per cent under Whitlam (cited in Gleeson, 2006: 41).

In pursuit of structural economic reform, neoliberalism engendered a rate of social dependency that made the state more, not less, crucial to everyday life.

In Australia, before the great slide of 2008, the average ‘sovereign consumer’ could afford much of the staple coming from countries where wages were low and environmental costs ignored. But many critical mainstays of health and well-being were unaffordable. In the era of ‘Made in China’ affluence, a DVD player was inexpensive but basic dental care was beyond reach for many. The evidence was declining indicators of fundamental well being, such as oral health, in the general populace, but especially in the lower orders. To illustrate the point, it was recently reported:

More than 650,000 people are on public dental waiting lists across the nation…with the dental health of children worsening and rates of tooth decay and gum disease well above many other developed countries (Clayfield, 2009).

In the wake of the global crisis, much has been made of the overproduction and overconsumption of ‘fictive economic value’, including ephemeral housing wealth. Much of the consumer good
streams that were brought within reach of the middle and lower classes during the era of aspiration carried fictive human value, unrelated to basic human needs. The expanding flow of household consumer goods did little to aid the cause of social reproduction.

Fictive value was also manifest in the collective consumption areas recast by neoliberal reform. In particular, human services, including health, disability, childhood and aged care, were remade into forms that actually entrenched social vulnerability (see the recent assessments in King & Meagher, 2009). In the mental health and disability fields, state dependants were reconstituted as consumers. And yet, as the failures of ‘reformed’ (marketised) human services were revealed internationally, this was shown to be subjectivity without agency. The homeless army of mentally ill souls is testament alone to that proposition. In early childhood and aged support, publicly subsidised corporates produced miserable, and ultimately crisis prone, modes of care. The limits of subjectivity under neoliberalism were never more apparent than in care fields where the subject was a ‘unit of profit’. Despite driving costs and conditions downwards, the corporates could not extract sufficient value from care, even with generous state subsidy.

The 2008 collapse of the Australian multinational childcare provider, ABC Learning, epitomized the widely failing cause of social reproduction under neoliberalism. The developmental needs of children, the next embodiment of society, were discounted by the lust for economic gratification. Future social time was thus discounted. The evidence presented by leading child health expert, Fiona Stanley, shows that Australian children were fatter, sicker and sadder than their forbears. The magnitude of the threat to reproduction was captured in the warning by child experts, including Stanley, that the ‘present generation of children may be the first in the history of the world to have lower life expectancy than their parents’ (Stanley et al., 2005:52).

The simultaneous escalation of national wealth and childhood morbidity has been registered in many developed countries. The Canadians Keating & Hertzman have described this as ‘Modernity’s Paradox’. In the US, the psychologist Myers believes that compared to the 1950s, contemporary Americans:
…are twice as rich and no happier. Meanwhile the divorce rate doubled. Teen suicide tripled...Depression rates have soared, especially among teens and young adults. I call this conjunction of material prosperity and social recession the American paradox.

To summarise, the crisis of social reproduction under neoliberalism reflected a gross underconsumption of social values. By condemning consumption generally, the new ‘progressive’ politics emerging in the wake of neoliberalism neglects two things:

- the looming crisis of reproduction that is the principal social legacy of neoliberalism; and
- the immiseration and underconsumption endured prior to the neoliberal default by many social groups, notably, the homeless, the mentally ill, the unemployed and the swelling ranks of casualised labour.

The Question of Overproduction

Finally, the threat of climate warming, already manifest, is a root consequence of overproduction, not overconsumption. In capitalism the market is a dynamic, self valorising force. Market relations are characterised by relentless, convulsive expansion, not equilibrium or ‘steady state’ optimality. The unplanned nature of capitalist competition means that, periodically, ‘individual capitals, industries, sectors, experience difficulty in selling their entire output’ (Bottomore et al., 1991: 405). It is ‘only by accident, or by theoretical idealization, that a situation of equilibrium can prevail in all branches, with output matching demand…’ (ibid.) Market relations thus relentlessly drive aggregate output beyond social need and thus ever towards the precipice of overproduction. Harvey (2008: 24) writes:

Capitalists have to produce a surplus product in order to produce surplus value; this in turn must be reinvested in order to generate more surplus value. The result of continued reinvestment is the expansion of surplus production at a compound rate...paralleled by the growth path of urbanization under capitalism...The
perpetual need to find profitable terrains for capital-surplus
production and absorption...presents the capitalist with a number
of barriers to continuous and trouble-free expansion.

This inexorably drives a twin territorial expansion: for the *extraction* of
resources (human and natural) and for the *absorption* of waste – or in a
word, *globalisation*. In the converging fields of contemporary climate
science and climate debate, the question of ‘absorption’ comes starkly
into focus. The constant expansion in productive capacity ‘puts
increasing pressure on the natural environment to yield up necessary raw
materials and absorb the inevitable waste’ (Harvey, 2008: 24).
Economic globalisation, given new impetus by neoliberalism, produced
new terrains for resource extraction but it did not expand the atmosphere.
Therein lays the source of the problem of climate change, which has
arisen from historical overburdening of the atmospheric terrain.

The dream of green reform – of industrial ecology, of ecological
modernisation – is that economic growth can be decoupled from this twin
territorial expansion. This strongly cherished but weakly embraced ideal
may never be meaningfully falsified. The global ecological crisis – of
declining resource reserves and of failing waste absorption – betrays a
systemic disinterest in reform, whatever its theoretical possibilities. The *
limits to growth* was circumvented by the growth path of globalising
capitalism. Wright (2004) observes:

> Ecological markers suggest that in the early 1960s, humans were
> using about 70 per cent of nature’s yearly output; by the early
> 1980s, we’d reached 100 per cent; and in 1999, we were at 125
> per cent. Such numbers may be imprecise, but their trend is clear
> – they mark the road to bankruptcy.

Australia encounters the twin global economic and ecological crises after
seventeen years of continuous growth. This unprecedented expansion –
the ‘The Longest Decade’ (Megalogenis, 2008) – has not, however,
bequeathed a legacy of affluent resilience. In many social departments
there are no excess stocks to run down. Social malnourishment is
nowhere more apparent than in the interstitial spaces of the nations’ cities
where the unhomed lurk in quiet desperation.
Decades of green censure have done little or nothing to reset the path of consumption, which remains set on ceaseless expansion. We may recall Erich Fromm’s (1942) warning that the destructive contradictions of individuation would drive the flight to mass consumption but that this would provide no solace for the drudgery of everyday life. Cultural critic Terry Eagleton provides another critical view of work and consumption in contemporary market societies:

One of the most powerful indictments of capitalism is that it compels us to invest most of our creative energies in matters which are purely utilitarian. The means of life become the end. Life consists in laying the material infrastructure for living. It is astonishing that in the twenty-first century, this material organization of life should bulk as large as it did in the Stone Age (2007:155).

Neoliberalism has generated, however, a new crisis in the provision of this ‘material infrastructure for living’, which is now denied to many. It also hastened at the same time an overproduction of ‘material organisation’ that now threatens the world with natural default, especially in the form of global warming. This twin crisis opens an urban age. Its consequences may extend far beyond the contemporary Global Financial Crisis. The new social and ecological crises facing the world’s cities may be our greatest species challenge yet.

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A NOTE ON THE CREDIT CRISIS, TIME AND SOCIAL ORDER

Stephen Horton

The materialisation of space-time is a central project for capitalism. Within the finance sector, the relationship between the (exchange) value of money now and the (capital) value of money in the future is a central structuring principle, effecting interest rates and financial stability. This short note analyses the relationship of the two forms of modern money in the context of the 2008/9 global financial crisis. It argues that the state’s socialisation of private toxic debt has meant the internalisation of ‘negative time’ within the public sector. The note concludes with some suggestions as to the effects of this new temporal dimension in the structure of the state and its social control.

Money and Time

Marx first proposed a duality of modern money as a means of circulation and as a store of value (cf. Marx, 1976: 188 – 247). This dual nature of money in the capitalist economy is reflected in overnight inter-bank credit and treasury bills and is the starting point of this explanation of the current crisis.

At the height of the financial crisis the ‘TED spread’ was widely used in the popular media as a measure of the freeze in credit. In arithmetic terms the TED spread is the difference between the (positive) interest rate on overnight, inter-bank loans and the (negative) interest or discount rate on short-term, 3-month U.S. government securities (‘T-bills’). These two interest or flow rates apply to different forms of money. Overnight inter-bank credit allows banks to manage the cash flow of large withdrawals and, more importantly, to meet (overnight) money-reserve obligations. Such credit creates money at the terminal point of market
exchange: money-for-payment, the most ancient form of money. At the moment of payment, the nexus of circulation, money, passing from debtor to creditor, is suspended between propriety interests, and thus, momentarily, stilled-in-time. The frictional flow of materialised money – or money-flash-frozen, as it were, in the moment of pure exchange – is measured in the overnight, interbank credit rate.

The Treasury or T-Bill, in contrast, exchanges, or makes equivalent in a promissory note, less money now for more money in the future. It discounts the present to a (larger) future. In a frame of positive time, it proffers, for example, $1,000 to be liquidated 3 months hence for $998 (now). In so far the 3-month T-Bill backed by the full authority of the state is risk free, the interest/discount rate of the note reflects the most basic value of the passing of contemporary time. It is an index of the vitality of money, its capacity, at a particular historical juncture, to increase itself. It traces, in short, the life force of capital. As Marx noted: ‘[M]oney which begets money’, such is the description of capital given by its first interpreters …’ (Marx, 1976: 256).

Substantively, the TED spread subtracts the dynamic force of capital, of money impregnated with time, from the inertia of money stilled in the immediate relation of payment. Figure 1 (shown in graphical form on the next page) traces the relation of the two money times over the last decade and their resolution in the TED spread. It shows movements in (a) LIBOR - the London Interbank Offered Rate – which is a measure of the interest rate on overnight interbank loans; (b) the interest rate on US T-Bills; and (c) the TED spread – that is, (a) minus (b).

