



Implications for the Queensland Economy from Current World Economic Conditions

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1. Executive Summary

The Queensland economy is currently experiencing economic slowdown as a result of the world recession and is not expected to begin recovery until late 2009. This slowdown is expected to produce significant labour market problems in terms of the extent of unemployment and underemployment, but more so because of its expected speed, which will place significantly more pressure on the resources of the Commonwealth and State than has been experienced since the early 1990s. A less obvious, but just as serious problem will be the impact of the recession on those marginalised parts of the population that are collectively described as the socially excluded.

This report, examines current economic data to make plausible assumptions about the extent and duration of the recession. Specifically it suggests that;

- By June 2010 approx. 27,800 young people seeking full time work
- This exceeded by people aged 45-54 years seeking work.
- Long term unemployed increases from 17,500 in 2008-09 to anything between 42,500 and 44,500 in 2010.
- Mature age workers will be hardest hit but also new entrants into the labour market (school and university leavers).
- Total unemployment expected to rise to 170,000 by June 2010.
- Youth unemployment to reach 25,000 by the same date
- An increase of 100,000 persons who could be classified as socially excluded
- An even greater number of persons (150,000, including dependents) who will become economically vulnerable to economic shock.

The tendency in times of economic recession is for Governments to become fiscally conservative in an effort to contain the impact of lost revenue and to concentrate on providing policy assistance to the "easiest" cases; those in the labour market that are short-term employed. This report argues that there are significant costs in failing to quickly respond to the more ingrained labour market problems of long-term unemployment and marginalisation. Building on work from Mangan and Stephen (2007) the report shows quick response remedial policies, though initially costly, will produce major net long-term financial benefits to the economy resulting from increased productivity, lower health costs and lower social security costs and reduce law enforcement costs. The study quantifies some of these benefits and argues that the projected savings will greatly outweigh the initial costs of targeted Government programs, particularly where these programs go beyond traditional labour market programs and encapsulate whole of Government responses across health, housing and financial counselling.

2. Introduction

The Latest IMF and World Bank forecasts for the World Economy 2009/2010 suggest a period of negative growth across virtually all economies¹. In their latest edition of *Global Economic Prospects*, the World Bank notes that global growth is expected to contract by 1.7 percent this year. This would be the first decline in world output since World War II. GDP is projected to decline by 3 percent in OECD countries and by 2 percent in other high-income economies.

The World Bank's baseline forecast predicts growth momentum to turn weakly positive in 2010 as financial-sector consolidation, lost wealth and knock-on effects from the financial crisis, continue to dampen economic activity. However, the pace and timing of the recovery is still highly uncertain.

"Across the developing world, we see that conditions of recession are affecting the poorest people, making them even more vulnerable than before to sudden shocks—but also reducing opportunities available to them, and frustrating their hopes".

The IMF has issued similar predictions and these are reinforced by the forecasts of most major Treasuries. Australia, after clinging stubbornly to a belief that they were less exposed than others, has now forecast negative growth in 2009, and after a period of relative calm, the Australian labour market has now started to experience rapid increases in the rate of unemployment², indicating a lagged effect from the economic shocks that have impacted on our major trading partners.

Unemployment is often the most visible form of economic hardship resulting from recession. However, behind these official rates are other labour market impacts that often escape attention, including under-employment and hidden unemployment. On top of this is a marked increase in what is called, social exclusion.

Even in the early stages of the labour market adjustment, the current recession seems to be different from earlier recessions in several significant ways:

- First, the participation rate is remaining high, indicating that hidden unemployment will be less than normally occurs in a downturn, with persons choosing to stay visible in the labour market, by joining the ranks of the unemployed rather than withdrawing into "involuntary" hidden unemployment. This will have the effect of making the costs of the recession more visible.
- Second, the downward rigidity in the participation rate may be because of the rise in what is known as the "added worker effect", where other family members attempt to rejoin the workforce to compensate for job loss or hours reduction by the primary income earner.
- Third, the decline in Superannuation earnings has meant that many who were due to retire have postponed that decision resulting in fewer job openings for new entrants/re-entrants.

¹ GDP growth in the developing world will slow to a projected 2.1 percent in 2009 from 5.8 percent in 2008, according to **World Bank** estimates. The Bank has more than halved its November 2008 projection of 4.4 percent growth in developing countries in 2009, reflecting the rapid deterioration of global financial and economic conditions. (www.worldbank.com)

² The month to month increase February to March in total unemployment in Australia was 1% to a level of 5.7%

- Job prospects for the long term unemployed and the marginally employed have become much worse.

The cumulative result of these factors is a labour market problem of a size and complexity that has not been seen in Queensland for over a decade, and which has occurred much more rapidly than normal. It will manifest itself in a number of ways:

- Increased total unemployment with notable increases in youth unemployment.
- A rapid expansion in the number of long term unemployed (defined as an unemployment duration of one year or more).
- A slowdown in the rate job entry, particularly affecting school and University leavers.
- Increased pockets of chronic unemployment in regional and rural areas and in the outer suburbs of Brisbane.
- Further marginalization of the socially excluded.

The dangers of this situation, which will eventually be resolved by market forces across the world, is the long term damage down to those who experience labour market scarring, and the subsequent future economic costs that will accrue. The need to minimise these costs, both economic and social through appropriately targeted socio economic policies, is the central concern of this paper. It is based on the premise that early and effective policy responses will reduce economic costs in the long run.

