

June 2020



## The Recovery Book

What Australian governments  
should do now

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This report was written by John Daley, Danielle Wood, Brendan Coates, Stephen Duckett, Julie Sonnemann, Marion Terrill, Tony Wood and Kate Griffiths. All Grattan Institute staff have made substantial contributions to this report.

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## Overview

COVID-19 is the biggest social and economic shock since World War II. Across the world, hundreds of thousands have died. In Australia, millions are out of work. Within two months, policies and systems for welfare, employment, childcare, health, and education have been turned on their head after decades of (at most) incremental reform.

Recovering from such a shock is a big task. Australia needs to roll back social distancing restrictions in a controlled way so that the virus does not again spread exponentially through the community.

Australia faces a globally synchronised deep recession. Governments have cushioned the impacts with more than \$160 billion of spending, to support businesses and households. But many of these programs are due to roll off together at the end of September. To avoid a severe economic crunch, they should be wound down more gradually in a package that will cost about \$30 billion in 2020-21.

The recovery should also be aided by ongoing reforms such as permanent increases to JobSeeker, Rent Assistance, and childcare that would cost at least \$21 billion over the next two years. If governments want to get unemployment back down to 5 per cent or below by mid-2022 then they will need to be prepared to add to the temporary stimulus by spending another \$20-to-\$40 billion on services, infrastructure, and building social housing, depending on how the economic recovery plays out. Assuming interest rates remain low, governments should be in no rush to consolidate their budgets while economies remain weak in Australia and across the globe.

COVID-19 has changed long-term consumer and business behaviour. This implies structural change in the economy. Governments should let businesses close if they lack a sustainable future, and avoid bailouts unless necessary to underpin capacity in a vital industry.

Some changes to working patterns are likely to stick, even without health restrictions. Governments need to adapt their transport priorities to the new world, particularly for cycling infrastructure, congestion pricing, and incentives for smaller cars. But they should not rush to spend money on new infrastructure, unless the case is compelling after taking into account the changed world in which we now live.

Australia should not simply ‘snap-back’ to its old health system; instead, many changes that were implemented during the emergency should be kept and adapted for the future. These include improved access through telehealth, more use of out-of-hospital care, and better use of private hospital facilities.

Many school students have learnt less than normal with remote instruction, particularly if they come from disadvantaged backgrounds. Over the next six months, governments should fund schools to provide additional tutoring programs for disadvantaged students.

Parliaments were suspended, and governments have used special powers and spent in unprecedented ways through an emergency. Some changes – such as the National Cabinet – are worth keeping. But our institutions need to re-establish appropriate scrutiny, debate, and representation for the longer term. Decision-making and spending must be transparent. And establishing a national integrity commission is now even more urgent, given that emergencies often provide cover for wrongdoing.

This is a huge agenda, almost all needed in the next six months. It will stretch government resources. Other less urgent (but important) reforms should wait until there is time and resources to do them properly.