The limit case of the relationship was precipitated by the U.S. state response to the bursting of the dot-com speculative bubble (when the technology rich NASDAQ stock index peaked in March 2000). As interest rates were rapidly reduced - the T-Bill rate falling from over 650 bps to 160 bps in December 2001 - the LIBOR rate, in face of rising financial optimism induced by the credit easing stimulus, fell in concert. In the third quarter of 2001 the two rates simultaneously reached approximately 200 basis points (bps) and the TED spread touched zero as money flowed indifferently between its two forms of expression.
Figure 1: Interest Rates and the TED spread
In more ‘normal’ times, the friction of money-as-a-medium-of-payment exceeds the force of money-which-begets-money by a marginal amount. There is, in short, a structural preference, when all is said and done, for the immediacy of money-in-the-hand.

Figure 1 (opposite) shows basic now-money and the fruitional value of 3-month capital closely tracking each other in all but the last period. These are the upper two lines in Figure 1. In the first seven years of Millennium plenty the two values – LIBOR and T-Bill – despite ranging between 100 and 670 basis points, differ by no more than 50 basis points and, for a long period, are within 30 bps of each other (100 bps ≡ 1%). So the TED spread (the lowest of the three trend lines in Figure 1) remained small and quite stable until early 2007.

Then, in mid-2007, as ‘sub-prime’ credit problems became current, the frictional preference for money in the hand, as measured by the TED index, jumped 240 basis points. The US state responded with an aggressive cut in interest rates. The signal reduction of capital vitality induced, after a number of hesitations that pushed the TED index back up, a greater fall in the friction of money-as-payment. In early 2008 the TED index, the friction of money flow, stabilised at around 130 bps. In October, as the T-Bill trace of the vitality of capital declined to zero (for the first time since 1929) the LIBOR, far from mirroring the decline, spiked (with the TED spread) to 465 bps. As interest rates fell the LIBOR rose: a structural relation had been reversed.

The disruption of the relationship between future-money and now-money may, immediately, be ascribed to a crisis in confidence. Bankers no longer expected money, even overnight money, to beget money: rather, they feared, money would be lost. Money, in short, acquired a negative temporal connotation. Loss producing debt is iconic negative money-time. In bad debt capital turns pathological and money destroys money. In a crisis the negative money time of toxic assets brings the positive thrust of capital money to a halt. The flow of money no longer divides in two forms but is brought to a halt in the inertia of a single preference: for money in the hand, ‘now money’.
State Response

The October 2009 spike in the TED spread, a signal of clear and structural danger, forced the hand of the (neo-liberal) state. The global response, from the USA to China, was twofold. The most urgent initiatives exchanged good (public) money for bad (private) debt: the suggestion of ‘bad’ banks being symptomatic. In so doing the state transferred the negative time of money from the sphere of finance to its sphere of politically mediated social order.

The second major state initiative has been Keynesian stimulation of aggregate demand with infrastructural spending, tax cuts and, even, cash ‘gifts’ to individuals. The effects of this increase in the flow of money for payment and the transfer of negative time from the finance sector to the state are reflected in Figure 2 below.

Figure 2: Three Month US Treasury Securities Yield

Source: The Financial Forecast Center™ (http://forecasts.org/3mT.htm; accessed 18.4.2009).
The state interventions have done little for the vitality of capital, with the T-Bill rate rising only marginally above zero. The LIBOR, on the other hand, in concert with widespread ‘cash’ stimulation, has fallen sharply, reducing the TED spread to approximately 100 bps. This remains 70 bps above the historic norm of 30 bps. It remains an open question as to whether, and, if so, by how much, state intervention can restore the vitality of capital. Beyond the political friction of intervention there is a definite financial limit to the amount of good money the state can create. The lingering ‘lost decade’ of Japanese capital has been widely used to suggest the possibility of chronic economic lassitude. The concern of this article, however, is not economic prognosis but some first suggestions of the consequences of the internalisation of negative money time in the state.
State Time

The thesis is that the crisis accentuates the tendency towards an extended and intensified hyper-neoliberal state. Neo-liberal here denotes a core belief in the market economy, a firm assumption of social order and an often rhetorical commitment to representative democracy. The contemporary extension of social order is readily manifest in recurrent policy announcements and the expenditure of trillions of dollars of public money. It is, however, not only the scale of intervention that is novel, but also its content. As the US Administration forces Chrysler into bankruptcy, sets parameters for bank existence (i.e. stress tests) and pronounces on market privilege (i.e. executive salaries), an Australian newspaper, in a report headlined King Kevin and the big end of town, characterises the consequence of the past year as follows:

From Rudd Bank to broadband and mortgages, the Government is everywhere in corporate life. There is a new gorilla on Australia's corporate scene … In the chaotic final months of last year when markets were dysfunctional, the Rudd Government's new hands-on role was accepted almost blindly (Murray, 2009).

The dependence of the modern (political) state on finance capital is well established. Former US President Bill Clinton infamously confessed he always monitored bond market reaction to a major policy announcement. Now, it is proposed, the state is being constituted beyond its traditional form as instrument, albeit it a politically contested one. The hyper neoliberal state is an emergent economic stakeholder. While the neo-liberal state had derivate interests in market profit, in contemporary crisis mode the state has acquired a property interest in money-which-begets-money. More immediately it has acquired a property interest in money-which-destroys-money; that is to say, negative time embodied in toxic debt. The state must, at the level of structure, account for this time.

Time is elemental to modernity. In 1964 ‘the first prophet of the electronic age’, a seer of the globalised world of 24/7, declared: ‘Today, after more than a century of electric technology, we have extended our central nervous system in a global embrace, abolishing both space and time as far as our planet is concerned’ (McLuhan, 1964: 3). The state, in the perceived bureaucratic inefficiency of the nation state, has long been
seen as a partial exception to, or laggard of, this rule of modern time and space. Its interventions, both tardy and, in the global village, narrowly focused, have also been, in neo-liberal times, limited by a belief in the über-efficiency of the hidden hand of the market.

Symptomatic of time in the neo-liberal state, it is pertinent to observe its use by political leaders. In 2005, for example, it was noted that ‘... no modern president was a more famous vacationer than Ronald Reagan … Reagan spent all or part of 335 days in Santa Barbara – a total that [George W.] Bush will surpass this month in Crawford with three and a half years left in his second term’ (VandeHei and Baker, 2005). The President’s average annual leave, in excess of 2 months, is in contrast to down time in the private sector: ‘[t]he sum of the average paid vacation and paid holidays provided to U.S. workers in the private sector, 15 in total’ (Correspondents, 2007). In Australia workers are entitled to 28 days of annual paid leave, again miserly in the context of the neo-liberal Howard administration that the formidable Paul Keating described as, the ‘laziest, most indolent, unimaginative in our post-war history ... 10 years in a hammock’ (Australian Associated Press, 2007).

These are impressionistic accounts (or, in discourse analysis, signifiers to be interpreted) but in either case there are good reasons to think that, recently, much has changed. In the US and Australia current administrations find themselves in an expanded, executive role organising not only the conditions of finance capital but, increasingly, both the broad economy and wider society. Central banks in out of sequence meetings ‘slash’ interest rates; Australian bureaucrats complain of working hours and the Prime Minister curtails Christmas vacations. In its first weeks a new US Presidency distributes $787 billion dollars to financial corporations, industry and consumers. ‘Never before in our history has a tax cut taken effect faster’, declares the President.

In the US and Australia the state is both extending its reach and quickening its pace. Its public officials, with few exceptions, are technically competent before they are politically ambitious (e.g. fiscal conservatives). The hyper neo-liberal state is extending its rational competence to increasing spheres of financial and social life. The contemporary medium of rational competence is information: the representation of social and spatial structures in data of time frozen in assemblage (e.g. the TED spread trace, base-lines, social indicators,
temporal mapping). In its control of cities the hyper modern state can be expected to extend and intensify the imperative of spatio-temporal rationality. Mental labour for the production and processing of data is essential to this task.

The vitality of capital sets a limit to the scope and intensity of state intervention. If the contemporary crisis proves to be something other than a ‘normal’, if extreme, economic/value correction, the ‘rational imperative’ of the state to control space and time as a total social structure will increase.

The Great Depression saw the emergence of a total state intimately associated with finance capital and marked by a distinct social division between organisers (associated with the state apparatus) and the organised. Built on the obsessive keeping of records and processing of data (and, it may be noted, also wedded to the production of images or spectacle – mass rallies, torchlight parades, filmed Olympics), it culminated in fascism. Named for a classic symbol of power (the fasces), it was characterised by a virulent need for control over both space and time. Individuals question its veracity and have yet to find an original source but of the first fascist state it is socially remembered that ‘Mussolini made the trains run on time’. The phenomenal forms of the contemporary crisis are different but the effect of the latest credit crisis is to accentuate the state imperative for informationally-based control over social space and time.

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BUSINESS AS USUAL? RESPONDING TO THE GFC ON THE GOLD COAST

Paul Burton

The nature and causes of the current global crisis continue to generate substantial debate, including over whether it is primarily a financial crisis, an economic crisis, a crisis of political legitimacy or some combination of all. While the roots of the crisis may well lie in the rapid expansion of an unsustainable financial regime it clearly became a more wide ranging economic crisis, posing substantial challenges to the financial rectitude of many governments and to the legitimacy of at least some superficial aspects of the capitalist mode of production.

This article is concerned less with the underlying causes and genesis of the crisis than with its spatial manifestations, or rather with its characteristics as an urban crisis. After considering briefly the analysis of the crisis presented by the Prime Minister, it focuses on manifestations of and responses to the crisis in the city of the Gold Coast in South East Queensland, described by some as ‘our most obvious capitalist area’ or ‘a free market city’ (Jones, 1986) but also as a place of ‘adolescent urbanism’ (Burton, 2009).

The GFC and Rudd’s Response

One of the most common responses to the GFC by governments around the world has been the introduction of packages of public spending designed to shore up vulnerable financial institutions and stimulate
economic growth. The nature of economic growth and the measurement of economic health are important aspects of our understanding of this crisis and thus of how we frame possible responses. Technical definitions of growth and recession also matter when it comes to wider measures of business confidence in markets and public confidence in government. Earlier this year (2009) the Westpac-Melbourne Institute Index of Consumer Sentiment rose by over 23% in two months. This was ‘unquestionably a stunning result’ according to Westpac Chief Economist, Bill Evans, and one attributed mainly to Australia dodging a technical recession while the rest of the world failed to do so (Westpac Banking Corporation, 2009).