2.1 Stress points in the Queensland economy

With the Australian economy in recession, the odds clearly favour the State economy to do the same. As well, there are other aspects of the Queensland economy that are a cause for concern. These include: -

- The reliance in parts of regional Queensland on export-led mining. For example, recent estimates of the significance of Rio-Tinto coal operations to the Bowen Basin, estimate that between one fifth and one quarter of regional GDP comes directly from coal mining output, as do 1/3 of the regions exports (Synergies, 2009). This type of dependence on mining is repeated in other areas.
- A downturn in the property market, both in terms of new building construction and in terms of the turnover in housing stock. In October 2008, total dwelling approvals (trend) in Queensland were 7.4% lower than September 2008, compared to a 3% drop for the same period in Australia as a whole (OESR, 2008) and the total annual change in dwelling approvals was 38.9% and 20.9% respectively. Although this example is for one discreet time period, and may not reflect a general trend, it might be expected that if Queensland is to be the least affected State in Australia by the current recession, then the relative data cited here would have been reversed, with declines in approvals in Australia exceeding those in Queensland.
- The impact of stock market falls on superannuation and other wealth assets, both in terms of wealth effects on shareholders and reductions in consumption of the approximate 85,000 self funded retirees in Queensland³.
- The consequent fall in State Government receipts from stamp duties both in the property market and from the sale of new cars and car registrations. Queensland Treasury estimate that a loss of \$884 million in anticipated tax revenues has already occurred in Queensland 2008-09. Budget estimates

³ These numbers were estimated from national figures supplied by the Self –Funded Retirees Association (2008)

- reduced taxation revenue.
- Observed declines in international tourism-outward trips are starting to exceed inward trips in 2009.
- Signs of a fragile labour market, with the ANZ job indicator (Dec, 2008) indicating that indications of new hires were at their lowest level since 1975.
- Potential for significantly reduced consumer spending.
- Lower GST receipts, with Queensland estimated to lose approximately \$240 million in 2009.

Some of these factors have been noted by Queensland Treasury and factored in their prediction of a 2.5% GSP growth rate in Queensland in 2008/09⁴, while others have not been specially considered. As a result, it may be useful to consider other scenarios where the Queensland economic performance more closely resembles that for Australia.⁵

2.2 Labour market scenarios

This section sets out the likely scenarios for the Queensland economy over the period 2008/09-2009/10 and are based upon work by Mangan (2009) and assuming current growth rate projection for Australia as a whole apply to Queensland.

It must be stressed that, in the absence of formal modelling, a number of operational assumptions are undertaken as well as reliance being placed on secondary data, such as estimates of growth rates and unemployment rates obtained from the observed past behaviour of output, and unemployment in industrialized economies. As a result, the potential outcomes are designed only to indicate the potential magnitude of the unemployment and growth issues that may face the Queensland economy in the next couple of years, and as an aid to effective policy making.

However, at this stage in the recessionary cycle, this type of deductive approach may be more applicable than formal modelling because the implications of the current economic downturn across the world are still unfolding, and the extent and depth of various national and international stimulus packages are either unknown or are yet to be implemented.⁶ The outcomes outlined here represent possible short term labour market occurrences, from a base case to a situation (believed to be the current situation) and examining 2009/10 on the assumption that Queensland performs at the level suggested by the latest GSP Economic Forecast Estimates (EFU), estimates or performs at level suggested for Australia as a whole from the same sources.

A number of studies have traced the stages (likely path) of recent recessions. Claessens, Kose and Terrones (2008), examined 122 recessions, 112 credit contractions, 114 episodes of house price declines and 234 episodes of equity price declines across OECD countries between 1960 and 2007. The aim of their analysis was to determine how macroeconomic and financial variables behave around recessions, credit crunches and asset busts (homes and equity), and to examine if recessions associated with credit crunches and asset price busts differ from other recessions.

⁴ The EFU sets out GSP growth in the last Quarter of 2008/09 in Queensland at 0.5%

⁵ We are unaware of any study that argues that the Queensland Economy is likely to grow more slowly than Australia as a whole.

⁶ For example, modelling the US economy prior to the new stimulus package promised by the incoming President would be ill advised.

- A typical recession lasts almost 4 quarters and is associated with an output drop of 2%, and while recessions have been becoming shorter and milder over time, they remain highly synchronized across countries.
- Episodes of credit crunches, house price and equity price busts last much longer than the recession itself - a credit crunch lasts 2.5 years and is associated with a 20 percent decline in credit, a housing bust tends to persist for up to 4 years and an equity price bust lasts for 10 quarters and reduces the value of the equity base by 50%.
- Recessions associated with credit crunches and house price busts are deeper and last longer than other recessions and the extent of declines in house prices tend to deepen the recession.
- Overall, these findings highlight the belief that linkages between the financial sector and the real economy tends to aggravate output loss during the recession.

On this basis, it is difficult to argue that the current recession world-wide will be short.

Mangan (2009) used current official estimates as a base case and made assumptions relating Output contraction to unemployment growth. In macro economics this is normally referred to as Okun's Law, named after the American economist that first made empirical estimates of the relationship.⁷ Despite its generality, Okun's Law has become a useful concept in macroeconomics both theoretically and empirically and the Okun coefficient is a useful "rule of thumb" in forecasting and policymaking. For example, Blinder (1997, p.241) has remarked that,

Okun's Law "closes the loop between real output growth and changes in unemployment with stunning reliability".

Average Okun coefficients were used to link predicted growth rates to probable unemployment rates within potential outcome (b) and contrasted with current predicted outcome (a). The results are shown in table 1.

Table 1: Short-term labour market outcomes for Queensland 2008/09 to 2009/10 under various scenarios

Potential Outcome (a)	2008/09	2009/10	2009/10
Annual GSP Growth Rate	2.50%	1.00%	0.75%
EFU Unemployment Rate	4.25%	6.25	7.2
Estimated Unemployed	96,664	142,153	163,760

⁷ A typical version of Okun's Law is a gap equation of the type ; $Y_t - y_t^* = a(u_t - u_t^*) + e_t$, $a < 0$ where, y is the log of observed real output, u is the log of observed unemployment, y^* and u^* are corresponding potential values and e_t is a random error term

Increase over current unemployed	12,564	58,053	67,098
Long term unemployed	17,497	37,102	42,741
Potential Outcome (b)	2008/09	2009/10	2009/10
Okun coefficient adjusted unemployment rate	4.50%	7.0%	7.5%
Estimated Unemployed	102,000	163,000	170,583
Increase over current unemployed	17,900	61,500	68,583
Long term unemployed	18,460	42,543 ⁸	44,522

Source: Mangan (2009)

Under the higher estimates (which I believe are conservative) the Queensland labour market will yield the following results:

- By June 2009, total unemployment will approximate 97,000 an increase of 13,000. This will push long term unemployment to 17,500.
- By June 2010 the situation will deteriorate substantially; the unemployment rate will reach 7.5% with over 170,000 persons unemployed and a substantial number long-term unemployed. On the basis of the above predictions it is possible to estimate likely numbers of youth unemployment.

