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TITLE: Was the mining boom good for you?

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Recently, there have been warnings that Australians will have to be prepared for the end of the mining boom and the lower living standards that will impose. The assumption is that the mining boom delivered higher incomes to Australian workers but its demise signals an end to this bonanza and a belt-tightening adjustment on the part of the bulk of Australians. Those with long memories will recall that in the mid-1980s, the Hawke Government similarly used the fall in the terms-of-trade to justify a reduction in real wages.

The above assumption is rarely examined rigorously but The Australia Institute has recently done just that and the results are arresting.

The main benefits of the boom were considered to be transmitted through the terms-of-trade, which essentially measure the purchasing power of exports by dividing an index of export prices with an index of import prices. Commodity prices began to increase towards the end of 2004 and then exploded over the next few years. The commodity price index kept by the Reserve Bank of Australia went from around 100 in 2004 to peak at around 280 in September 2008. It was these increases in commodity prices that chiefly drove Australia's terms of trade although there would have been some boost from cheap imported goods from China.

According to the Australian Bureau of Statistics (ABS), the terms-of-trade effect produced a nine per cent real increase in national income between the December quarter 2004 and the December quarter 2008. That was over and above the impacts occurring at the same time on some of the main factors also affecting national income, which included higher employment, higher wages and other incomes and increases in productivity.

Nine per cent is roughly the result when the terms-of-trade increase over the same period (44 per cent) is multiplied by the share of exports in GDP, which averaged 21 per cent. The ABS uses more sophisticated measures but they arrive at approximately the same figure.

If the nine per cent had been shared equally, it would have represented additional annual income per person of almost \$4000 per annum. If it had been distributed pro

rata, everyone would have received a nine per cent increase to their incomes. However, the mining boom didn't work like that.

The initial impact of the mining boom devolved on to the profits of the various mining companies and their shareholders would conceivably have received substantial gains. However, many of these beneficiaries were foreign shareholders and much of the paper profits would have been lost in the period since December 2008. After these initial effects, the ripples then spread to the mining company suppliers, contractors and workforce, translating into more work and higher incomes. From there the ripples continued with strong local and regional effects, particularly in WA and Queensland. However, by the time the ripples reached the rest of the economy they were so weak as to be imperceptible.

The Secretary of the Treasury, Ken Henry, suggested that Australians would enjoy the benefits of the boom by way of cheaper import prices. However, people whose incomes are indexed to inflation, including those relying on government benefits such as the unemployed, would have been able to purchase only the same bundle of goods and services during the boom as before it. Flat panel TVs may have become relatively cheaper, but if people could not afford one before the boom they could not afford one afterwards either, unless they gave up something else. For the cheaper import prices to have improved anyone's living standards, there would have to have been a commensurate real increase in their incomes.

The two main sources of household income are wages and government income support payments. A jump in real wages, compared with what might have occurred in the absence of the boom, would have been necessary for wage earners to have benefited from the mining boom. This can be tested.

The preferred measure of wages is the wage price index because it tracks what is happening to a fixed composition of jobs. Dividing that index by the consumer price index derives a measure of real wages, allowing a comparison of real wages both before and after the mining boom.

Real wages increased only slightly more in the four years after the boom than they did before it. The difference was 0.2 per cent per annum, which is only a smidgin above zero. Indeed, the Reserve Bank's alternative measure of prices, which eliminates the volatile components, eradicates even that 0.2 per cent. Nevertheless, that 0.2 per cent for four years is well short of the nine per cent increase in real incomes implied as a result of the mining boom.

While it is hard to identify any improvement in wages using the Australia-wide figures, there is no doubt that wages in some regions and some occupations did increase. For example, average weekly earnings in mining increased by 33 per cent over the four years ending in 2008. On the other hand workers in 'accommodation, cafes and restaurants' received a mere 12.3 per cent increase, which amounted to an actual real-wage cut of one per cent. State-by-state figures are less dramatic but WA wages displayed the greatest growth at 22 per cent compared with the national average of 17.6 per cent.

Most pensions are now indexed to wages or the consumer price index, whichever is larger. The largest of these pensions, in terms of the numbers of recipients, is the age pension and the indexation arrangements allow the pension to increase gradually over time in line with community standards. This group did not receive any benefit from the mining boom because wages themselves did not benefit. As

discussed above, wages increased by only 0.2 per cent, nowhere near the nine per cent the mining boom might have been expected to deliver.

The remaining government income support payments, the allowances, are indexed and, as already pointed out, there has been no benefit passed on through that mechanism.

Some households would have benefited through their direct and indirect holdings of shares in mining companies such as BHP Billiton and Rio Tinto because of the large paper gains, up to 170 per cent in the S&P/ASX Resources index. Even at the end of December 2008, mining shares were still 57 per cent above their 2004 levels. However, share ownership is largely confined to higher-income households with the top 20 per cent owning 86 per cent of shares.

Share ownership is skewed even among those that do own mining shares. For example, Rio Tinto and BHP Billiton account for 51 per cent of the resources index; 67 shareholders, 0.13 of one per cent of shareholders, own 68 per cent of Rio Tinto while 78 shareholders, 0.01 of one per cent of shareholders, own 59 per cent of BHP Billiton. Both companies show a large number of small shareholders. Around 130,453 people, or 87 per cent of Rio Tinto shareholders, own just eight per cent of Rio Tinto while 308,000 people, or 59 per cent of BHP Billiton shareholders, own just four per cent of BHP Billiton.

This proves that any gains accruing through share ownership would be strongly concentrated among a small number of wealthy shareowners.

While it is hard to identify any gains flowing to the majority of Australians as a result of the mining boom, it is possible to identify some negative impacts. The Australian dollar is often cited as a commodity currency, which means that its value tends to move with commodity-price movements. As a result of the strong increase in commodity prices, Australia certainly did experience an appreciation in the Australian dollar, by 31 per cent against the US dollar. The effect was to reduce Australia's competitiveness in other trade-exposed areas, with manufacturing being particularly hard hit.

In addition to the exchange rate impacts, monetary policy was tightened significantly over this period. Most increases in the interest rate were explained, at least in part, by the increase in commodity prices. The new Governor of the Reserve Bank, Glenn Stevens, seemed especially keen to ensure that the mining boom did not spill over into the rest of the economy.

The result was higher interest rates that spread throughout the Australian economy far more widely than any benefits of the mining boom.

At their peak, higher mortgage-interest rates were transferring an additional \$24 billion per annum, when compared with 2004, from the household sector, the equivalent of a three per cent reduction in living standards for households as a whole. New home buyers were the worst affected. For a new home mortgage of \$300,000 taken out by someone on average weekly earnings, the increase in mortgage interest rates would have taken away 12.9 per cent of their post-tax earnings by mid-2008.

Some of the additional costs would have been returned in the higher deposit interest rates available on a limited number of deposit types. However, for most of the deposits that households are likely to use, interest is not paid or paid at trivial rates.

in fact, the mining boom bonanza barely spread beyond the mining industry itself but the negative implications of the mining boom were felt very widely. This is important in view of the current suggestions that the end of the mining boom implies that Australians will have to tighten their belts.

Symmetry should apply in the event of a slump in commodity prices. Just as the benefits of the boom were largely confined to the mining industry, the adverse effects of any slump in commodity prices should likewise be confined to the mining industry.