Challenging the preoccupation with short term fluctuations in GDP as the main measure of national economic vitality, some political economists have considered the arguments for constructing and applying new measures of growth, progress and well-being (for example, Stilwell, 1999). Hamilton’s Genuine Progress Indicator (GPI) presents one interesting alternative: his comparison of Australia’s GDP and GPI profiles over a 45 year period from 1950 shows a steady increase in GDP but a downturn in GPI from the 1980s onward (Hamilton, 1997). This disjuncture was caused by changes in the underlying distribution of income – with the post-1980 downturn in GPI coinciding with a decline in the share of total income received by the bottom 20% of the population – along with rising levels of foreign debt, the growing cost of unemployment and overwork and rising costs of greenhouse gas emissions. Thus, while conventional economic measures suggested that things had got better for most Australians, an alternative measure indicated that the uneven distributional pattern has had a negative effect, not just on those who directly lost out, but on the aggregate as well.

The distributional impacts of the crisis were not especially prominent in the analysis of the current crisis presented by Prime Minister in his essay in The Monthly (Rudd, 2009). The essay is fascinating, however, both for its content and for the fact that the Prime Minister chose to present his views in an extended essay as well as in the more conventional sound-bite format. The challenge for the social democracy, according to Rudd,
is to ‘save capitalism from itself’. If this is not achieved then ‘new political voices of the extreme Left and nationalist Right will begin to achieve a legitimacy hitherto denied them’. While the ‘unrestrained greed’ of extreme capitalism is to be rejected in principle and regulated in practice, ‘the great strengths of open, competitive markets’ must be acknowledged. In short:

Social democracy’s continuing philosophical claim to legitimacy is its capacity to balance the private and the public, profit and wages, the market and the state (Rudd, 2009:21).

The challenge facing the government is to restore and rebuild confidence in the value and potential of properly regulated markets; but little is said about new forms of government, new machinery and processes of government and the new approaches to policy making that are needed to rebuild this confidence on the ground. Little also has been said to date about how these new approaches to government might apply at state and local, as well as federal, levels and how they might play out in the Australian cities where most of us live.

**Cities and the GFC**

Cities are not just a stage on which the economic crisis is played out. The quality of life for most Australian citizens is heavily influenced by the qualities of the city in which they live: by the nature and location of their housing; by the availability of employment opportunities; the quality of local services and by the ease with which they can move around their city.

Those responsible for managing and planning cities are obliged to deal with growth – positive or negative, actual and potential. They seek out footloose capital in order to stimulate growth in their area and compete with other places for this privilege. They try to organise growth so that it occurs in the places and in the forms they prefer and they must try to influence its phasing and timing. Prospective developers (in the broadest
possible sense of the word) routinely challenge these impositions on their activities for being onerous, ill-considered, causing delay and imposing unnecessary burdens on business. But the regulations provide valuable certainty in otherwise volatile markets, offer a brake on the more excessive proposals and collectivise some of the costs of development.

This is one of the enduring contradictions of urban development and planning in a capitalist society: trying to manage the difficult balance between regulation and facilitation, between reducing the profitability of development through taxation and the need to raise money to provide public goods, and between social investment and social consumption spending (O’Connor, 1973; Saunders, 1981). In Queensland the threat of a fiscal crisis of the local state prompted a recent round of council amalgamations, designed in part to improve their financial sustainability through economies of scale. More generally, there is a related, albeit lower profile, threat to Australian local government in the form of the capacity of councillors and the strategic planning capability of councils – as the following regional case study illustrates.

The Gold Coast and the GFC

The small towns of Southport, Burleigh, Nerang and Elston (later renamed Surfers Paradise) grew in the first half of the 20th century and the whole of this area began to develop a reputation both as a holiday destination and as place of innovative housing development. Canal estates emerged and, from the late 1950s, high rise developments also began to appear and now dominate much of the coastal strip. Strata and community title legislation, along with favourable taxation regimes, further stimulated development and contributed to the Gold Coast’s enduring image as a place of relaxed lifestyles and dubious politics: ‘a sunny place for shady people’ according to Jones (1986). Administratively, the South Coast Town Council became Gold Coast Town Council in 1958 and merged with Albert Shire Council in 1995 to
become Gold Coast City Council, the second largest local government jurisdiction in the country responsible for managing the sixth largest city.

The recent economic crisis has provoked some notable corporate failures on the Coast in the last year (2008-09). The Raptis Group, one of the most prominent local development companies has gone into administration along with local boat builder, Riviera and finance company, City Pacific. While these failures have a potent symbolic value, they also led to considerable hardship on the ground: an army of sub-contractors suffered through delays in the completion of Raptis’ Southport Central scheme; substantial numbers of young apprentices in marine construction and engineering were laid off by Riviera and dependent companies; and many City Pacific investors lost all of their savings. More generally, the local development and construction sector has suffered from a pronounced contraction in the number of property finance lenders and the virtual disappearance of so-called mezzanine financing, previously a popular source of development finance on the Gold Coast (Abrahams, 2009).

There is, however, a sense of *déjà vu* about economic crises on the Gold Coast. In the early 1990s, the Raptis Group only just survived the global downturn of that time but by the end of the decade had bounced back and completed the commercially successful Chevron Renaissance project in the heart of Surfers Paradise. After the slump of the early 1970s, local real estate agents, the McWilliam brothers, formed PRD, which expanded rapidly as the local property sector revived to become one of the largest real estate companies in Australia by the time they were bought by Colliers International in 2006. In a city driven by property development and speculation it is not surprising that periods of national and international economic downturn are accentuated, but nor is it surprising that the economic misfortunes of some provide opportunities for others. Taken as a whole, the city economy has been remarkably resilient over the course of its comparatively short history.

This experience of the Gold Coast emphasises that place matters: that a global crisis will impact differently on the Gold Coast compared with
Brisbane, Sydney or Melbourne. The differences reflect different trajectories of economic development and local economic structures. A city based on tourism and building for an expanding population will have a different exposure or risk profile to one based primarily on manufacturing or financial services. However, the differences are also a product of local governance structures and how local councils, in partnership with other tiers of government, respond to major threats to their local economy.

On the surface Gold Coast City Council was reasonably well placed to cope with the crisis in 2009. Despite the recent loss of substantial revenue streams (from the transfer of bulk water assets to another entity and from the rate revenues lost from Beenleigh’s population as a result of the previous year’s council amalgamations), the Council still had a budget of over $1 billion and an expanding rate base due to the continued inflow of migrants from overseas and from inter-state. State and Commonwealth investment in a new light rail system and a major new university hospital had been secured and two new sporting franchises established for soccer and AFL.

However, the Council faced a substantial reduction in the revenue from fees and infrastructure charges that had been driven by development activity and it continues to struggle with the perennial political challenge of minimising rate increases without cutting local services and other investment programmes.

While councils are regularly criticised in the press for their parochialism and short-sightedness, on the Gold Coast the Council had already embarked on a new programme of strategic planning for its future. The Bold Future visioning project was established in June 2007, with responsibility for overseeing the work and preparing a report to Council given to an Advisory Committee which met for the first time in October 2007 and submitted its final report to Council in November 2008. The Advisory Committee included representatives from many sectors and commissioned an extensive programme of public participation and community engagement.
A noteworthy aspect of this process is the high degree of consensus around the key principles to be applied when planning for and managing the future growth of the city. The overall vision for the future of the city over the coming 30 years is increasingly green, including a desire to see more vegetation cover within the city and a general disposition towards more localised lifestyles, with greater opportunities to work, learn, shop and play within distinct communities. This green vision also includes a clear preference for better connections between these smaller sub-city scale places that offer feasible alternatives to private car use and recognition that new forms and sources of employment will be needed if the growing population is to have reasonable opportunities for relatively secure and well paid employment.

As the economic crisis unfolded early in 2009, a different approach to planning for the future emerged in the city – one in which the interests of the development industry, never enamoured of the green and open, consultative character of *Bold Future*, were more prominent. The *Gold Coast Bulletin*, in conjunction with Griffith University and Business Gold Coast, hosted a half day event in March 2009 designed to identify local ‘shovel ready’ projects that would help the city deal with the economic crisis. Based loosely on the Prime Minister’s 2020 summit, the event brought together around one hundred local people, most invited because of their perceived knowledge and experience of business, commerce, tourism and property development, but with around one third of places filled by individuals who nominated themselves through the pages of the *Bulletin*.

The proposals that emerged from this process have since been promoted regularly in the *Bulletin* and supported by Gold Coast City Council (GCCC, 2009). They have included increased support for tourism promotion, the development of new eco-tourism opportunities and the integration of education and R&D facilities at the Gold Coast Health and Knowledge Precinct. One set of proposals signals a concerted effort to restore the principles of the old regime of governance on the Gold Coast. It echoes the views of the Urban Development Institute of Australia and the Property Council of Australia and reflects a belief that the
development sector would be best placed to meet the challenges of growth in Australian cities if its development proposals can be realised on land within an ever expanding urban footprint, are approved quickly by local councils and are supported by infrastructure paid for by local general taxation rather than by specific charges.

Buttressed by research that even The Australian described as of questionable rigour (Ryder, 2009), this viewpoint is unable to countenance the possibility that suburban expansion may already be unsustainable, let alone in a low carbon future, that complex development applications may take time to properly determine and that the public at large is resistant to increases in general taxation to underwrite the profitability of housing developers.

How has the Council dealt with the challenges illustrated by these different visions for the future of the city? In practice it is working within existing legislative and policy frameworks to plan for the longer term future, while trying to manage the short term political pressures of fiscal and social responsibility. It has prepared a Climate Change Strategy that proposes a number of modest measures (methane capture from landfill, green vehicles for council staff, and energy efficiency measures in council buildings) while avoiding issues such as coastal protection and the prohibition of new building in flood prone areas. It is currently reviewing its Planning Scheme and aspires to produce a clearer and simpler scheme that delivers good outcomes in a timely manner, but it is struggling with uncertainty created by a state-level transformation of the Integrated Planning Act into the Sustainable Planning Act.