By June 2009

- Youth Unemployment (aged 15-19 years seeking FT) stays at the same rate (13.4 % of total unemployment , *19.3% of total unemployed seeking full time work);
- Total youth unemployed seeking FT work =20,500 (approx)⁹.

By June 2010 (best case scenario)

- One in 3 of new unemployed are youth (this level was average during downturns in 1990's);
- This adds 26,466 to youth unemployment of which 14,027 will be seeking FT;
- Total seeking FT = 24,427;
- Unemployment rate (seeking FT of total unemployed) = 15.0 (14.98%);
- Unemployment rate of total seeking part time 21.1%.

⁸ Using upper end (26%) of LTU range

⁹ Based on the following assumptions; Youth defined as those aged 15-19 years, 71% of Total unemployed are seeking FT work and 53.5 % of youth unemployed are seeking Full time work

By June 2010 (likely scenario):

Use Current ABS Total youth Unemployment rate (24%, at March, 2009, 28.6% in South Australia), which translates into 17.1% youth unemployment for youth seeking Full time work in Queensland as a percentage of total unemployment and 24% of those seeking Full time work suggests total youth seeking FT at 27,800 (approx). This places youth unemployment base towards the levels it was at in the early 1990s. As well, as alarming as these data are, it is likely that youth unemployment will be exceeded in absolute number rather than percentage) by 45-54 years for both men and women. Unemployment is growing fastest among males in both youth and mature workers. Male's fastest growth among youth (about 60%).

To place the unemployment results (both numbers and rates) in perspective, it is useful to consider changes in GSP and total unemployment rates in Queensland over the last decade. This is shown in table 2: -

Table 2: Change in GSP and Unemployment rates Queensland 1992-2008

Year	Change in GSP	Unemployment rate
1992	2.06	10.2
1999	6.07	7.6
2000	5.58	7.4
2001	2.64	8.4
2002	5.85	7.5
2003	4.84	6.8
2004	6.37	5.6
2005	5.03	5.0
2006	3.59	4.6
2007	4.76	3.6
2008	5.31	3.7

Source: OESR, various years

It can be seen that unemployment rates at or above the 7.5% predicted in Outcome 2, existed in Queensland between 1992 and 2004, but not at such low levels of GSP. The lowest levels of GSP recorded in Queensland over the last 20 years were 2.06% in 1992 and 2.64% in 2001. Corresponding with these low growth rates were the highest observed unemployment rates (10.2% and 8/4%). It is also during this period unemployment rates in Queensland were generally above those in the rest of Australia, primarily because of supply side reasons with participation rates being higher in Queensland than elsewhere, and the labour supply in Queensland being boosted by high level of interstate migration, which produced situations of temporary excess supply (LMRU, 2004). Economic growth during the last five years has overshadowed the supply effect (that is job growth exceeded supply growth), but the issue of excess supply may occur again if recession drives up interstate migration and the very low rates of growth are unable to absorb the extra labour supply. The present situation is in one sense a return to the high unemployment rates of two decades ago but at much lower predicted growth rates. It would appear necessary that increased Government spending be used to make up the shortfall in economic growth.

Between August 1998 and December 2008, the yearly average number of unemployed persons in Queensland was approximately 122,000 persons and the yearly average number of long term unemployed was approximately 22,000 persons

(approximately 18% of the total stock of unemployed). On a number of occasions over that ten year period, the total number of unemployed persons exceeded 150,000.¹⁰ Taken in this context, the levels and rates of unemployment suggested in the base-line case and in the best case scenario for 2010, appear to be a return to moderately below average labour market conditions after a period of unusually buoyant labour market conditions.

However of greater concern to policy makers would be the speed of the predicted unemployment increases suggested, particularly in Outcome 2, and the specific problems this creates for new entrants to the labour market and for those already unemployed or marginally attached to the workforce.

For example, a one year increase in unemployment suggested by Outcome 2 of 69,000 persons is rapid by any standards, and would require considerably more by way of policy response that has been the norm in recent years. Over the last decade the largest year on year increase in unemployment (measured at September) was 16,600 between September 2000 and September 2001. During this time, all other year on year movements in the stock of unemployment were downwards, with the largest being a 20,000 person reduction in the number of unemployed between September 2003 and September 2004. However, in the period September 2000 to September 2001, half of the total increase in unemployed (8,756 persons) were classified as long term unemployed. The reason for this is reasonably straightforward. The downturn that impacted in the labour market in that 12 month period, disproportionately affected those that were currently unemployed and job seeking, and as a result, extended their unemployment duration to the point that they became reclassified as being long term unemployed.

Year on year increases of 61,000 persons or 69,000 persons as predicted, are significant events and place a strain on labour market policy makers well in excess of what they have had to face over the last decade. As well, if the "reclassification" effect seen in 2000/01 is repeated, a considerable proportion of the increase in unemployment may end up being reclassified as long term unemployed some time during 2009.