## Recommendations

|                                   | Commonwealth                                                                                                                                                                                                                                                                                                                                                                                                                                                                | States and territories                                                                                                                                                                                                         |
|-----------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Controlling COVID-19</b>       | <ul style="list-style-type: none"> <li>• Maintain mandatory quarantine of international arrivals</li> <li>• Support states in promoting ongoing social distancing</li> </ul>                                                                                                                                                                                                                                                                                                | <ul style="list-style-type: none"> <li>• Re-open workplaces slowly; maintain testing and contact tracing</li> <li>• Use local lockdowns and communicate ahead of implementation</li> </ul>                                     |
| <b>Fiscal and monetary policy</b> | <ul style="list-style-type: none"> <li>• Restore economic activity to its potential level, with unemployment at or below 5 per cent, within the next two years</li> <li>• Deploy substantial further fiscal stimulus (incl. support for business and workers, social housing, and small-scale infrastructure)</li> <li>• Don't focus on budget consolidation in the near-term</li> <li>• Abandon legislated increases in compulsory superannuation contributions</li> </ul> |                                                                                                                                                                                                                                |
| <b>Business</b>                   | <ul style="list-style-type: none"> <li>• Extend JobKeeper for 3 months for businesses still in strife; end it early for those no longer in need; pay in advance; include temporary migrants, short-term casuals, and unis; lower rate for part-time workers</li> <li>• Avoid bailouts, and enforce competition laws</li> </ul>                                                                                                                                              | <ul style="list-style-type: none"> <li>• Strengthen the commercial tenancy code, including rent relief for businesses on JobKeeper</li> <li>• Promote local tourism</li> </ul>                                                 |
| <b>Supporting workers</b>         | <ul style="list-style-type: none"> <li>• Gradually phase down the Coronavirus Supplement</li> <li>• Raise the permanent rate of JobSeeker and boost Rent Assistance</li> <li>• Tighten early access to superannuation before the second tranche</li> <li>• Boost the childcare subsidy and flatten the taper rate</li> </ul>                                                                                                                                                | <ul style="list-style-type: none"> <li>• Implement social distancing and hygiene measures on public transport; provide temporary parking and shuttles for commuters; repurpose road space for cycling and walking</li> </ul>   |
| <b>Infrastructure</b>             | <ul style="list-style-type: none"> <li>• Focus on small, shovel-ready projects</li> </ul>                                                                                                                                                                                                                                                                                                                                                                                   | <ul style="list-style-type: none"> <li>• Pause large projects where the benefits are now in doubt</li> <li>• Fast-track small projects and maintenance work</li> </ul>                                                         |
| <b>Industry</b>                   | <ul style="list-style-type: none"> <li>• Generally avoid industry assistance; establish clear criteria if supporting projects</li> <li>• Ignore calls for infrastructure spending inconsistent with a low-emissions future</li> </ul>                                                                                                                                                                                                                                       |                                                                                                                                                                                                                                |
| <b>Health</b>                     | <ul style="list-style-type: none"> <li>• Keep GP telehealth but revise items for continuity of care</li> </ul>                                                                                                                                                                                                                                                                                                                                                              | <ul style="list-style-type: none"> <li>• Revise care paths when restarting elective procedures to reduce low- or no-value care and encourage workforce substitution</li> <li>• Expand out-of-hospital care services</li> </ul> |
| <b>Education</b>                  | <ul style="list-style-type: none"> <li>• Promote Australia as 'open for international students' from 2021</li> <li>• Invest in a national school education 'catch-up' strategy via a temporary loading for the remainder of 2020</li> </ul>                                                                                                                                                                                                                                 | <ul style="list-style-type: none"> <li>• Help disadvantaged students recover learning losses through tutoring, and literacy and numeracy programs</li> </ul>                                                                   |
| <b>Institutions</b>               | <ul style="list-style-type: none"> <li>• Continue to focus on federal-state cooperation through the recovery (including tough reforms on funding and responsibilities)</li> <li>• Bring back parliaments for catch-up sittings (virtually, if need be) and unwind ministerial discretion</li> <li>• Develop rules to provide transparency on National Cabinet meetings; establish a national integrity commission</li> </ul>                                                |                                                                                                                                                                                                                                |

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## 1 Priorities for recovery

### 1.1 Where are we now?

COVID-19 is the biggest social and economic shock since World War II. Across the world, hundreds of thousands have died. In Australia, millions are out of work. Within two months, policies and systems for welfare, employment, childcare, health, and education have been turned on their head after decades of (at most) incremental reform.

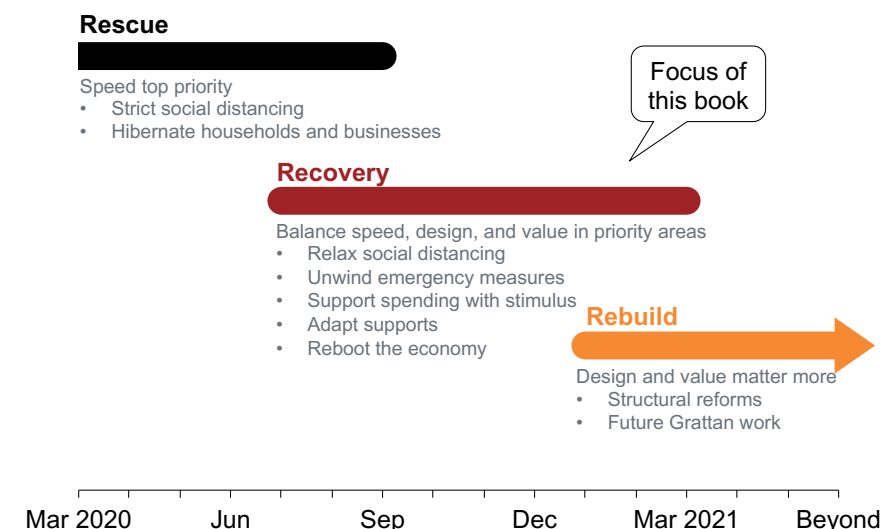
Australia has been luckier, and has managed the crisis better, than most. New case numbers are small, quarantine systems are in place, there is much more capacity to test, track, and trace new cases, and hospitals are better placed to respond to any resurgence.