More generally, the challenges faced by the Gold Coast City Council are those faced by many of the larger Australian cities: reconciling the short term imperatives of the electoral cycle with the longer term challenges of managing a relatively fixed urban environment; dealing with the inter-organisational problems of a three-tier system of government; meeting growing demand for social and physical infrastructure within a constrained budget; and exercising clear and strong leadership while trying to engage effectively with the mass of the population.
Conclusion

Towards the end of the most recent long boom period of Australian capitalism, described by Lloyd (2008) as its ‘millennial phase’, the local state on the Gold Coast showed some signs of a new regime of governance with greater emphasis on long term planning and strategic intervention. In earlier periods it had been seen, correctly in the main, as a local regime dedicated to serving the direct interests of local development capital. Its planning scheme in the 1980s was described as a ‘convenience document’ (Jones, 1986); and what was good for developers was generally held to be good for the city as a whole.

In the early years of the new millennium, however, there were signs that the Council was prepared to pursue a more modern approach to planning and to negotiate vigorously with developers to achieve higher quality architectural and urban design outcomes. The Bold Future process indicated a commitment to a longer term and more strategic approach with a greater emphasis on social and community planning in the still rapidly expanding suburbs. This can be interpreted as an acceptance that urban growth might mean more than just an increase in population and house construction. As Wilkinson and Pickett (2009: 247) have said, ‘further improvements in the quality of life no longer depend on further economic growth: the issue is now community and how we relate to each other.’

The effect of the current economic crisis has been to restore the primary concern of all tiers of government with economic growth. In urban Australia responses by government to the crisis have typically been limited to traditional economic stimulation measures in the face of familiar calls from developers for public subsidy and reduced regulation. There is little evidence of different conceptions of growth figuring in the discourses of national and local politics; and embryonic local plans for more sustainable urban futures appear to be under threat. However, the medium-term prospects remain contestable, as the experience of the Gold Coast illustrates. Meanwhile, although some commentators have asked,
'crisis, what crisis?', it might be more appropriate to describe the current state of play as 'business as usual'.

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**LABOUR and INDUSTRY**

*A Journal of the Social and Economic Relations of Work*

*Volume 20, Number 1: August 2009*

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While the ‘ground zero’ of the Global Financial Crisis has been among the metropoles of financial capitalism, the material grounding of the crisis has been in the urban periphery at the intersection of, land, housing, credit, energy and transport. It has been a suburban crisis, with its faultlines fracturing most prominently across the USA but with major tremors and aftershocks in other heavily suburbanised economies, such as Australia, New Zealand, Canada and the UK. In turn the global financial crisis threatens to reshape suburbia in uncertain and unpredictable ways.

This article explores how the crisis interacts with more long-standing stressors pressing against Australian urban housing, credit, energy and transport systems. It raises questions about the implications for Australian suburbia of a forthcoming era of insecure energy supplies and wider limits to urbanisation.

Finance, Credit and Urban Planning

The immediate locus of the global financial crisis has been among financial institutions with immediate and secondary exposure to risk within the US home loan market. The collapse of major financial institutions has been tied specifically to the failure of a range of 'sub-prime' mortgage instruments. But a mortgage (typically the credit
foncier form) is a specific socio-tenurial relation that orders credit, space, labour, technology and energy within a particular urban temporal diagram. The modern material expression of this diagram is overwhelmingly suburban. The moment of recent failure has been in the synovial joints linking money, land, fuel and transport technology. Credit backed by land, in the form of mortgages, underpins large tracts of modern financial systems. But petroleum, the great energiser of post-WWII suburbia, is no longer a reliable fuel for credit-based urbanisation.

The regulatory regime of modern town planning is both a response to and codification of the spatio-temporal imperatives of capitalist urbanisation and the tensions and contradictions generated by the simultaneous expansion of space and compression of time (Harvey 1989). The concentration of capital in time-space and competition for space produced the ‘housing problem’ of accommodating labour that has for more than a century been conundrum for business and state alike (Harloe 1995). Most solutions tried so far have pursued a version of the suburban formation, from the municipal socialism of the early tramway suburbs, the normative Garden City and Anglo-Swedish satellite town, to the extensive Australian suburb or the dispersed sprawl of suburban USA (Hall 1996).

Value in land is a correlate of accessibility – a relationship that is conventionally analysed through neo-classical bid-rent curves and distance decay gradients (Muth 1961; Wingo 1961; Alonso 1964). Suburban spatial accessibility depends on fuel and technology to overcome the temporal frictions of urban space. Suburbia fertilised by fossil energy-time proved a rich pasture for the harvest of money-credit. Home ownership expanded to the masses, embracing the cities with a ‘mortgage belt’.

Land, housing, space, transport and debt are thus intimately linked in the political economy of the suburban assemblage but are also subject to the ongoing crises that affect components of the system and make battlers of suburban residents.
Growing Stresses: The USA and Australia

In the USA of the late-1990s the weakening of restraint on credit and the risks to accumulation this implied stimulated the penetration of mortgage lending into weaker and weaker segments of the socio-economic structure. This penetration was translated into suburban space through real estate and land development processes. Except for a few historical (industrial-financial) centres like Chicago, New York or Boston, US cities are almost entirely automobile dependent (Newman and Kenworthy 1989).

Petroleum prices rose from around US$25 per barrel in 2004 to over US$140 per barrel in 2008. The early effects of this oil impost on the global economy were difficult to discern and were probably masked in part by the positive short-run consumption effects of sub-prime lending in the US. Secondary circuits of capital flowing from oil producers also shielded the global economy from direct impact, as did further flows of capital arising from the undervaluation of Chinese labour.

Nevertheless, the cost of petroleum imports to the US grew sharply, from just over US$125 billion in 2000-2003 to over US$450 billion by 2008 (as shown in Figure 1 on the following page). With global GDP remaining fairly robust in the interim only a few commentators sought to enquire as to what effect high oil prices might have on the global economy.

One obvious effect has been on the automotive sector, which is directly exposed to higher fuel costs. For the first time in more than 20 years US total vehicle miles travelled declined over a sustained period, with the inflection occurring between 2007 and 2008 (as shown in Figure 2 on the following page). In parallel the US automobile industry, which had demonstrated persistent intransigence in the face of demands for more efficient vehicles, saw collapsing sales and floundered towards a state bailout.
Figure 1: Value of US Petroleum Imports, 1999-2008, Millions of Dollars.

Source: Bureau of Economic Analysis (2008)

Figure 2: Vehicle Miles Travelled, USA, 1984-2009.

Source: US Department of Transportation (2009).
Official and civic discussion of the global financial crisis has largely avoided consideration of the links between the failure of the suburban sub-prime land and credit system and the higher transport costs imposed by the 2004-2008 oil shock. Among the few to interrogate such links, Hamilton (2009a: 39) has tested the effect of the 2004-2008 oil shock on the US macro economy and concluded that:

At a minimum it is clear that something other than housing deteriorated to turn slow growth into a recession. That something, in my mind, includes the collapse in automobile purchases, slowdown in overall consumption spending, and deteriorating consumer sentiment, in which the oil shock was indisputably a contributing factor.

Hamilton has had a long-run interest in the links between the US economy and petroleum prices. He has shown that seven of the past nine US recessions were preceded or accompanied by a run-up in oil prices. Viewed from this perspective, the recent financial collapse is one of a series of economic failures that are linked to petroleum dependence which in the USA is intimately tied to suburban arrangements. The current crisis is more intense and extensive because it has occurred in combination with rapid global economic growth and a decided weakness in the debt capacity of a major economic sector – suburbia – that is heavily dependent on petroleum.

Cortwright (2008: 1-2) noted two links between higher commuting costs due to the oil shock and the incidence of sub-prime foreclosures in the USA:

First, there has been an income effect. Suburban households spend more of their income on transportation, and gas in particular, and have, therefore, taken the biggest hit to household budgets from gas price increases. As a result, they have less income to spend on housing. Second, there has been a price effect. Because distant suburban housing requires more driving, potential buyers are now willing to bid less for houses at the suburban fringe.
In Australia approximately 50 per cent of the national population is found in the middle and outer suburbs of the nation’s major cities (O’Connor and Healy 2004). The US experience has not been directly replicated in Australia, however. Some patterns suggest congruity. For example, households in Australian suburbia depend on automobiles for approximately 80 per cent of their travel. Petrol prices increased from around $0.85/L in 2004 to over $1.60/L in 2008, generating considerable additional household financial stress (Dodson and Sipe 2008b). Australian household debt hit a record high of 160 per cent of income in early-2008 (Reserve Bank of Australia 2009). Repossessions have grown in recent years but the most recent (post-crisis) evidence suggests they have begun to moderate. Australian households have been rapidly deleveraging in the face of the global financial crisis and the prospects of an Australian recession; household debt to income ratios fell 6 percentage points in the 9 months to December 2008 (RBA 2009).

Unlike its US counterpart, Australian suburbia appears to have avoided the most profound impacts of the global financial crisis. This performance is in part due to a range of state interventions, including rapid drops in official interest rates, aggressive fiscal largesse through tax credits for lower income segments and generous first home owner grants that have reinflated the housing-finance system. It is difficult to get precise data on the latter effects, but the spatial impact of first home owner grants is overwhelmingly suburban (Productivity Commission 2004).

There is also evidence that Australia’s suburban households have been adjusting to the less certain environment of the past few years by altering their travel behaviour. Those with access to good quality services can offset vehicle running costs by using collective transport. Public transport patronage in the major cities has been growing sharply (Dodson and Sipe 2008b) and in some cities has generated considerable civic concern, especially in Melbourne where state transport capacity has been institutionally weakened (Mees 2005). In Brisbane public transport use grew by 12.5 per cent annually during 2004-2007, from 3.5 per cent annual growth in the previous three years (Translink 2007). In addition,
Australian motor vehicle sales have changed in both number and composition as households reduce ownership levels and downsize to smaller cars. This in turn has affected the viability of the Australian motor vehicle manufacturing sector which faces an uncertain future (Bracks 2008).