As well as the size of the increase in unemployment, it is also important to predict the characteristics of those made unemployed and the industrial and regional distribution of the unemployment that will occur. Table 1 predicts how many of the unemployed would (at some time during 2009), exceed the 12 month duration period and become classified as long term unemployed. The significance of this group is that they require more dedicated policy attention and as well as the well known scarring effect that long term unemployment has on future job prospects.¹¹

Currently (2007/08), Queensland has the lowest level of long term unemployed in Australia (9.1%), which is also historically low for the State. The corresponding rate for Australia is 15% and for the rest of Australia (excluding Queensland), the rate is 16.1%. The Australian Bureau of Statistics (ABS, 2006) suggests 18%-26% as a default or normal rate for the LTU/Total unemployment ratio, depending upon the level of unemployment.

Long term unemployment in Queensland peaked at 27% in 1998, stayed above 20%

¹⁰ For example, September 1997, March 1998, February 1999, March 2000 and October 2001

¹¹ This particularly true of graduates who face a delayed labour market entry, see Norton, A. (2008) "Will the down turn have a scarring of graduate job seekers, <http://andrewnorton.info/2009/01/will-the-downturn-have-a-scarring-effect-on-graduate-jobseekers>

until 2003, and has averaged above 21% over the last 10 years. Long term unemployed numbers above 30,000 were relatively common in the late 1990's, and so, on a historical basis, the economy has recent experience in coping with numbers such as these. However, numbers of this size normally build up over a lengthy period and not as rapidly as the one year increase of over 25,000 suggested in outcome 2. For example, over the last decade the largest year on year movement was downwards (2002-2003), and the largest upward movement was of approximately 3,000 (2003-2004). While part (but not all) of the problem is simply a reclassification issue, the emergence of so many LTUs in so short a time is a major issue to consider.

In summary, long term unemployment in Queensland is expected to rise to 18,500 in 2009 and grow substantially in 2010 to between 42,500 and 44,500 persons. If the situation of past recessions is followed, youth, mature age and non-standard employees will be the most impacted. However, the credit driven nature of the current recession is unusual in that it is reaching mining and middle level finance sector jobs at a much earlier stage. As well, the labour market position of the over 55 years is unpredictable. This group has (proportionately), been the major beneficiaries of the recent labour market tightness. It is not certain if the recession will bring a return to past trends, mature age workers faring worst, or whether they will maintain their new labour market position at the expense of other groups in the labour market.

Apart from the impacting sectors, current employees most at risk in recession are those on contract or other forms of non-standard employment, although Jewson et. al suggests that in the initial phases of a recession, employers may try to substitute full time positions for casual and part-time positions (Jewson, 2003)¹²; the latest monthly unemployment data in Australia suggest that this stage may have already passed, with the number of part-time jobs falling for the first time in 5 years in Australia. In the initial stages almost all burden, apart from those in the initially impacted sectors, falls upon Private sector workers and own-account workers in world-wide recessions, those in industries with international exposure face increase risk.

2.3 The Industry distribution of job loss

In the absence of formal modelling it is difficult to track the likely path of job loss. However, several sectors have suffered job loss in late 2008/ early 2009¹³. These are:-

- Construction
- Mining
- Business Services
- Aviation
- Retail
- Banking and Finance
- Tourism related activities¹⁴

The significance of these job losses depends upon the size of the job cuts, the reasons for the job cuts (for example, are they a precursor of more job losses) and the

¹² Of course those most at risk of harm are job seekers, including those currently unemployed

¹³ Recent job losses have not fully flowed through to official statistics but press announcements confirm Queensland job losses in Mining[(Okay Creek (230), Mount Isa (159); Coppabella/Moorvale (180), Century (135), Eloise (90) Lady Anne (145); Twin Hills (55) Mongana (130) Wolfram (26); Mount Gordon (100) and Sarat (25); in Banking and Finance (Suncorp (600), ANZ and Macquarie bank and in Community Service (ABC learning) , Gladstone Alumina (600), Qantas (1700 – across Australia)

¹⁴ Difficult to quantify as any job losses here will show up in retail and or Personal Service industry.

significance of the impacted industry in terms of its inter-connectedness with other sectors in the economy.¹⁵

Within Queensland, five private sector industries account for over 55% of employment, and considered jointly with the three layers of Public Service, account for over 70-75%. Specifically, Retail and Wholesale (19.2%) Manufacturing (10.2%), Property and Business Services (10%), Core State Public Service (9.9%), other Public Service (6-7%), are the main employers in the State. By contrast, the Mining industry directly employs less than 2%¹⁶. However, Mining looms large in terms of the impact the sector has as an important client to a number of manufacturing and service industries throughout the State, a high wage employer, a major contributor to export services and a source of State Government Finances. One (partial) way of illustrating the relative impact of job losses in one sector on the rest of the economy, is to refer to “employment” multipliers produced by input-output and CGE models. These data are not without controversy and, in the case of traditional IO analysis, are often misleading when used in a predictive sense.

Nevertheless they represent one of the few means of describing the relative importance to total employment of job losses (gains) in particular sectors. Below, in table 4, elasticity coefficients, and type 1 and type 11 employment multipliers for Queensland industries are shown. By way of definition, an employment multiplier examines the average total employment impact of an employment change in one sector (the impacting sector); type 1 and type 11 estimates may differ due to different assumptions about the distribution of consumption effects. Elasticity coefficients estimate the relationship between a one percent increase in final demand for the product or service in the sector and total employment.¹⁷

The data in table 4 confirms the relative importance of the Mining industry to jobs elsewhere in the economy and concurs with estimates recently made by Rolfe (2009). Taken literally, the over 1,500 job losses announced recently in Queensland would translate into approximately 9,000 full time equivalent jobs throughout the rest of the economy. Employment multipliers of this type do not provide the speed of adjustment and they do not allow for substitution. That is, they do not consider the possibility that some of these retrenched workers will find alternative employment either within the industry or elsewhere. In other words, they are a worst case scenario. They also do not factor the cushioning impact of Government transfer payments on the consumption patterns of those made unemployed (Mangan and Phibbs, 1986).¹⁸

Table 3: Total employment multipliers- Queensland

Sector	Elasticity	Type I	Type II
Sheep	0.641	1.246	1.246
Grains	0.783	1.122	1.122
Beef cattle	0.098	1.501	1.501
Dairy cattle & pigs	0.053	1.353	1.353

¹⁵ One way of doing this is to refer to employment multipliers although the use of these is not without controversy.