Governments are relaxing many of the restrictions that were put in place to limit the spread of the virus. But Australia is far from 'back to normal'. We are likely to be living in a 'with-COVID' world rather than a 'post-COVID' world for a long time. Social behaviour and government policy need to reflect that new cases from overseas can spark new outbreaks, and some states will continue to have some COVID-19 in the community.

Nevertheless, many of the emergency support measures can now be wound back or refined. The patient may not be back to full health, but the focus of Australia's people, businesses, and governments, is now on recovery. This *Recovery Book* explains how governments should shape this transition from emergency to a 'with-COVID' world.

Commonwealth, state, and territory governments all deferred their budgets, normally due in May, until October. These budgets are a staging post for policies focused on recovery. This book aims to lay out the priorities for these October 2020 budgets. It is unlike Grattan's Orange Books in the past, which have tried to articulate overall priorities for the longer term. The impact of COVID-19 is so large that

Figure 1.1: Australia is now entering the recovery phase



(for once) the urgent is also the important. The agenda we lay out should also be the focus for the National Cabinet, which has economic recovery as its primary focus.

### 1.2 The near-term agenda

Australia is emerging from the 'rescue phase' of this crisis and is now entering the 'recovery phase' (see Figure 1.1).

There is a lot that needs to be done within six months. By October, Australian governments must decide:

- How do we unwind policies put in place for the emergency (such as JobKeeper, rent relief, payroll tax relief, and suspension of insolvency laws) that cannot be sustained for the longer term?
- How do we refine – rather than simply wind back – those policy changes driven by the COVID-19 emergency (such as telehealth, higher JobSeeker payments, and childcare support) that may be worth keeping for the longer term?
- What further policies are required for a with-COVID world (such as changes to the transport system, or dealing with the secondary health effects of lockdown)?
- What policies do we need to add or change to cope with an ‘ordinary’ globally synchronised deep recession, to minimise the long-term economic damage that would occur if viable businesses were destroyed or more people become long-term unemployed?<sup>1</sup>
- How do we remediate the losses that have hit some particularly hard (such as lost education for disadvantaged children)?

This book outlines the huge policy agenda that is time critical, and that governments should deal with over the next six months (see Figure 1.2).

### 1.3 Prioritisation

Given the size of this agenda, and its urgency – either because programs are expiring, or because it is important to respond quickly and decisively in a recession – governments are unlikely to have political or bureaucratic resources to successfully pursue long-term reforms that are outside these parameters, no matter how valuable they might be.

Figure 1.2: The urgent agenda is very large

#### Emergency policies to unwind gradually

- JobKeeper
- SME loan guarantee
- State tax and fee relief
- Residential tenancy law suspension
- Commercial tenancy law suspension
- Insolvency law suspension
- Government transparency and accountability suspension

#### Emergency measures to keep but refine

- Quarantine arrangements
- Social distancing requirements
- JobSeeker increase and eligibility
- Childcare affordability
- Telehealth
- Private / public health interaction
- National Cabinet

#### Policies for the ‘with-COVID’ world

- Social distancing behaviour promotion
- Public transport social distancing and hygiene
- Commuter parking
- Congestion pricing
- Major infrastructure project rethink given behaviour changes

#### Policies in response to the recession

- Unconventional monetary policy
- Rent Allowance increase
- Social housing investment
- Small infrastructure projects
- Hard-hit industry support
- International student promotion
- Local tourism promotion
- Catch-up tutoring for disadvantaged students

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1. Cerra et al (2020) and see Chapter 3.

Structural reforms are needed: COVID-19 will have substantial and long-lasting impacts on our economy and society. Big adjustments will be required to adapt to a 'with-COVID' world. Economic growth may be slower while we absorb the costs of those adjustments. Bold economic reforms can accelerate the transition and minimise the costs.

But wholesale reforms with big payoffs are inherently complex and invoke big trade-offs. Therefore such reforms should not be the focus of governments in the immediate recovery phase. When governments try to do too much, they can implement half-baked reforms that usually come to nothing.<sup>2</sup> Consequently those decisions that don't have to be taken within six months will not be the focus of this book, and we think governments should deliberately defer them too.