Long-Term Implications

It is probably too early to discern what the longer run impact of the global financial crisis will be on Australian cities. The effects of the oil shocks were still working through the urban economy at the time the financial crisis intensified. And some of the sharper aggregate effects of the petroleum shocks on Australia’s national economy were offset by rebounding revenues from exports of other fossil energy sources such as coal and gas. Coal is a stationary energy though and is unsuited to the fluid mobility needs of extensive suburbia. Even if complex coal liquification technology was adopted Australian suburbia would still feel the petroleum pinch. In the medium term the state will likely need to play a much greater task of supporting the suburban matrix through injections of transfer payments and infrastructure, as well as stabilising commercial and retail development. This, however, will likely prove unsustainable, both functionally and fiscally, without a dramatic, broader and sustained reconfiguration of the role of both the state and of suburbia.

Considerable uncertainty surrounds the future trajectory of petroleum prices which, in early-November 2009, sit at an uneasy US$78 per barrel. There is a growing acceptance, if not yet complete consensus, that the world faces serious petroleum supply problems over the long term. Many observers point to the real possibility that global oil production may enter a permanent decline within the next decade (e.g. Birol quoted in Hurst 2009). Urry (2009) has warned of an unstable ‘resource capitalism’ erupting from these compounding pressures.

Research in Australia by Dodson and Sipe (2007; 2008b; 2008a) and Baum and Mitchell (2009) shows that the particular household level
impacts of the global financial and energy crisis are likely to be spatially differentiated. Lower socio-economic status households in the most car-dependent suburbs – with the most fragile housing values and weakest labour markets – are likely to fare much more poorly than higher socio-economic groups in ‘transit-rich’, high housing values and strong labour market areas. Dodson, Sipe and Li (2009) have further shown that eco-vehicle technologies are unlikely to offer much of a medium term salve; their high cost puts them out of reach of the many low income suburbanites driving old large ‘battlermobiles’. Newman (quoted in Campion 2008), speaking on the energy and climate challenges facing Australian cities, has suggested that it ‘…will mean a new residential abandonment in car-dependent suburbs. There will be wealthy eco-claves surrounded by Mad Max suburbs’. Considerable state action will be required to avoid such a distressing reconfiguration of Australian suburbia.

It appears the world will face a protracted period of weak and unstable credit markets combined with increasingly insecure global petroleum supplies set in a wider context of economic fragility (Hamilton 2009a). Speaking in the US context, Hamilton (2009b) has warned that:

Notwithstanding, the recent rise in oil prices again underscores the present reality of the long-run challenges. Even if we see significant short-run gains in global oil production capabilities, if demand from China and elsewhere returns to its previous rate of growth, it will not be too long before the same calculus that produced the oil price spike of 2007-08 will be back to haunt us again.

The International Energy Agency’s chief economist (Birol, quoted in Connor 2009) has become increasingly concerned at the implications of weakening global oil supply for the post-GFC recovery of the world’s economies, stating that:

[T]he global economy will still be very fragile, very vulnerable. Many people think there will be a recovery in a few years' time but it will be a slow recovery and a fragile
recovery and we will have the risk that the recovery will be strangled with higher oil prices.

The enormous spatial, social, technical and financial project of suburbia is now a national economic liability in the USA. The Australian suburban formation differs from its US counterpart in important ways, but it would be foolhardy to assume that a cognate set of energy and credit pressures will not eventually bear upon what Gleeson (2006) has called Australia’s ‘heartlands’.

The simultaneous climate crisis is set to compel a rapid reduction in transport emissions and potentially stimulate a technological rupture in the suburban transport infrastructure. Further constraints of land and water will impose natural limits on the spatial spread of urbanisation. And, while the State has returned to the economic field with expansionary Keynesian policies, the magnitude of monetary and economic intervention could presage a new fiscal crisis (O’Connor 1973). A prolonged state fiscal crisis redux would be different in character but potentially as dramatically transformational as that which ushered in neoliberalism. Such forces are unlikely to leave the suburban matrix of labour, land, housing, debt/credit, automobile and oil unaltered.

Conclusions

The specific contours of the arrangements that will emerge from these pending transformations are as yet unknown and impossible to accurately discern. It is likely that the suburban effects on the ground will contrast sharply from either ‘business as usual’ or from the contemporary planning utopias of sustainable transit-oriented centres. Nor is the ‘panic urbanism’ (Coutard and Guy 2007) articulated by some scholars (for example Atkinson 2007a; Atkinson 2007b; Atkinson 2008) necessarily a reliable script for Australian cities.

The petroleum question will be crucial though. The urban consolidation policies of contemporary Australian plans that are making citadels of the
inner cities will confront a wider suburban spatial restructuring which they will mostly be too slow and weak to address. New vehicle or fuel technologies are unlikely to serve as a direct substitute and face years of trickling through second-hand markets. Suburbia may carve new tracks on re-constructed public transport systems, as Mees (2000) and Dodson and Sipe (2008b) have argued; but these systems, in turn, depend for their effectiveness on the organising and coordinating power of the state. Such retro-structuring could reset the city on a markedly different path to the car and freeway model, as a cursory glance at European typologies suggests. A similar shift away from dependence on private housing tenures may also be required. But any departure from recent arrangements will be subject to current historical, institutional and spatial contingencies.

The spatial and temporal relations that emerge from this particular reconstitutive context in Australia may differ from models found elsewhere, whether in North America or Europe, while those other places will themselves be transforming. Suburbia will endure but it is being driven into an era of reconstruction and reconfiguration, the political economic topography of which is only barely perceptible in the dim beams of our contemporary headlights.

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RESPONDING TO THE FINANCIAL CRISIS: FROM COMPETITIVE TO COOPERATIVE URBANISM

Kurt Iveson

You never want a serious crisis to go to waste.
(Rahm Emanuel, US White House Chief of Staff, Nov. 2008)

Across the political spectrum, the Global Financial Crisis has been mobilised as an opportunity to argue for new policy agendas. In Australia, Labor Prime Minister Kevin Rudd (2009: 25) has used the crisis to launch a critique of neoliberal capitalism, arguing that:

The time has come, off the back of the current crisis, to proclaim that the great neo-liberal experiment of the past 30 years has failed, that the emperor has no clothes. Neo-liberalism, and the free-market fundamentalism it has produced, has been revealed as little more than personal greed dressed up as an economic philosophy.

However, this is not the first time that neoliberalism has suffered a crisis of legitimacy, and previous responses to problems of neoliberal capitalism have involved the mutation and deepening of neoliberalisation (see Brenner and Theodore 2002; Peck and Tickell 2002). In response to the current crisis, we need to make every effort to ‘ward off stiff doses of capitalist medicine, which for many will be worse than the financial malady they will be designed to cure’ (Blackburn 2008: 106).

This article considers the opportunities within the present moment to wind back the influence of neoliberal ideologies and technologies of
urban governance in Australian cities. Its core claim is that we need to develop a model of what I call cooperative urbanism to undermine the dominance of inter-urban competition and urban entrepreneurialism in shaping urban policy.

**Competitive Urbanism in Action: Brand Sydney**

We need not look very hard to find examples in Australian cities of the kind of capitalist medicine to which Blackburn refers. The ‘Brand Sydney’ project is one such example.

It should have been no surprise that Sydney would be initially hit hard by the global financial crisis in 2008. Two decades of state-led efforts to position Sydney as a ‘global city’ (McGuirk 2004) had made its economy increasingly dependent on the very economic activities which are bound up with the crisis, such as financial services, housing speculation and international tourism. When the extent of Sydney’s exposure to the global financial downturn had become obvious, what was the NSW Labor Government’s response? Among other things (such as a renewed push for the privatisation of electricity infrastructure), in August 2008 Premier Morris Iemma launched Brand Sydney. The purpose of this multi-million dollar project was ‘to attract significant projects and major events, showcasing Sydney’s role as a business hub in the Asia Pacific and promoting the State as a great place to do business’. It was to do this by bringing together state and local government with the private sector to develop a more unified brand narrative to market Sydney. In a recent opinion piece on the project’s progress, Brand Sydney Chair John O’Neill (2009) described it as ‘something radical, a bit more out of left field, to bring Sydney out of its doldrums’.

*Brand Sydney* is hardly new, radical or left field. The notion that a city’s fortunes can be improved through better branding or ‘place-marketing’ is now a well-established policy orthodoxy around the world (Hall and Hubbard 1998). The underlying premise of the Brand Sydney project is all too familiar. The pathway to prosperity for Sydney is said to lie in
winning a competition with other cities for mobile investment and tourist dollars. In this competition, the image of the city counts for everything. A ‘sexy’ brand identity that marks Sydney apart from other places in Australia and the region becomes the political priority. Different proposals for urban policy are measured according to whether or not they contribute to the brand narrative. The success of this strategy is assessed with reference to measures of Sydney’s international profile. Of course, this approach has informed bids for Sydney to host major events like the Olympics and APEC, and subsidies for corporate investments like the construction of Fox Studios.

The *Brand Sydney* project is indicative of two of the most troubling aspects of neoliberal urban governance in Sydney (and elsewhere in Australia). First, the taken-for-grantedness of inter-urban competition as the ‘reality’ to which all urban policy initiatives most ultimately respond. Second, the associated alignment of the city’s collective interests with the interests of (some fractions of) capital – particularly in the areas of real estate, finance and tourism.

In his influential discussion of urban entrepreneurialism, David Harvey (1989) argued that inter-urban competition had emerged as a kind of ‘coercive law’ to which strategies for urban governance must respond. While the responses may be different (a point to which I will return), inter-urban competition has achieved the status of a ‘macro-necessity’ which conditions the ‘micro-diversity’ of governance arrangements across different cities (Jessop, Peck *et al.* 1999). The primacy of inter-urban competition has been fundamental to the global spread of neoliberal technologies of urban governance with which we are now so familiar – from privatisation and marketisation of urban infrastructure provision through to punitive law and order strategies ostensibly designed to enhance ‘quality of life’.