¹⁶ See, Government Statistician’s Office “ Guide Lines for Impact Analysis”, Brisbane 1994)

¹⁷ For a discussion of the use of IO in analysing employment in Australia see Valadkhani, A (2003) “Using Input-Output Analysis to Identify Australia’s High Employment Generating industries” *Australian Bulletin of Labour* 29 (3) , 199-211

¹⁸ See, Mangan, J and Phibbs, P (1986) “Income and Employment Loss in a Steel City- Did We get it Wrong?” *Urban Policy and Research* 5(3), 113-117

Other. Agriculture	0.770	1.295	1.295
Sugar Cane	0.000	1.448	1.448
Forestry &Fishing	0.789	1.270	1.270
Black Coal & Oil	2.812	6.208	6.208
Non Ferrous metal	0.987	1.956	1.956
Other Mining	0.367	1.720	1.720
Food manufacturing	1.919	2.708	2.708
Textiles &Footwear	1.199	1.526	1.526
Wood &paper	0.490	1.685	1.685
Chemicals	0.916	1.869	1.869
Non Metallic Minerals	0.340	2.702	2.702
Basic Metals	0.589	1.796	1.796
Machinery	0.945	1.433	1.433
Miscellaneous Manufacturing	1.003	1.456	1.456
Electricity	0.749	1.786	1.786
Residential Building	1.988	2.087	2.087
Other Construction	1.459	1.492	1.492
Trade	1.049	1.486	1.486
Accommodation	1.175	1.477	1.477
Road Transport	0.531	1.679	1.679
Rail & Pipe	0.731	1.643	1.643
Other Transport	0.945	1.935	1.935
Community	0.483	1.487	1.487
Finance	0.519	2.084	2.084
Ownership of Dwellings	2.063	0.000	0.000
Government Administration	1.199	1.437	1.437
Education	1.035	1.070	1.070
Health	1.079	1.123	1.123
Cultural	1.157	1.597	1.597
Personal Services	1.070	1.135	1.135

Source; Centre for Economic Policy Analysis (CEPM) 2006

Other key impacting sectors (type 1 multipliers above 2) include Food manufacturing (2.7); Non-Metallic Minerals (2.08); Residential Building (2.09).

At this stage in the labour downturn, trends in job loss, with the exception of those announced, have yet to emerge. In the absence of current knowledge, it is best to fall back on knowledge of past recessions, with job losses showing up in Construction, retail (particularly in consumer durables), personal services, entertainment and recreation (including tourism). Given the nature and source of the current economic downturn, Banking and Finance are also likely to be impacted. Non-standard and contract employees are first affected in these areas and in the early stages as well, private sector employers may attempt to reduce labour costs, by cutting wages rather than employment.

The current recession is complicated by the fact that it is largely driven by credit restrictions which impact simultaneously across the economy. However, at this stage the main labour market outcomes likely to occur appear to be a reduction in the

number of new jobs, with a resultant growth in the numbers of unsuccessful job seekers, including school leavers and those seeking re-entry, the growth in long term unemployment, and a reduction in working hours for those currently in employment in retail and hospitality.

2.3.1 The spatial distribution

If the names of all unemployed persons in the State were placed in a container and a name drawn out, there is an 80% likelihood that the chosen person would reside in South East Queensland, and a significant chance that the person would live in the outer suburbs of Brisbane (both north and south). As a result, any sustained labour market downturn would disproportionately affect South East Queensland.¹⁹ However, to this point, the announced job losses have come disproportionately in regional Queensland, particularly Central Queensland and North West Queensland. Similarly, those areas that have enjoyed the highest employment growth during the commodity boom such as the Mackay and Fitzroy regions may be most susceptible to job losses via a reversal of the growth process. An added complication is that the concentrated nature of the industry base in rural areas suggests that contraction in key industries could seriously dry up the number of new and entry level jobs in these regions.

2.3.2 Social exclusion

Mangan and Stephen (2007) estimated the extent of social exclusion in Queensland during the economic boom times of 2006/07. They found that despite the buoyant economic conditions of the time approximately 6.4% of the civilian population aged 15 years or over could be regarded as socially excluded. They estimated social exclusion by a two stage process of principal component analysis and multinomial logit. Social exclusion was shown to be a combination of a number of labour market, financial, and social variables such as homelessness, general and social networks. In the second stage of their model they estimated those factors which caused the risk (probability) of being socially excluded to change. These variables were grouped around 4 main sectors:-

- Credit worthiness;
- Work related capacities;
- Educational capacities;
- Health Capacities (access to health services, ability to spend the community average on health);
- Social Amenities and Capacities (access to housing, community participation, Shifts (improvements) in these variables lowered the risk of social exclusion, but the relationship is symmetrical.

The current recession is certain to increase the numbers that may be defined as socially excluded as well as at risk of social exclusion. For example, table 3 uses the methodology (coefficients derived) in the Mangan and Stephen (2007) study to examine the impact of deteriorations in capability variables; specifically a one unit worsening in the predictor variables. The results are shown in table 3:

Table 4: Change in probabilities of exclusion following capability declines

¹⁹ Defined as Brisbane, Sunshine and Gold Coasts, West Moreton , Darling Downs and Wide-Bay Burnett

Probabilities	Original prediction ²⁰	Credit change	Finance change	Education Change	Work Change	Social change	Health change
Not excluded	.839	.814	.817	.803	.793	.845	.804
At risk of exclusion	.095	.101	.097	.104	.135	.091	.096
Excluded	.064	.085	.086	.093	.072	.074	.100
Total	100	100	100	100	100	100	100

By way of interpretation, the default case has 83.9% of the population not at risk, 9.5% at risk of social exclusion and 6.4% able to be defined as socially excluded. The scenarios change as one factor is made worse (with the others held constant). In truth, the other factors would not remain constant and so these scenarios may be regarded as conservative.