Of course, major policy issues not related to COVID-19, many of which we canvassed in Grattan's *Commonwealth Orange Book 2019* and *State Orange Book 2018*, have not gone away.<sup>3</sup> Reforming electricity system regulation, teacher workforce reform, and tax reform – among many other priorities – should still happen. Governments can use the coming months to lay the foundations for such reforms by highlighting the problems we face, and beginning the preparatory work on policy design to solve them. But governments should not attempt to tackle in earnest such issues not related to COVID-19 until more immediate challenges have been addressed.

Grattan will release further work next year focusing on what governments should do beyond the recovery phase to help rebuild the Australian economy and living standards for years to come.

## 1.4 Structure of this book

The remainder of this book looks at the urgent issues that Australian governments should tackle between now and the end of 2020.

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2. Daley et al (2019, pp. 21–22).

3. Daley et al (2019); and Daley et al (2018b).

Chapter 2 examines how Australia should emerge from the variety of **social and economic restrictions** that have been put in place to restrict the spread of COVID-19.

Chapter 3 considers the high-level **fiscal and monetary policy** responses required as Australia confronts a globally synchronised deep recession. Substantial fiscal stimulus is needed to help the economy return to full employment. And the Reserve Bank should consider adopting further unconventional monetary policies to boost employment and spur on inflation and faster wage growth.

Chapter 4 discusses how **business support measures** should be adapted. A number of emergency measures, including the JobKeeper wage subsidy scheme and suspension of the usual rules for tenancy and insolvency, were put in place to enable businesses to 'hibernate' through the crisis. These measures must now be unwound in a way that minimises the long-term economic damage.

Chapter 5 investigates how to help **households back to work**. Hundreds of thousands of Australians have lost work, and will need new supports and a stronger safety net for longer than the programs currently in place. Others have been working from home for the past three months to help minimise the spread of COVID-19. As they return to work, the Commonwealth Government should increase the support it provides for childcare to reduce the disincentives to work. And public and private transport systems need to be adapted to help people get to work in a 'with-COVID' world.

Chapter 6 thinks through how governments should – and should not – invest in **infrastructure** and assist **industries**. Governments will be under pressure to do more to reduce the stresses of a significant recession, but should keep a cool head and focus on 'no regrets' projects.



Chapter 7 discusses the changes made to **health systems**, how these should be improved to protect even better against COVID-19, and how to refine beneficial changes that were put in place during the past few months, particularly telehealth, and the relationship between the private and public health systems.

Chapter 8 explores how to help **students returning to school**. A temporary, targeted 'catch-up' package for disadvantaged students would help recover the learning losses from remote schooling.

Chapter 9 considers Australia's **governance institutions**, many of which were suspended or radically reshaped through the emergency. Some new structures, such as the National Cabinet, will persist and need to be refined to ensure that norms of transparency and accountability are sustained.

## 2 Emerging from hibernation

Through the recovery phase – and beyond – Australian governments must continue to monitor the progress of COVID-19. Depending on the extent of its spread, they will have to adapt, relax or re-impose restrictions on social and economic activity, including international travel, public gatherings, public transport, schools, workplaces, and community activities, and encourage individual behaviour, to prevent the transmission of COVID-19.

Designing, monitoring, and adapting these restrictions has consumed a lot of government attention through the rescue phase, and is likely to continue to do so in the recovery phase.

Precisely because Australia has been much more successful at containing COVID-19 than most other countries, mandatory quarantining of international arrivals will still be needed for quite some time.

Continued testing, and swift and accurate contact tracing will be crucial as students return to the classroom and workers return to the office. By isolating people who may have been infected, chains of transmission can be broken, and outbreaks controlled.<sup>4</sup>

But contact tracing alone is not sufficient. It should be combined with structural measures and ongoing social distancing to increase the likelihood of controlling outbreaks.

Australia is progressively easing social distancing restrictions and coming out of lockdown. Decisions on when – and in which order – restrictions should be eased should be informed by evidence.

Schools can remain open with social distancing policies in place, but should close if a case is detected. Shops are more risky, particularly

if they have a high density of patrons. Workplaces are particularly high risk and should be re-opened slowly, with people continuing to work from home where possible to minimise the number of people interacting.

While there are active cases of COVID-19 in Australia, there is always the possibility of a second wave. The risk of a second wave is higher if policies and behaviour return to normal too soon. State governments must be prepared to act decisively to control outbreaks, through local lockdowns if need be.