For Peck and Tickell (2002), the status of inter-urban competition as an ‘extralocal rule system’ has been achieved through a pernicious feedback loop, as local governance strategies which purport to *respond* to the
‘reality’ of competition in fact help to consolidate and deepen that very reality. The adoption of entrepreneurial strategies such as Brand Sydney

only serve to further accelerate the (actual and potential) mobility of capital, employment, and public investment. In selling themselves, cities are therefore actively facilitating and subsidizing the very geographic mobility that first rendered them vulnerable, while also validating and reproducing the extralocal rule systems to which they are (increasingly) subjected … The logic of interurban competition, then, turns cities into accomplices in their own subordination… (2002: 393).

This is not to say that competitive pressures only exist in the minds of local boosters. However, we need not take these competitive pressures for granted as an unalterable reality. It is precisely in establishing these pressures as inevitable, as beyond the reach of political action, that advocates of neoliberal governance strategies have been so influential in shaping policy agendas.

In particular, once inter-urban competition is established as the condition to which urban governance must inevitably respond, this ‘opens up a range of mechanisms for social control’ as advocates of entrepreneurial strategies for growth mobilise a ‘rhetoric of urban governance which concentrates on the idea of togetherness in defense against a hostile and threatening world of international trade and heightened competition’ (Harvey 1989: 14). The local boosters, in short, position themselves as acting not in their own particular interests, but in the best interests of the city as a whole, in the face of the ‘harsh realities of the global marketplace’.

The last two decades of planning ‘reform’ in NSW are illustrative of this process. There has been a slow but steady concentration of decision-making power in the body of the Planning Minister and his unelected appointees, who can increasingly clear the way for developments to take place when they are considered to be in the ‘state interest’ (Cook 2006). This is not a problem per se — but it becomes a problem when the Minister narrowly defines the ‘state interest’ as a matter of enhancing
(and latterly protecting) Sydney’s status as a ‘global city’. As such, this concentration of power is designed not to democratise planning, but rather to privilege the interests of developers, financiers, multinational capital and tourist operators whose activities are at the core of their definition of Sydney’s ‘global city’ brand.

**Challenging Neoliberal Urban Governance**

What are the alternatives to this neoliberalisation of urban governance in Sydney and other Australian cities? There are at least three kinds of political action that show some promise: (i) progressive entrepreneurialism; (ii) redefining the interests of ‘the city’; and (iii) cooperative urbanism.

**Progressive entrepreneurialism**

Even where the coercive discipline of inter-urban competition has taken precedence, there is some scope for different kinds of responses in different places (Harvey 1989; Larner 2003). Not all urban entrepreneurialisms are the same, and some may have progressive elements. The ‘Renew Newcastle’ project is one example. In 2008, with the appearance of vacant retail and office space in Newcastle city centre, a collective of artists and ‘social entrepreneurs’ initially convened by Marcus Westbury established a project to make these vacant spaces available to local artists, artisans and cooperative ventures at no or little cost until a commercial tenant can be found. So far, Renew Newcastle has licensed over 41 projects across 26 vacant properties, ranging from local arts and crafts galleries to food co-ops.¹

In one sense, the rationale for this project fits squarely within the discourse of urban entrepreneurialism – that the image of the city will suffer if vacant commercial space is left to deteriorate, and that the city will ultimately derive economic benefits from the unleashing of

¹ See http://www.renewnewcastle.org/
‘creativity’ in these once-vacant spaces. Furthermore, Renew Newcastle operates as a text-book entrepreneurial partnership involving local businesses (in real estate, law and marketing), the local Council, Newcastle University and Arts NSW.

Nonetheless, there is also a potential challenge here to the normalisation of private property rights, and a potential politicisation of questions about culture, affordability and community (Westbury 2008). It remains to be seen whether or not the project will generate a coherent critique of market failure and an alternative framework for allocating space into the long-term. However, the project does suggest that even within the rhetoric of urban entrepreneurialism lie some progressive opportunities.

**Redefining the interests of ‘the city’**

By encouraging the notion that ‘the city’ has interests of its own, inter-urban competition opens a space for progressive local coalitions to declare themselves to be the true bearers of the city’s collective interests (Harvey 1989: 16). Research by geographer Jane Wills (2008) documents some of the important achievements of the London Citizens alliance in mitigating some of the more unjust aspects of urban development in that city. In Sydney, the difficult political labour of progressive coalition building is underway through the formation of the Sydney Alliance (SA).² The SA is modelled on the partial success of citizen movements in cities in the North America and Europe, and based on the well-established organising model of the Industrial Areas Foundation in the US.³ Seed-funded by Unions NSW in 2007, the SA is designed to bring together religious and community organisations with organised labour with the primary purpose of ‘acting for the common good, achieving social change, and building peace in our communities’. It is too early to measure the impact of this initiative, which is currently in development and will not be formally launched until 2011, but a number of significant unions and community groups are already involved.

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³ See [http://www.industrialareasfoundation.org/](http://www.industrialareasfoundation.org/)
The Sydney Alliance initiative is attractive because of its potentially programmatic character. Damien Cahill (2007: 230) has observed that ‘where opposition to neoliberalism [in Australia] has emerged, from trade unions and elsewhere, it has been primarily defensive’ (see also Brenner and Theodore 2002: 359). Through the SA, there is the potential for progressive and constructive proposals for policy as new kinds of connection are forged between interests previously operating in isolation. This could work to challenge the neoliberal logic which equates the interests of capital with the interests of the city.

Cooperative urbanism

Notwithstanding these examples at the urban scale, broader action is also needed if we are to challenge inter-urban competition, which acts as one of the ‘extralocal rule systems that provide a major source of neoliberalism’s reproductive and adaptive capacity’ (Peck and Tickell 2002: 401). Principled non-participation is not an option. As Harvey writes:

> The problem is to devise a geopolitical strategy of inter-urban linkage that mitigates inter-urban competition and shifts political horizons away from the locality and into a more generalisable challenge to capitalist uneven development (Harvey 1989: 16)

Initiatives need to be premised on *mitigating* (rather than accommodating) the influence of inter-urban competition through *cooperative urbanism*. A necessary condition in the Australian case would be for the Commonwealth government to play a major role in urban policy to foster this cooperative urbanism. However, current Commonwealth initiatives in the urban policy realm do not appear to be working in this fashion.

Rudd’s (2009) essay on neoliberalism has been interpreted by the punditry as an attempt to pin the blame for the GFC on the ideology of his political opponents on the right. But Rudd also had his sights set on the political left. By narrowly defining neoliberalism as an ideology supporting unregulated markets (Cahill 2009), and by critiquing this
ideology on the grounds that it let a few greedy individuals and institutions run riot, he neatly rejects any demands for more systematic reform of free market capitalism. Markets are not to blame, he insists, because they remain the best means we have available to make collective decisions and allocate resources. His stated task is to ‘save capitalism from itself’ (Rudd 2009: 20), by ensuring that markets are not open to abuse by greedy, irresponsible capitalists. Primarily, this is a matter for government regulation, stimulation, and amelioration.

We can see this viewpoint reflected in the way the Commonwealth has organised its infrastructure spending. Certainly, following the election of the Rudd Labor government in 2007, there has been a welcome focus on addressing infrastructure needs through government action, including the establishment of Infrastructure Australia via the *Infrastructure Australia Act 2008*. But how are the most urgent needs to be identified? Infrastructure Australia conducted initial information-gathering exercises to determine a broad list of priorities (Infrastructure Australia 2008). In addressing those priorities, however, localities have been expected to organise themselves into partnerships of actors who would develop and pitch project ideas. Funding allocations appear to have been based to a large extent on the capacity of localities to form robust partnerships able to both pitch and part-fund projects, rather than on the urgency of the need (Irvine 2009; Smith 2009).

Infrastructure Australia’s *modus operandi* has reinforced the notion that cities and towns must compete with one another to survive and thrive (Infrastructure Australia 2008: 41), based on the premise that the common good is to be best secured through the actions and efforts of local entrepreneurs and officials who act responsibly in their locality’s interest. It is textbook neoliberal policy, whereby:

> government funds increasingly flow to cities on the basis of economic potential and governance capacity rather than manifest

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4 See http://www.infrastructureaustralia.gov.au/
social need, and do so through allocation regimes that are competitively constituted … (Peck and Tickell 2002: 395).

However, even within the strictly delimited domain of government action identified by Rudd, there are some interesting progressive possibilities. Perhaps the Commonwealth’s intervention in the provision of broadband infrastructure lends some credibility to Rudd’s promise that Government will step in to fund or provide public goods in certain areas. And, early on, there were at least some signs that some issues previously left to the States (such as environmental and water management for the Murray-Darling Basin) warranted Commonwealth intervention and coordination through a new ‘co-operative federalism’ (Steketee 2008).

Rudd’s analysis of the failures of neoliberalism needs to be extended to consider its influence on urban governance, and the problematic effects of competitive urbanism. Commonwealth leadership could help to forge a cooperative urbanism which identifies and addresses problems common to our major cities, based on its own assessment of the common good. Rhetorically at least, this is not necessarily anathema to Rudd, who has argued that:

Government, properly constituted and properly directed, is for the common good, embracing both individual freedom and fairness, a project designed for the many, not just the few (Rudd 2009).

One might expect the ‘proper constitution and direction’ of government to include a serious rethink of urban policy. However, his Government’s ‘Major Cities Unit’, located within Infrastructure Australia, has no capacity in this regard, with a staff of only four persons.

**Conclusion**

As Peck and Tickell (2002: 392) have observed, ‘One of neoliberalism’s real strengths has been its capacity to capitalise on [crisis] conditions’. To counter this strength, an important priority is to counter the taken-for-grantedness of inter-urban competition and its influence on urban
governance. This article has suggested some of the kinds of actions this might involve at both the urban and the national scales.

The kinds of progressive efforts highlighted here do not necessarily complement each other perfectly. What they do have in common, however, is the attempt to re-politicise urban policy around the question of how the common good is best achieved. They each contest the depoliticising notion, so characteristic of neoliberal urbanism, that inter-urban competition is simply the reality which must inevitably determine the priorities and possibilities of urban governance.