It can be seen that the risk of social exclusion increases particularly when working conditions deteriorate (unemployment rate rises, greater job insecurity), for example the not at risk group falls to 79.3%, the at risk group rises to 13.5% and those considered excluded rises to 7.2% of the civilian labour force. If Health capabilities worsen, (less access to treatment, postponement of medical services, reduced health services) the socially excluded group grows even more. Similarly any declines in social factors such as housing availability lead to significant increases in the at-risk and in the socially excluded groups. Deteriorations in all capability variables increase the vulnerability of the population substantially with the socially excluded rising as a consequence.

The clear lesson that during economic recession Governments need to spend to maintain health levels, education and social factors, particularly where unemployment has undermined the ability of the individual to provide for themselves. Otherwise these factors will tend to worsen economic downturns. However, the lesson is clear that in recessionary conditions, on the downswing, unemployment and work change exert the greatest harm on community welfare and should be the focus of attention.

3. Policy issues

Economic recessions create problems because at the very time that Governments need to spend more, their tax receipts are down. Deficit financing is seen as the most likely reaction. While Queensland has had high rates of unemployment before, it has not had such low GSP rates (approaching negative values) in recent memory. This places an added burden on the economy and indicates that recovery will be slow. The analysis above indicates that the labour market will be a key area of the recession with unemployment numbers expected to rise to 170,000 by June 2010, long term unemployment to reach 43,000 and youth unemployment to reach 25,000. These are normal events in a recession, with the most immediate effects being felt at both ends of the age spectrum. However, this recession may be different. Its root cause was in a breakdown of financial markets and this sector, normally characterised by stable middle and higher income jobs, has already witnessed substantial job loss.

As well, there is a looming social crisis among those referred to as the socially

²⁰ Predetermined at .85, .10 .05

excluded. Mangan and Stephen (2007) estimated that 6% of the population (Including labour market participants and their dependents) could be considered socially excluded in Queensland during the period of high economic growth. This estimate is comparable with those made for the UK during a similar period. These persons suffer from a combination of health, housing, employment and financial capacity that effectively reduces their chances to be self supporting in the traditional way. In a policy sense they are difficult to reach. Traditional macro economic variables that stimulate an economy and reach the majority of the population are ineffective in reaching the socially excluded. That so many persons could be placed in this category during a period of economic boom is indicative of the rigid nature of the problem. Failure to tap into the extent of social exclusion in good times will exacerbate the problem to be faced in the current recession.

The policy options put in place currently by the Commonwealth Government are designed to shore up the traditional "macro economy" but apart from the case handouts, they will do little to directly impact upon social exclusion²¹.

3.1 The costs of unemployment and social exclusion

Traditionally, remedial Government policy in the areas of long term unemployment and social exclusion have often been seen as a "duty of care" issue, in which mainstream society has a quasi-charitable obligation to assist those in most need. As economies have gone into recession, this obligation has tended to be sidelined as the needs of others, particularly the short-term unemployed, have taken precedence.

However, over the last decade a rethinking of these issues has led to a realisation that failure to address ingrained unemployment and social exclusion has on-going and increasing costs for society. In other words, dealing with these issues as they arise becomes a prudent financial (investment) decision for Governments. Hunter (2000) detailed the ongoing social costs of social exclusion among Indigenous Australians and pointed out their much higher propensity to be involved in crime, be victims of crime and suffer from long term social problems connected with life style. He pointed out that, denied remedial help, these issues tended to magnify with continuing budget implications for Governments.

The logic behind this argument is quite clear. Short term unemployed persons represent a loss to the economy through the loss of wages and productivity, which flow into the general economy via reduced consumer spending, and diversion of Government spending towards increased social security. Off-setting this is dis-saving. On average a short term unemployed person will be out of work for between 4-6 months. By contrast, the long term unemployed and the socially excluded represent long term commitments of public money. In a financial sense, it is then clearly in the interests of Government to reduce the extent of these problems and to devise the most cost-effective means of dealing with them.

Mangan and Stephen (2007) showed that, in terms of reducing social exclusion, non-traditional means such as providing means of limited credit, extending the availability of public housing and improving access to health services, achieved better results in

²¹ These policies include the purchase of \$8bn in Residential Mortgage Backed Securities by the Office of Financial Management (AOFM) The guaranteeing (for a fee) of Bank, Building Society and Credit Union Funds; the \$10.4Bn stimulus package designed to maintain purchasing power in the economy; postponement of BAS payments; and the Second stimulus package (\$46 Bn) beginning April 2009.

reducing these problems than the traditional macro-economic policy variables. The key approach they suggested was a whole of Government response involving an integrated approach to jointly tackle the housing, health, finance and labour market issues that co-exist amongst this group.

3.1.1 Costs of increased social disadvantage

In this section the costs associated with Social exclusion, and by extension, the potential benefits from reducing (or at least limiting the rate of increase) social exclusion are explored. In this analysis, social exclusion is used as a proxy for all social costs associated with recession and labour market downturn. Most persons, even those exposed to short term unemployment or reduced working hours, will emerge from the recession relatively unscathed. They will require some additional transfer payments from the commonwealth and may benefit from retraining or other forms of labour market program. However, some will be adversely affected in a more profound manner. Mangan and Stephen (2007) highlighted the existence of a substantial group of persons who cope in a buoyant economy, but who are susceptible across a range of categories to economic downturn, these are persons in precarious employment, faced with high housing costs with significant health problems and without normal access to credit or finance. In 2007, this group was seen as being at risk of social exclusion and was estimated at approximately 9.5 % of the population. Calculations for this paper show that the size of this group could increase to 13% in 2010, with some of the earlier group moving into the excluded category. One stage lower than these were the socially excluded, who had largely left the labour market through a variety of health, homelessness and/or long term unemployment. These were estimated to be as high as 6% of the Queensland population.