### 2.1 Robust quarantine and contact tracing systems

The rest of the world is still a long way from control of COVID-19, and Australia must make sure it does not import new cases. Current mandatory quarantining of international arrivals must remain in place, and breaches – a growing cause of outbreaks in Australia – must be prevented.<sup>5</sup> The Commonwealth Government should maintain and enforce safety guidelines for new arrivals.

Quarantine exemptions could be made with other countries, such as New Zealand, that have no active COVID-19 cases and that have their own effective international arrival practices in place.

Robust contact tracing systems are essential if restrictions are lifted while the virus is still circulating in the community. If minor outbreaks occur, and can be managed through contact tracing and isolation, then governments can have more confidence in lifting restrictions.<sup>6</sup> The big risk is an outbreak that overwhelms contact tracing capacity and ignites exponential spread of the virus through the community. All

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5. Laschon (2020).

6. Duckett et al (2020, pp. 41–43).

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4. WHO (2020).

Australian states and territories now have dedicated contact tracing teams, potentially assisted by the COVIDSafe app.<sup>7</sup>

## 2.2 Restrictions on activity

While contact tracing can reduce the risk of COVID-19 cases turning into outbreaks, it cannot on its own prevent the spread of COVID-19.<sup>8</sup> Contact tracing must be combined with behaviour changes and social distancing measures designed to separate infected and uninfected people, preventing the transmission of the virus from one person to another.<sup>9</sup>

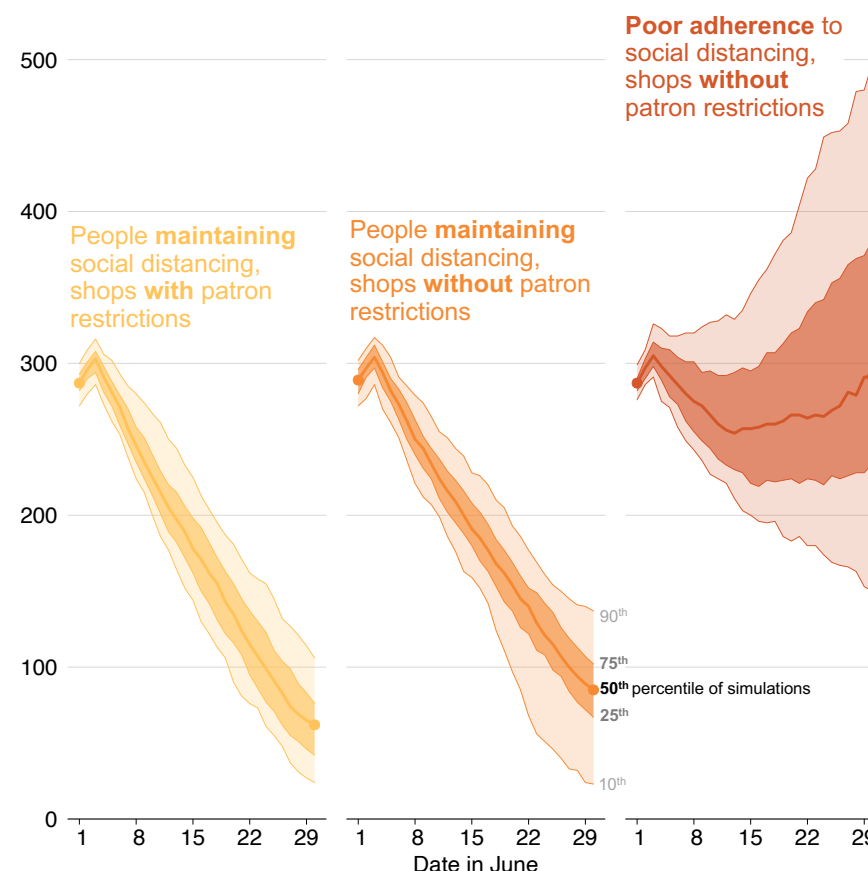
The extent and design of restrictions on social and economic activity depends on the current level of local transmission (discussed in the next section), the level of social adherence to behavioural change, the impact of each restriction on infection rates, and the social and economic cost of each restriction.

