

FINANCIAL REVIEW

SE Perspective
HD **The 'rock star' economy over the ditch**
BY Brian Toohey
WC 1,039 words
PD 15 February 2014
SN The Australian Financial Review
SC AFNR
ED First
PG 22
LA English
CY Copyright 2014. Fairfax Media Management Pty Limited.
LP

Capital idea

Australia seems determined to keep making policy mistakes that New Zealand avoided in achieving widespread applause for its economic performance. Paul Bloxham, HSBC Bank's chief economist in Australia, even describes it as "the rock star economy of 2014". Further accolades are expected when New Zealand's Bill English appears at the G20 finance ministers meeting in Sydney.

TD

Now that handouts to local car makers are finally ending, Tony Abbott's Coalition government is considering a \$10 **billion** to \$15 **billion**-program to help the inefficient local defence industry make 1000 armoured vehicles and at least \$50 **billion** for naval shipbuilders.

Partly due to good luck, partly to good policy, New Zealand is doing well on some economic indicators, discussed below. When it stopped assembling cars it did not switch to subsidising arms production. Its lack of a tax-free threshold helps fund low marginal tax rates, while Australia has gone in the opposite direction. Unlike Australia, it refused to introduce a compulsorily superannuation system that severely damages the budget and diverts resources into an artificially bloated funds management industry.

Rather than expand secrecy as the Abbott government is doing, New Zealand Prime Minister John Key's National Party government has been unusually open since elected in 2008. English has told this columnist that his decision to release most Treasury documents a few weeks after being written has improved policy and public acceptance of change.

Unfortunately, little attention is paid in Australia to the new tax scale that Key and English introduced. It has a marginal rate of 10.5 per cent from the first dollar, rising to 17.5 per cent between \$NZ14,000 and \$48,000, then 30 per cent until the top rate of 33 per cent applies from \$70,000 – instead of Australia's 45 per cent at \$180,000. They also cut the corporate rate to 28 per cent and increased the GST to 15 per cent. Tax credits help low and middle-income earners. Tax-free threshold

The Labor government's carbon tax package increased the tax-free threshold in Australia from \$6000 to \$18,200. It tried to cover part of the cost by lifting the 15 per cent marginal rate to 19 per cent and the 30 per cent rate to 32.5 per cent between \$37,000 and \$80,000 when it becomes 37 per cent. Oddly, the Henry tax review won plaudits for wanting to lift the tax-free threshold to \$25,000. It then tried to claw back part of the \$34 **billion** in lost revenue by more than doubling the marginal rate for more than 2 **million** low-income earners to 35 per cent, thus sharply increasing work disincentives.

New Zealand's benign strategic outlook lets it spend about 1 per cent of GDP on defence; Australia spends more than 1.6 per cent. According to the military publisher IHS Janes, **China** spends less than 1.5 per cent of GDP and the US more than 4 per cent. Andrew Davies, a senior analyst at the Australian Strategic Policy Institute, says: "Power projection across oceans remains a formidably difficult task, and the list of countries that could bring much combat power to bear against Australia's territories is (excluding the US) vanishingly small." Others argue that **China** won't have the necessary capability for decades. Moreover, an official review by two former defence department heads in 2011 said no country

would have a motive to seize and hold Australian territory, when it is much cheaper to **buy** the desired resources.

However, if Australia wants to improve its defence capability, it should import high-quality weapons, rather than spending **billions** extra on trouble-plagued local production. Backed by the Victorian and South Australian governments, the local industry is pressuring Abbott to "create jobs" by building a long list of weapons. Topping the list are uniquely designed submarines for about \$40 **billion**, although proven high-performance subs can be imported for \$5 **billion** to \$6 **billion**. Land combat vehicles

Having failed at car making, these states want to build "land combat vehicles" not yet chosen by Defence. Apparently, Defence wants a new US vehicle that is not ready to go into production as it is still being developed. New Zealand avoids wasteful procurement spending by a clear focus on what equipment is really justified, then relies on imports.

Its foreign policy priorities helped cement free-trade agreements with **China** and Taiwan that Australia is yet to achieve. After meeting Abbott in January, Key told journalists that, unlike Abbott, he would not back Japan in its dispute with **China** over a **group** of barren rocks near Taiwan. A prudent answer, given the difficulties in discerning whether Japan, **China** or Taiwan has the better claim.

Although Key and English have an extensive reform agenda, they take a measured approach that doesn't frighten the electorate. English was quoted in this newspaper on Wednesday as rejecting the notion that "the key to smaller government is just slicing bits off. The community expects governments to actually solve a few problems".

Key points to productivity improvements and strong export growth in areas such as **dairy** where Australia has lagged. Releasing the official New Zealand outlook for 2014 in December, English said the budget remains on track for a surplus in 2015-16. He expects economic growth to rise to 3.6 per cent over the year to March 2015 from 2.4 per cent to March 2014, before easing back. Many in the private sector expect Australia's current growth rate of around 2.3 per cent will be slow to return to the trend level of 3 per cent.

Unemployment is 6 per cent in both countries, but the trend is down in New Zealand and up in Australia. New Zealand's annual headline inflation rate is 1.6 per cent, but is expected to rise much closer to Australia's target rate of around 2.5 per cent. These outcomes have been achieved despite official estimates of government spending in New Zealand as a share of GDP being higher than in Australia and expected to remain so for many years.

NS e211 : Government Taxation/Revenue | nedc : Commentaries/Opinions | e21 : Government Finance | ecat : Economic News | ncat : Content Types | nfact : Factiva Filters | nfcpx : FC&E Executive News Filter

RE austr : Australia | nz : New Zealand | sydney : Sydney | apacz : Asia Pacific | ausnz : Australia/Oceania | nswals : New South Wales

PUB Fairfax Media Management Pty Limited

AN Document AFNR000020140214ea2f00023