In 2007, the numbers of persons that had a combination of issues sufficient to classify them as socially excluded was 130,000 adult persons (230,000 persons if dependents are included), with a further 190,000 adults (305,000 in total) at risk of exclusion. By 2010, without increased remedial action these numbers will increase to 300,000-350,000 persons excluded and 440,000 persons in the at-risk. This will represent almost 20% of the Queensland population²². Admittedly some of these persons will be assisted by unemployment benefits and other transfer payments but many will be outside the system, either ineligible or incapable of accessing assistance. The growth in these groups will impose substantial social and economic costs on the community. Arresting the likely growth in the size of these groups is of prime importance as a public policy issue.

3.1.2 Associated costs and benefits

Mangan and Stephen (2007) pointed out that in assessing the potential savings to the economy from a reduction in social exclusion and the risk of social exclusion groups that care should be taken to avoid double counting. For example, the socially disadvantaged make more demands, per capita, on the health system than other groups who have private health cover or who simply are less prone to illness. Therefore it would appear a straight forward conclusion that improving the health of socially excluded persons would reduce total hospital costs and represent a net benefit to society. However, in the short term, reduced health needs means less employment

²² While this percentage seems high it should be remembered that the SIEFA index indicated that 18% of the Queensland Population in 2006/07 could be considered disadvantaged under their socio-economic index.

needs in hospitals and ancillary services and a loss of income to some groups. Moreover if the spare capacity in the health system leads to an expansion of less socially useful activities in medical practice, the overall social benefits become less clear cut.

To help overcome this, they produced a list of current costs to society that would unambiguously be reduced if social exclusion and social disadvantage were reduced. These were:

- Productivity loss from inactivity and exclusion;
- Taxation income loss from inactivity and exclusion;
- payments diverted to social security and away from other uses;
- additional health costs associated with the socially disadvantaged.

This list fails to consider other potential costs such as Government administration costs, and time variant costs such as wage scarring and inter-generational costs such as the disadvantage passed on to children of the socially excluded and should be seen as conservative.

Using the methodology discussed in Mangan and Stephen (2007) and updating these on the basis of estimates of excluded/at risk estimates for 2010. The following cost/benefit approximations can be made:

Productivity gains from

- moving the excluded group one income quintile – \$2.3 Billion
- moving the excluded group two income quintiles- 5.06 Billion
- moving the at risk group, through employment or more paid hours, one income quintile- 3.55 Billion
- moving the at risk group, through employment or more paid hours, two income quintile- 5.92 Billion

Additional tax revenue

Using the average income rates for the second and third lowest quintile and the average associated tax rates, the tax gains from raising productivity described above approximate \$466 million- 1.51 Billion for the excluded and 1.36 Billion- 2.91 Billion for those at risk.

Savings in Social Security

Based on the methodology described in Mangan and Stephen (2007), savings in current social security payments would be 864 million (excluded) and 1.42 Billion for the at risk group.

Savings in the health sector

Mangan and Stephen, estimated that the socially excluded and those at risk are 4 times and 2.6 times more likely, respectively, to suffer illness requiring hospitalisation than the average member of the Queensland population. On this basis the potential savings from disadvantaged acquiring average hospital use characteristics was 23.5% of the total Queensland public Hospital budget, or 1.22 Billion from the excluded and \$773 million for the at risk groups.

Given that these types of costs existed in periods of economic prosperity it is perhaps unreasonable to expect Government policy to eradicate them completely during periods of recession. A more realistic aim would be to maintain the levels of exclusion and at risk to the same levels of 2007/08. Put another way, what are the additional

costs that will accrue if social exclusion levels and at risk levels are allowed to rise to the levels predicted for 2010 from their current levels.

These additional costs from increases in the excluded and at risk groups taken collectively are (taking the most conservative estimates)

- Additional productivity losses 1.750 Billion
- Tax losses- 529 million
- Additional Social security- 682 million
- Additional Health costs 630 million

In other words the additional social and economic burden placed on the Queensland economy by increases in the excluded and the at- risk group (most of whom would also be unemployed or underemployed) is on conservative estimates \$3.58 Billion per annum. The expenditure of moneys to help prevent this occurrence represents sound economic management.

3.2 Potential policy for the Commonwealth and State Governments

Policy making can only proceed on the basis of accurate information on the state of the labour market. Official data tends to lag actual events by several months and the apparently muted effects the world-wide recession is having in Australia (compared to overseas), may be misleading. Nevertheless, on the basis of current evidence, the State will be faced with larger labour market issues, significant problems for new-job seekers and increased social exclusion. In this section, a brief discussion of generic labour market options at the Commonwealth and State levels is provided, as well as more specific policies for each of the outlined scenarios.

3.3 Commonwealth Government responses

Fiscal Policies; including increased Government spending on infrastructure projects; tax cuts for business and consumers; increases in Government transfer payments and wage subsidies to help protect at risk groups such as mature age and workers with a disability. Consideration may also be given to the supply side of the labour market by altering immigration intakes, encouraging increased school retention and influencing the retirement rate, deferring tax payments and/or offering business start-up incentives. After a decade of Government retreat from these activities, the main issue here may be the efficiency of the delivery mechanisms rather than the value of the programs.

Monetary Policies; encourage the RBA to lower interest rates and the Banks to pass these cuts on to consumers; guarantee deposits and take other measures to speed up credit availability, specifically target credit card interest.²³

Labour Market programs; increase case management services for the unemployed; traineeships and apprenticeships for new and re-entrants; education and training and re-training packages for the unemployed.

Most of these options are now in place and future Commonwealth action will depend upon the impact of these policies. In the meantime, the use of active labour market policies for relocating retrenched workers and creating options for new job seekers is

²³ The danger here being the impact of further rate cuts on retirees especially self funded retirees

possibly their best course of immediate action.

State Governments; State Governments are more restricted in their range of potential actions, but can be influential in a number of ways.