Grattan modelling suggests that careful reopening of schools won't increase infection rates much.<sup>10</sup> If all shops and workplaces are to be re-opened, it will be vital to maintain behaviours such as physical distancing and handwashing, to minimise the use of shared eating spaces, and to maximise ventilation to stop outbreaks from gathering speed.<sup>11</sup> Figure 2.1 shows how much individual behaviour can affect the spread of infection when restrictions are lifted.<sup>12</sup>

Indoor events are likely to lead back to rapid growth of infections unless there are no local cases, or so few that contact tracing systems are

7. Although actual use of the app by health officials has been limited, the number of people using the app has been below expectations, and the app's functionality has been low: Duckett et al (2020, Section 2.1).
8. Kucharski et al (2020); and F. He et al (2020).
9. Fineberg et al (2020, p. 7).
10. Duckett et al (2020, pp. 47–48).
11. Duckett et al (ibid, pp. 44–46).
12. Ibid (Figure 3.5).

**Figure 2.1: Poor social distancing in open shops presents a severe risk**  
Results from simulation of active local COVID-19 cases



Notes: Grattan's COVID-19 microsimulation model, which is described in Duckett et al (2020, Appendix A). Starting point is imputed active local cases at 1 June. This chart mostly reflects case numbers in Victoria and NSW, because active cases were low or zero elsewhere. Duckett et al (ibid, Appendix B) shows state results.

effective in containing outbreaks. Large outdoor events – such as sporting events – may pose less risk if there is ample ventilation and limited social mixing.<sup>13</sup> But mass gatherings create the risk of millions of potential contacts and chances to transmit the virus, which can overwhelm contact tracing capacity.

### 2.3 The strategic design of restrictions

The extent of restrictions on economic and social behaviour should depend on the extent of local transmission at the time.

There are three underlying scenarios, which require different responses:

- Elimination: there is *no* local transmission – this implies that all active cases have been identified and effectively quarantined.
- Suppression: There is *some* local transmission, but the number of new cases is small, and not obviously increasing.
- Growth: Local transmissions are evidently increasing.

States should maintain different restrictions if they have different rates of local transmission. Restrictions are obviously needed much less in states that have effectively eliminated the virus from their local population. These states are quite rationally keeping their borders closed to states where COVID-19 persists.

#### 2.3.1 Elimination: when there are no active COVID-19 cases

When there are no active cases in a community – a feat achieved by the NT, SA, Tasmania, and WA<sup>14</sup> – much more of life can return to normal. This may not amount to complete ‘elimination’, because

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13. Rainey et al (2016).

14. Plank et al (2020).

travellers may enter with the disease. But other restrictions can be removed if travellers are quarantined, and (crucially) care is taken to ensure that while in quarantine they do not infect anyone in the wider community. In this world, capacity constraints on workplaces, shops, and hospitality can be removed.

A government can only afford to permit this much activity if it is confident that there really are no cases out in the community. But some people with COVID-19 have remained infectious long after their diagnosis, well beyond 21 days.<sup>15</sup> Therefore testing must remain a routine part of life even after an area thinks it is free of COVID-19. If local cases are identified, contact tracers must be at the ready, and widespread testing should restart in affected areas.

Of course if most restrictions have been lifted, then any quarantine breach is likely to lead to rapid growth in infections. To reduce the potential rate of growth, a government would be sensible to keep suppression measures in place that are relatively low cost (such as encouraging people to wash their hands regularly). And a government must be ready to reimpose restrictions on activities that tend to increase transmission a lot if there is a quarantine breach.

#### 2.3.2 Suppression: while there are few active COVID-19 cases in Australia

If there are only a few local transmissions, a government needs a combination of restrictions and effective track-and-trace systems to suppress the growth of infections. If a government only aims to suppress the virus, but not eliminate it, then some restrictions can be released earlier.

The disadvantage of such a suppression strategy is that many restrictions must remain in place indefinitely – affecting life much more

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15. Modellers acknowledge this risk in New Zealand: Plank et al (ibid).

than if the virus has been eliminated – and government is relying heavily on its track and trace system being continuously effective in breaking most of the chains of infection. By contrast, if the virus has been eliminated, the track and trace system is only under pressure on the rare occasions that the disease manages to escape from quarantine.

In a state that has suppressed – but not eliminated – the virus, rates of infection will depend on:

- the efficacy of testing, contact tracing, and isolation;
- individual behaviour, such as handwashing, physical distancing, and mask wearing; and
- restrictions on social and economic behaviour.

Individual behaviour can change, so it is impossible to predict accurately how many social and economic restrictions can be lifted by how much before infection rates increase, and the virus again spreads uncontrollably. But governments can make informed estimates about which restrictions can be lifted reasonably. They can learn from experience which environments are most prone to the spread of infection. And they should be prepared to reimpose some restrictions if it becomes apparent that local infections are growing quickly, as they have in late June 2020 in Victoria.