Will the possibilities to pursue different directions at the local scale be supported with action at the extralocal scale, prioritising the common good over the sectional interests of entrepreneurial partnerships? The role of the Commonwealth in forging such support through inter-urban linkages is crucial. As long as the Rudd government’s understanding of neoliberalism remains narrow, the great neoliberal experiment rolls on. Local alternatives are (always) brewing, but the prospect for them gaining genuine traction depends upon their articulation with a wider vision of “the just city” which does not pit cities in competition with one another.

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RESPONDING TO THE CRISIS:
WHY GOVERNMENTS AND BUSINESSES GAMBLE BUT THE PEOPLE DO NOT

Boris Frankel

Writing during the dark period of the Second World War, Bertolt Brecht (1967: 286) observed that:

History shows that peoples do not lightly undertake radical changes in the economic system. The people are not gamblers. They do not speculate. They hate and fear the disorder which accompanies social change. Only when the order under which they have lived turns to an indubitable and intolerable disorder do the people dare, and even then nervously, uncertainly, again and again shrinking back in turn, to change the situation.

Contrast the reluctance of people to gamble on radical social change with the high risk-taking business and government gamblers who caused the current world recession and many other socio-economic problems. Governments constantly gamble that voters will not become aware of dilapidated infrastructure or inadequate allocation of capital for essential services until after the next election. Similarly, statutory authorities – either through inadequate policing or informal collusion with the industry sectors they are supposed to police – gamble that appalling corporate ‘financial engineering’ and commercial property practices, or dangerous production of toxins and other sorts of detriments to social amenities and public health will not come to light in the near future.
Today, the biggest gamble waged by governments and large sectors of business is the gamble that the urgent calls made by environmentalists for emergency action to prevent climate chaos can be ignored, stalled, pared down or deferred to other countries. The more cautious are politicians and business leaders, the higher the future environmental stakes they are prepared to gamble.

During periods of relative political calm or ‘business as usual’ it is easy for most people to overlook the major political economic gamblers and accept the trivialising label of the electorate as ‘punters’. However, it is precisely during major crises, such as the current recession, that the public begin to question government and corporate spin. At the moment there is little evidence that a majority of the electorate in OECD countries have rejected the modified neo-liberal policies advanced by governments and business lobbies to solve the crisis.

Crucially, for the public to reject prevailing government and business solutions to the twin economic and environmental crises, something much more fundamental has to occur. First, mass movements must emerge and a majority of the electorate (not merely handfuls of academics, policy makers and political activists) must be persuaded by a comprehensive debunking of dominant ideas and practices, namely: (a) neo-liberal modes of governance; and (b) the production and consumption foundations of the old carbon economy.

Second, a plausible and feasible set of alternative policy solutions must explain – and reassure mass electorates – how the simultaneous administrative, economic and environmental crises can be overcome within a transitional time frame, while at the same time providing adequate income, jobs and the restructuring of existing urban forms into sustainable lifestyles.

Third, governments in developed OECD countries need to massively raise or harness the additional fiscal resources that are necessary for alternative solutions – despite their ballooning indebtedness. This will be difficult given a prolonged period of low growth or deflation plus the threats to democracy from authoritarian populist parties.
Fourth, while OECD countries require major structural reforms, many developing countries face grim scenarios due to their very limited capacity to deal with glaring social inequalities and the debilitating consequences of prolonged recession or stagnation. It is clear that the pre-recession 2005 Millennium Development Goals, adopted at Gleneagles and aiming to cut poverty by 2015, will be substantially under-achieved.

Also, it is sobering to compare pre-recession estimates of future energy and social problems in developing countries with post-2008 global finances following the impact of financial bail-out costs on G8 countries’ budgets. For example, the Gleneagles Communiqué estimated that $US16 trillion would be needed to transform world energy sectors to renewable sources in the next 25 years. Yet, the 2006 OECD-FAO Agricultural Outlook 2006-2015 Report also assumed that oil prices would fall to $US40 per barrel. This is wildly unrealistic, given the spike in 2007-08 oil prices and brokers currently factoring in a price of $US95 to $US100 per barrel by the end of 2010. The UN-Habitat’s State of the World’s Cities Report 2006/2007 states that, by 2030, 5 billion people will live in cities of which 4 billion will be in developing countries. Within 20 years it is projected that Africa’s urban population of 748 million (largely slum dwellers) will be greater than Europe’s total population (UN-Habitat 2006). The scale of social problems and global growth demand for energy will be phenomenal. Unfortunately, the feeble response of the G20 to the plight of developing countries guarantees continuing mass loss of life and shocking poverty for hundreds of millions of people.

Given the scale of the global crisis and the prospect of prolonged stagnation/low growth rates, it is necessary to ask: if there is no quick return to ‘business as usual’, what is the tipping point that will lead a majority of people to swap places with governments and businesses and become social change gamblers? Part of the answer is to be found in how the crisis has been explained to electorates and how a range of governments, parties, social movements and business groups have responded to the current crisis.
 Responses to the Crisis

A mountain of media, government and academic commentary has posited a false dualism between the financial crisis (‘Wall Street’) and the ‘real economy’ (‘High Street’). This dualism not only fundamentally ignores the inseparable interconnectedness of financial institutions to all other ‘real economy’ production, distribution and consumer processes, but ignores the very size of financial sectors in terms of ‘real economy’ employment, presence on equity markets and their roles as driving forces of capitalist economies (Frankel 2001).

Despite the revelations of the past two years, the larger international publics are still unaware of how dramatically close the US economy – and possibly the world economy – was to profound chaos, or total collapse. We now know from recent US Congressional testimony that a collapse of the US economy was only miraculously averted – precisely between 11a.m. and 2.p.m. on September 18th 2008 – when Treasury and Federal Reserve officials suspended financial transactions, thus preventing the liquidation of $US5.5 trillion from the banking system.

Similarly, the public is aware of the gambling financial engineers who cost investors trillions of dollars and rendered millions of mortgagees homeless, but they are less aware of the actual size of these losses and their impact on future budget expenditure and taxes. For example, the IMF’s April 2009 global financial stability report estimates the financial sector write downs were at least $US4,400 billion, or 37 years of IMF official development assistance at 2008 levels. It also estimates that governments have already provided $US8,900 billion of financing for banks, but that the refinancing gap (rollovers of short term debt and maturing long-term debt) will rise from $US20,700 billion in 2008 to $US25,600 billion in 2011 (over 60% of banks’ assets).

By comparison, the impact of the recession on public debt and budgets (so far) remains manageable in most countries. Nevertheless, Gordon Brown’s UK government has designated $120 billion worth of public expenditure cuts – a severe constraint on any alternative plan to create
new sustainable cities and jobs for the future. The UK’s budgetary position may even be better than the public finances in Germany, Italy, Spain and other EU countries. Australia’s indebtedness and budgetary deficits are very mild compared with most other OECD countries, even though the political Right is seeking to create fear of unsustainable debt.

The ability of international banks to finance pre-2007 levels of private investment and growth remains questionable. As large net borrowers of foreign capital, Australian businesses may find it difficult to fund high levels of investment ventures with risk assessments of BBB and sub-BBB in constrained global investment markets (given the failure of various international A to AAA-rated ventures to raise sufficient competitively priced funding). This may be a blessing if it slows or prevents ugly and inappropriate urban commercial property development. On the positive side, the tightening of private capital liquidity also constitutes a domestic opportunity to rethink existing neo-liberal public and private sector capital raising and expenditure priorities.

Sadly, there is very little interest from Australian Federal and State Labor governments to explore post-neo-liberal public policies and fiscal strategies. On the contrary, with a few minor exceptions, neo-liberalism thrives – from Premier Bligh’s privatisation agenda in Queensland and Brumby’s green light to developers in Victoria, to Gillard’s national education and industrial relations policies. At the helm, Kevin Rudd (2009) prematurely believes we are witnessing the end of neo-liberalism: he conveniently ignores the deep-seated commitment to neo-liberal fiscal and monetary strategies that are daily revealed by his own Federal Ministers.

Like State Labor governments, the Rudd government is poll-driven and heavily geared to an obsolete carbon economic model. Crucially, the social amelioration policies in areas such as housing and social inclusion are largely excluded from prominence in cabinet. The latter are overshadowed by a ministerial governance structure that reflects traditional rightwing Labor foreign and military emphasis on the US alliance (see the 2009 Defence White Paper) and an eagerness to please
corporate interests. Zealously defending the mining and agribusiness sectors, Rudd’s policies are little different to Howard’s anti-green agenda (leaving aside the token signing of the Kyoto treaty). As a government conducting war (with two ministers and a parliamentary secretary in Defence), no separate minister for education, little emphasis on urban renewal, poorly targeted stimulus packages largely geared to conventional consumption spending, and an infrastructure budget heavily favouring road transport, this is a government that is not only conservative but, like the State governments, very neglectful of the massive environmental and economic problems confronting the majority of people living in urban Australia.

Non-government Responses

The trade union movement – the largest social movement in Australia - has largely confined itself to jobs and working conditions, thus rendering itself almost irrelevant to the broader political struggle over public finances and the future structure of Australia’s political economy.

Lacking sufficient analysts capable of formulating macro-economic alternatives that will challenge Rudd’s neo-liberalism, the ACTU is now supine and dependent on Labor governments. Accordingly, despite the rhetoric of co-operation, Rudd and his senior Ministers – especially ex-ACTU leaders - treat it with contempt. The recent 2009 ACTU Congress was silent on crucial issues, such a new public financial architecture, new manufacturing industries, and the urban services and governance structures needed in the coming decade. It is true that the ACTU and Australian Conservation Foundation (ACF/ACTU 2008) promote their Green Gold Rush objective of achieving 847,000 green jobs by 2030. Welcome though this may be, a maximum of about 40,000 new jobs per year is pitifully inadequate in an economic context where there may be approximately 1.8 to 2 million people unemployed and underemployed in 2010.
There has been no published Australian study to this date which documents in detail what is the scale of urban restructuring necessary in the next two decades to create the basis for sustainable employment in the transition to a low or net zero carbon emissions economy. Unfortunately, some of the main opponents of a new low-carbon economy are conservative industry unions bolstering the Federal and State Labor governments.