Infrastructure spending; while this must be coordinated with commonwealth projects, a well managed public works program can be very effective in taking up the slack left by downturns in mining and manufacturing. In recessions, the dangers of crowding out private sector investment are reduced and the costs of factors of production are less. In affected regional areas there is often a ready workforce of retrenched miners etc.

Manipulation of State taxes; always a difficult policy option, one because they deprived the State of needed revenue at a time of maximum demand on their services and, two, because economists often argue that minor variations in areas such as payroll tax and stamp duty do not produce much in the way of economic stimulation.²⁴

Active labour market Policies; State Governments are well suited to initiate or manage active labour market programs because they normally maintain large departments geared to these tasks. Such policies can range from traineeship and apprenticeship policies, to allowing new entrants a taste of the labour market in the Public Service; relocation and re-training programs for retrenched workers; targeted packages by type of worker (mature; youth; indigenous); targeted by geographical location; targeted by space.

3.4 Specific Recommendations (for State) by outcome

Base-line case-modest increase in total unemployment (17,900) with a LTU number of 18,500; main areas of concern - new entrants and retrenched workers in rural areas.

Recommended policy; intensification of labour market programs including use of traineeship and apprenticeship for new entrants; graduate experience programs within Public Service and training, re-location programs for retrenched workers and targeted education and life skill programs for long term unemployed. Some consideration for capital works in regional areas impacted by Mining retrenchments.²⁵

Outcome 1 (2009/10) - One year increase in total unemployment of 61,500 with LTU of 42,500.

Recommended policy; as above but with more intensity and particular attention being paid to preventing scarring of new entrants by creating entry opportunities and in re-engaging long term unemployed. This may involve some incentives to employers and an expansion of short-term hiring in the Public Service. The Infrastructure program needs to become more targeted and spread over a greater geographical area. Innovative programs to increase job seeking activity among unemployed such as travel assistance need to be negotiated with Commonwealth. Care must be taken to identify the composition of the stock of unemployed to see if the expected casualties, youth, mature and non-standard workers bear the brunt or is the new "credit crunch" recession impacting on previously secure workers?

²⁴ See " In Defence of Payroll Tax, SMH.com.au Dec 30 2004

²⁵ The difficulty here is that the practice of fly-in fly out and drive in-drive out workers and disparate mine purchasing policy means that economic impacts from reductions in Mine activity are not always felt in the surrounding areas.

Outcome 2 (2009/10) - One year increase in total unemployed of 68,000, LTU of 44,500. The problem here is becoming not only the level of total employment, but also the rapidity of its growth. Greater information should be sought on the causes of unemployment and the chief impacting sectors: direct assistance to companies facing closure (where feasible), major emphasis on maintaining entry level jobs/labour market experience of new job seekers, maximum expansion of infrastructure program, possible manipulation of state taxes.

4. Summary

The labour market outcomes for Queensland discussed here, even the more serious, Outcome 2, are not beyond the experience of the recent path, but the 2009/10 outcomes are different from past events, due to the speed of the growth in unemployment and long term unemployment. In part, this is a consequence of the previous tightness of the labour market which produced a range of jobs that were very sensitive to a slow-down in growth and where participation was at historically high levels. As well, the events associated with the world credit crisis are somewhat unique and the real effects may not have yet surfaced. Although Queensland has been described as being better able to cope than the rest of the Australian economy, its relative reliance on Mining and Tourism allows a counter argument to be mounted, whereby the boom States of Western Australia and Queensland, are likely to be the most affected.

This paper used a base line scenario (current) based on GSP performance for 2008/09 suggested by the EFU forecasts but with different, (and we believe), more likely accompanying unemployment rates, and compared these with possible labour outcomes for Queensland in 2009/10. Under both outcomes, year to year increases in unemployment of over 60,000 persons are predicted, and increase in long term unemployment of up to 25,000.

ABS data revealed recently, that the Queensland labour market has already reached a total unemployment rate of 4.5% and total unemployment of 105,000. In other words, it is tracking to at least reach the outcomes predicted in this paper for 2009/10, and therefore a program of active labour market programs is required to mitigate the effects of the recession. Specifically a mechanism for facilitating the continued entry of new job seekers into the labour market needs to be implemented. One possible way to do this is an expansion of the graduate and grade 12 intakes by Public Service Departments and/or an expansion of trainee and apprenticeships, funded by the Commonwealth, but administered by the State.

Secondly, case management and retraining of long term unemployed needs to be intensified with the numbers of LTU predicted to rise sharply. Thirdly, the regional adjustment packages for retrenched regional workers need to be increased with public servants and unions working closely with employers.

The latter part of the paper demonstrated the likely rise in those suffering labour market and financial stress (the at-risk group) and those formally classified as socially excluded. The additional costs associated with this have been conservatively measured at 3.6 Billion. Action to reduce these costs becomes important from the point of view of effective use of Government money as well as from a social point of view.

In line with this the demand management powers of the State through increased spending and infrastructure programs, need to be activated in a manner complementary to Commonwealth issues.

In the final analysis, some consensus need be found on what constitutes an equilibrium or socially acceptable level of unemployment. A decade ago, policy makers would have been pleased with unemployment rates of 6 or 7% and the 5% target of the late 1990's was seen by some as unrealistic. However, the risks of complacency are high. As Caton (2008) points out, that unemployment behaviour tends to have thresholds. Once the rate climbs to 6% it can very quickly go to 10%.

At this stage there is no real guide as to what stage in the recession cycle the economy is in, although this report believes it is somewhere between stages 2 and 3. Some jobs have been lost in Mining and Finance and newspapers are predicting big losses in retail and hospitality.²⁶ The normally reliable ANZ job indicators are also showing a big drop in new job opportunities. On this basis, the main task is to maintain opportunities for new job seekers and for the provision of re-location packages for retrenched workers.

²⁶ See for example Sydney Morning Herald 16th January 2009 "500.00 jobless in work shake-up" p.1