Schools are already open, and they should continue to enforce social distancing policies, to reduce risk of outbreaks before detection. If a case is detected in a school, it should be closed and rigorous contact tracing implemented.

Patron spacing limits in shops should be maintained if local transmission of COVID-19 continues in particular areas. The onus should be on the employer or owner of the workplace, cafe, or shop, to be aware of the risks, to have developed a safe opening plan informed

by resources from government health authorities, and to enforce the plan. The onus is on public health authorities to be clear about what a good safe opening plan looks like for employers and owners.

If local transmission is not increasing, workplaces should be reopened slowly. The risk of opening workplaces will depend on how workplaces are opened and how people behave. The risks are lower if the return to work is staggered, with a proportion of people working from home on any given day by rotation, and office time limited to more important activities.<sup>16</sup> There should be continued reminders about the importance of social distancing and hygiene. Workers should keep their distance from each other, and minimise time spent in shared spaces such as kitchens.<sup>17</sup>

Government guidelines for businesses should be clear, and their implementation should be monitored. When there is an infection in a workplace, rigorous contact tracing, testing, and isolation must be implemented. Workers who show symptoms of COVID-19 must not be allowed in the workplace, and must be supported to continue their work from home where possible, or through government support if not.<sup>18</sup>

People in the community should continue to take social distancing precautions, including wearing masks in high-risk situations.<sup>19</sup> As fewer COVID-19 cases are reported and risk perceptions are lowered, people must be reminded about their social distancing responsibilities. Hand sanitiser must be available and used as part of the new normal.<sup>20</sup>

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16. Prem et al (2020). See also Cirrincione et al (2020, section 3.1).

17. Duckett et al (2020, p. 45).

18. A 'hardship' payment for casual workers in Queensland was introduced in June to support people who are unable to work due to isolation: Palaszczuk and Fentiman (2020). This has been identified as a key issue for safely opening businesses in NSW: Cavanough (2020).

19. Duckett et al (2020, pp. 43–44).

20. Lunn et al (2020).



The transition from lockdown to a new normal will take some months to stabilise, as new information emerges from experience. As structural measures to manage infection are put in place, new patterns of personal behaviour are likely to follow. It will be important that there is an effective communication campaign to support, encourage, and reinforce these changes.

Testing, contact tracing and isolation, and a graduated lifting of lockdown restrictions are likely to maintain a low rate of infection in Australia for an extended period – given how effective restrictions were when first imposed. But with low rates of infection and low perceptions of risk, social distancing and hygiene measures are less likely to be maintained. It is therefore important, while there are active COVID-19 cases in any state, that structural measures to control rates of infection over the longer term are put in place.

Even then, it is likely there will still be outbreaks and clusters. The capacity and effectiveness of testing and contact tracing will be critical to prevent wider spread and a return to exponential growth.

### 2.3.3 Growth: during a second wave

If COVID-19 escapes quarantine under an elimination scenario, or overwhelms the track-and-trace system under a suppression scenario, then governments need to have enough restrictions in place that infections do not grow rapidly in a ‘second wave’. The risk of a second wave – and the economic damage created by *fear* of a second wave<sup>21</sup> – is higher if policies and behaviour return to normal too soon.

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21. Even before restrictions came into effect in March, people were starting to avoid shops and public transport: Grattan Econ Tracker (2020). In Sweden, where there was no lockdown, public fear of the virus inflicted almost as much economic damage as in neighbouring Denmark with a much tighter lockdown: N. Smith (2020).

State and territory governments must monitor cases in local areas. They must be prepared to act decisively to control major outbreaks. Exactly how they will act in the case of a major outbreak must be determined in advance by the relevant public health authority, and should be communicated clearly with the public before outbreaks occur.

If frequent testing discovers an outbreak that may overwhelm contact tracing efforts, local lockdowns should be considered.<sup>22</sup> The mechanics – the threshold of cases for a lockdown, who can enter and exit the affected area, what happens to workplaces and schools – must be communicated with the public in advance of outbreaks occurring. This will ensure the public and local authorities know what to expect and how to react. It will also remind the public of the risks of COVID-19 spread: if it remains, and if there is an outbreak, lockdowns will have to return.

If these local measures fail, then the virus is likely to spread quickly if workplaces, major events, and state borders have already been reopened. If the virus begins to spread throughout a wider area, state and territory governments must reintroduce at least some of their lockdown restrictions to suppress infections.

