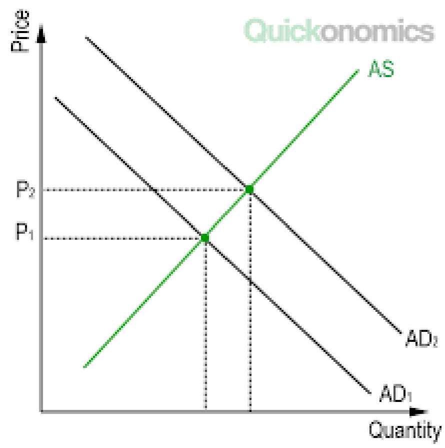
Discuss how the government's goal of sustainable economic growth may conflict with their key economic objectives

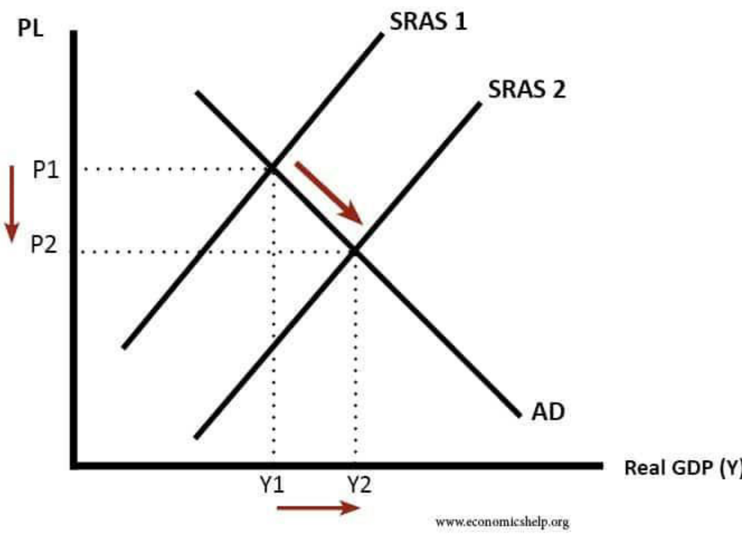
The government's goal of sustainable economic growth aims to improve quality of life and boost HDI in order to improve standards of living in the economy. Economic growth is needed to better solve the economic problem, the scarcity of resources being unable to fulfill all individual wants and needs. This can be achieved through the two macroeconomic policies of monetary and fiscal policy which targets aggregate demand which manages short term economic growth, a Keynesian approach, or through microeconomic policies such as labour market reforms, education and training which targets aggregate supply, long term economic growth and is a classical approach. However these policies may conflict with other economic objectives such as full employment, price stability, external stability, distribution of income and wealth and environmental sustainability thus the target for economic growth is 3-4%, minimising its trade-offs.

Aggregate demand driven economic growth will not conflict with the objective of full employment. With short term growth, there will be higher national incomes which leads to increased consumption and investment and as labour is a derived demand, there will be an increase in demand for labour, leading to a decrease in cyclical unemployment. This can be seen during MB2 when economic growth reached a peak of 3.4% in 2011 which caused unemployment to decrease to 5.2% in 2011, down from 5.75% the previous year. If cyclical unemployment reaches zero, then the economy is at the state of non-accelerating inflation rate of unemployment (NAIRU) which means there will be no trade-off with inflation, any lower unemployment then inflation will begin to increase rapidly. This means that government policy will aim for 4.5% unemployment (rate of NAIRU) so economic growth cannot be increased higher, without negative consequences. Conversely, if the government were to target aggregate supply led economic growth, then there would be structural change, possibly causing structural unemployment in the short term. This was seen when protection for the PMV industry in Australia was removed in order to increase allocative efficiency, causing the loss of 50,000 jobs. However increase in allocative efficiency will lead to higher aggregate supply and thus long term economic growth.