As for green movements, despite the massive global economic crisis they remain largely bereft of comprehensive anti-hegemonic fiscal and economic proposals — policies that are necessary to explain to the electorate how a transition to a low and post-carbon economy can be funded and constructed. Certainly, they have made substantial calls for all kinds of sustainable transport, energy and infrastructure polices, but these positive ideas are poorly linked to tax, social security, trade and other regulatory, investment and alternative industry practices.

It is not just labour and green social movements that are relatively silent on how to formulate and construct an alternative sustainable economy in the coming decades. Since the onset of the crisis it is difficult to detect any major reappraisal of neo-liberal macro-economic and social policies advocated by Australia’s leading business peak bodies. On the contrary, they continue to push for cuts to business taxes, increases in regressive GST and variations of WorkChoices. The Liberal Party has learnt nothing from the global debacle.

There is also little or no public debate in Australia of the 2020 scenarios that leading defenders of capitalism such as the World Economic Forum (WEF) produce. For example, the WEF 2009 report on the future of the global financial system floated four possible scenarios for the next 11 years: (a) re-engineered Western centrism; (b) fragmented protectionism; (c) financial regionalism; and (d) rebalanced multilateralism (WEF 2009). The least preferred scenario is a fragmentation of financial sectors and economies behind protectionist lines. The Report also worries about a resurgent Atlanticism of the US and EU, as well as the deepening of regional financial and economic divisions between the US, Europe, Asia...
and the BRIC countries. Clearly, its preferred model is a Bretton Woods Mark 3 that fuels global growth in a rebalanced multilateral new world financial system. Kevin Rudd and Paul Keating favour a Bretton Woods Mark 2 model that incorporates China and India into leadership roles in the IMF and other world bodies. However, the inclusion of newly emerging powers does not in itself insure against continued economic regionalism or prevent another, and possibly far worse, global crisis. Hence, the WEF hopes for a more genuinely multilateral Mark 3 global financial architecture which would include new crisis-preventing stabilising mechanisms, greater regulation, and the upgrade of the International Bank for Settlements as the global banker of last resort.

Like many other pro-market policy makers and economists dreaming of a state of equilibrium and foolproof crisis-management, the WEF’s goals for 2020 look almost certain to be undermined by deep-seated national interests, industry lobbies and a range of political conflicts. Significantly, the WEF scenarios inadvertently highlight how the majority of political and business leaders across the world still pursue short-sighted goals within narrow national or regional frameworks.

Australia lacks regional protection such as that afforded by membership of the EU and other blocs. Bi-lateral trade pacts are not an adequate substitute. For example, the Howard government committed to the Australia-US Free Trade pact because it claimed the US was Australia’s largest economic partner, but this was only true if one included financial transactions rather than just merchandise trade. Given the impact of the current crisis on US financial institutions, Australian business will be forced to seek other sources of capital inflow and strategic alliances. As a heavily traded currency, there is great risk that the Australian dollar could face very high volatility in the next decade, especially if its alignment to the US dollar proves untenable and/or new global carbon emissions pacts seriously affect commodity exports. In the WEF scenarios, with which regional bloc would Australia be forced to align itself in the absence of a new Bretton Woods Mark 3?
Given the lack of consensus within the G20, it is likely that fundamental reform of global financial institutions will be postponed. Domestically, there is very little prospect that neo-liberal social and economic policies will be abandoned within the next Australian electoral cycle unless there is a sudden and dramatic increase in political mobilisation from a Left and eco-social perspective.

As for climate change, even strong opponents of neo-liberal policies, such as the Australian Climate Emergency Coalition, are divided. Many believe that zero carbon emissions by 2020 can be achieved with little change to everyday life and the economic system (e.g. by following Al Gore’s ten-year renewable energy targets, implementing biochar sequestration and so forth). Others consider it is an illusion to believe that urban life and food production can continue former growth rates with just minimal ecological modernisation techniques.

Prospects

The present crisis has thrown up a whole range of concerns about macro-economic and environmental policy direction among anti-neo-liberals. Take the observation made by oft-cited urban political economist David Harvey:

…in the last 30 years an immense amount of the capital surplus has been absorbed into urbanization: urban restructuring, expansion and speculation. Every city I go to is a huge building site for capitalist surplus absorption. This way of absorbing capital surpluses has got more and more problematic over time. …Throughout the history of capitalism, the general rate of growth has been close to 2.5 per cent per annum, compound basis. That would mean that in 2030 you’d need to find profitable outlets for $3 trillion dollars. That’s a very tall order…Capitalism is running into serious environmental constraints, as well as market constraints, profitability constraints (Harvey 2009).
While I think that Harvey presents a powerful case, it could also be argued that capitalist businesses may overcome (for at least 15 to 20 years) significant surplus absorption problems by heavily investing in ecological modernisation. In Australia alone, the transformation of cities – renewable energy, retro-fitting and constructing new sustainable buildings, public transport, decentralised water facilities and many other proposals - would conservatively cost more than $600 billion over a ten year period. Whether governments provide the carrots and sticks to facilitate this redirection of capital is a political question rather than an economic one. Whether capital surpluses could be profitably absorbed after the initial 20-year greening of cities is a separate question.

Having read and heard many radical prognoses over past decades about unsustainable debt levels, the impending crisis-collapse of capitalism or, conversely, Panglossian pro-market predictions of endless growth, one is reluctant to assert with any confidence the likely character and outcomes of the present crisis. Will we remain with Brecht in dark years like those of the Second World War when he believed the people were reluctant to gamble? Or will the current generation embrace the need for a massive reconstruction of obsolete urban social and political structures in a similar spirit to an earlier generation that embraced the urgent necessity of post-war reconstruction?

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THE GFC AND UNIVERSITY ECONOMICS EDUCATION:

AN OPEN LETTER TO THE QUEEN

When the British Queen visited the London School of Economics she asked a question that any ordinary citizen might ask of our leading economists: why was it that so few economists had foreseen the recession? Two professors replied and this was widely reported in the British press. However, that reply did not satisfy some other economists, ten of whom wrote a different reply, as follows:

We are writing both in response to the question you posed at the London School of Economics last November – concerning why few economists had foreseen the credit crunch – and the answer to you from Professors Tim Besley and Peter Hennessy dated 22 July.

We agree with many of the points made by Professors Besley and Hennessy, principally those summarized in the next paragraph, but we regard their overall analysis as inadequate because it fails to acknowledge any deficiency in the training or culture of economists themselves.

Their letter rightly mentions that ‘some of the best mathematical minds’ were involved in risk management but ‘they frequently lost sight of the bigger picture’. Many believed that risks had been safely dispersed and ‘virtually removed’ through ‘an array of novel financial instruments … And politicians of all types were charmed by the market’. In summary, they conclude, ‘the failure to foresee the timing, extent and severity of the crisis and to head it off, while it had many causes, was principally a failure of the collective imagination of many bright people, both in this country and internationally, to understand the risks to the system as a whole.’

In addition to the factors mentioned in their letter, we suggest that part of this responsibility lies at the door of leading and influential economists in the United Kingdom and elsewhere. Some leading economists –
including Nobel Laureates Ronald Coase, Milton Freidman and Wassily Leontief – have complained that in recent years economics has turned virtually into a branch of applied mathematics, and has become detached from real-world institutions and events. (We can document these and other complaints fully on request.)

In 1988 the American Economic Association set up a commission on the state of graduate education in economics in the US. In a crushing indictment published in the *Journal of Economic Literature* in 1991, the Commission expressed its fear that ‘graduate programs may be turning out a generation with too many idiot savants skilled in technique but innocent of real economic issues.’

Far too little has since been done to rectify this problem. Consequently a preoccupation with a narrow range of formal techniques is now prevalent in most leading departments of economics throughout the world, and notably in the United Kingdom.

The letter by Professors Besley and Hennessy does not consider how the preference for mathematical technique over real-world substance diverted many economists from looking at the vital whole. It fails to reflect upon the drive to specialize in narrow areas of enquiry, to the detriment of any synthetic vision. For example, it does not consider the typical omission of psychology, philosophy or economic history from the current education of economists in prestigious institutions. It mentions neither the highly questionable belief in universal ‘rationality’ nor the ‘efficient markets hypothesis’ – both widely promoted by mainstream economists. It also fails to consider how economists have also been ‘charmed by the market’ and how simplistic and reckless market solutions have been widely and vigorously promoted by many economists.

What has been scarce is a professional wisdom informed by a rich knowledge of psychology, institutional structures and historical precedents. This insufficiency has been apparent among those economists giving advice to governments, banks, businesses and policy institutes. Non-quantified warnings about the potential instability of the global financial system should have been given much more attention.
We believe that the narrow training of economists – which concentrates on mathematical techniques and the building of empirically uncontrolled formal models – has been a major reason for this failure in our profession. This defect is enhanced by the pursuit of mathematical technique for its own sake in many leading academic journals and departments of economics.

There is a species of judgment, attainable through immersion in a literature or a history, that cannot be adequately expressed in formal mathematical models. It’s an essential part of a serious education in economics, but has been stripped out of most leading graduate programmes in economics in the world, including in the leading economics departments in the United Kingdom.

Models and techniques are important. But, given the complexity of the global economy, what is needed is a broader range of models and techniques governed by a far greater respect for substance, and much more attention to historical, institutional, psychological and other highly relevant factors.

In summary, the letter by Professors Tim Besley and Peter Hennessy overlooks the part that many leading economists have had in turning economics into a discipline that is detached from the real world, and in promoting unrealistic assumptions that have helped to sustain an uncritical view of how markets operate.

We respectfully submit that part of the problem lies in the additional factors that we have outlined above. As trained economists and United Kingdom citizens we have warned of these problems that beset our profession. Unfortunately, at present, we find ourselves in a minority. We would welcome any further observations that Your Majesty may have on these problems and their causes.

We remain your most humble and obedient servants,

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