Furthermore, with aggregate demand driven economic growth, there will be increased inflation which will have negative consequences on the economy such as decreased purchasing power and



worsening standards of living as well as the distribution of income and wealth. This occurs as with an increase in AD as seen in diagram 1, without a change in AS so AD_1 curve moves to AD_2 curve causing the price level, P_1 to increase to P_2, leading to demand-pull inflation. Again, during MB2 with short term driven economic growth of 3.4% in 2011, headline inflation rose to 3.33%. This was due to increased export revenue from China as well as an increase in consumption and investment due to increased national incomes. Inflation rose above its RBA target range of 2-3% leading the RBA to conduct contractionary monetary policy, increasing the cash rate from 4.25 to 4.75 within the span of 2011, conflicting with the fiscal policy's expansionary stance to increase economic growth. Conversely, if the government targets aggregate supply led growth, there would be no conflict with inflation. Shown on diagram 2,



increases in aggregate supply such as through increased productivity or efficiencies will lead to increased output from Y1 to Y2 and thus decreasing the price level from P1 to P2, averting any potential conflict between economic growth and inflation.

Moreover, sustained economic growth can conflict with the objectives of external stability. Increased economic growth will lead to an increase in national incomes, possibly resulting in increased import expenditure which will worsen BOGS and the current account deficit. From 2001 to 2004, economic growth increased from 1.9% to 4%, resulting in the CAD as a percentage of GDP to significantly increase from 2% to 6.3% in the same time period, worsening external stability. Further, increased economic growth can also lead to increased foreign direct investment as foreign investors seek a higher return on investment as economies with high growth rates tend to have higher profit generating businesses, guaranteeing higher dividend and profits payments. These returns on investment will be a debit on the NPY account, worsening CAD and will increase the level of NFD as seen between 2001 and 2004 when NFD increased from 50% to 55% as a percentage of GDP, worsening external stability. However, economic growth will have a mixed effect on the exchange rate as increased import spending will increase the supply of the dollar, causing a depreciation while increased FDIs will increase the demand for the AUD, causing an appreciation. This means that it will not conflict with the international competitiveness of the economy but will affect the size of CAD and NFD in regards to external stability.

Policies to improve short term economic growth can cause the distribution of income to worsen. This is because as there is increased aggregate demand led growth, high income earners will benefit more than low income earners. High income earners tend to be also wealthy which means they benefit off asset price inflation, as a result of demand-pull inflation as well as they tend to have their wages indexed, possibly having their wage growth increase at a higher rate than inflation. However, in times of high economic growth, there may be lower unemployment, leading to increased national incomes and thus improved distribution of income as seen from 2008 to 2015 when economic growth increased from 2.1% to 2.9%, leading the gini coefficient to decrease from 0.34 to 0.32. Piketty's theory states that the return on capital is greater than the level of economic growth, inequality will increase. This is because high income earners tend to hold a greater amount of capital and assets so if the rate of capital gains is higher than the rate of national incomes such as economic growth, the higher income earners will increase their wealth at a faster rate, thus worsening the distribution of income and wealth. Hence presenting the conflict between economic growth and the distribution of income and wealth.

Finally, policies to increase short term economic growth foregoes ecologically sustainable development. This is because increased economic growth requires an increase in output which leads to increased pollution and greater resource depletion, thus worsening environmental sustainability. Australia’s economic growth is heavily reliant on its exporting industries as the last two major increases in economic growth was during the second mining boom and the increased demand for iron ore from China during the recovery period from COVID-19. To increase economic growth, the government could allocate more resources in this industry however the exporting industries such as mining are harmful to the environment, with Australian export industries representing 3.6% of global CO_2 emissions. Australia is the largest coal and LNG exporter however coal is expected to last another 125 years so the government looks for alternatives which will lower the ability of macroeconomic policies to increase short-term economic growth as resources are spent into research and development to increase aggregate supply. In the long term, these policies will have a positive impact on the environment as well as increasing the level of aggregate supply, removing the trade-off from the short term relationship.

Thus, a more classical approach to increasing economic growth will have limited trade-offs with the government's other economic objectives however, short-term growth is needed to incentivise economic activity despite its negative effects on inflation, distribution of income and environmental sustainability.