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22. These types of localised lockdowns have been used in China when substantial outbreaks have been discovered. After a cluster of cases was detected, linked to a market in a Beijing district, lockdown measures were put in place for the neighbourhoods surrounding the market: Hua and Cadell (2020).

### 3 Managing the economy in transition

The economic fallout from the coronavirus crisis has been sharp and swift. Social distancing measures 'brick walled' key parts of the economy – tourism, international education, recreation, and much of retail and hospitality – largely shutting them down almost overnight. The second-round effects from lower incomes and greater uncertainty continue to ricochet around the economy.

The speed of this shock was unprecedented, as was the government response. Federal and state governments have unleashed major fiscal and monetary policy responses to support the economy and incomes during the shutdown.

But as the economy gradually re-opens, new economic challenges will emerge. The risk of renewed outbreaks means a smooth re-opening of the economy is far from assured. A globally synchronised recession, continuing consumer and business uncertainty, debt overhang for businesses and households, and a significant hit to population growth will all drag on economic activity in the next year and possibly beyond.

In the short-term, there has been an initial burst of activity as restrictions ease, supported by extensive government payments. But an abrupt withdrawal of government support in a few months' time would magnify the economic risks. If all, or even most, government emergency supports are withdrawn simultaneously in October, it will leave a substantial hole in incomes for households and businesses, and threaten the economic recovery. The Federal Government needs to phase-out JobKeeper and other supports more gradually. This will cost about \$30 billion in 2020-21.

Without further stimulus, unemployment will remain too high and the economy will grow more slowly than it could for many years. The

Reserve Bank should use the tools at its disposal to further stimulate economic activity, although there are limits to how much it can help.

Governments should start planning for sizeable fiscal stimulus to support the economy beyond October and into next year. The recovery would be aided by ongoing reforms such as increases to JobSeeker, Rent Assistance, and childcare that would cost at least \$21 billion over the next two years. If governments want to get unemployment back down to 5 per cent or below by mid-2022 then they will need to be prepared to spend another \$20-to-\$40 billion on services, infrastructure, and social housing.

Both federal and state governments will emerge from this crisis with a lot more debt than pre-pandemic. But they should not risk the economic recovery by moving too fast to consolidate their budget positions. Interest rates are at record lows and the debt position is manageable.

Governments can keep debt contained in the medium term by pursuing reforms to boost economic growth and by running tighter budgets after the economy has recovered. Governments should not rely on bracket creep, increasing inefficient taxes, or welfare cuts to do the heavy lifting on budget repair. If they do, the young and the vulnerable will pay twice: first with their job during the shutdown, and second with a higher tax burden, slower growth, and a weaker safety net.

Over time governments may need to reassess the appropriateness of their traditional anchors for macroeconomic policy. The Reserve Bank's inflation targeting framework and the government's medium-term fiscal strategy to achieve budget surpluses on average over the course of the economic cycle may no longer be fit for purpose.

### 3.1 The economic shock from COVID-19 has been sharp and swift

Australia is in the midst of a deep recession. The economy went backwards in the March quarter,<sup>23</sup> hit first by the summer bushfires and then by social distancing and travel restrictions in the final weeks of March. A much sharper contraction is expected for the June quarter, and Reserve Bank forecasts suggest the Australian economy could shrink by 5 per cent in 2020.<sup>24</sup>

The shock hit at unprecedented speed. Social distancing rules forced businesses across a range of sectors to close their doors virtually overnight. This sudden halt to activity across key parts of the economy is unique to this recession.

#### 3.1.1 Many Australian workers have lost their livelihoods

Many Australians were thrown out of work in a matter of weeks because of the COVID-19 crisis. The official unemployment rate rose from 5.2 per cent in March to 7.1 per cent in May. The true employment hit is much larger. The ABS has stated that if all ‘stood down’ workers were counted as ‘unemployed’, the unemployment rate would have been 11.3 per cent in May.<sup>25</sup>

The number of people with a job fell by 600,000 in April alone, and a further 230,000 in May – more than the total decline in employment in the 1980s and 1990s recessions.<sup>26</sup> Another 360,000 people still had a job but didn’t work any hours in May. Many of these people are likely

to be receiving the Federal Government’s JobKeeper wage subsidy (Section 3.2 on page 18).<sup>27</sup> And another 1.2 million people did *some* work but had fewer hours than usual. All up, that makes about 2.3 million people (almost 20 per cent of the labour force) who lost their job or lost hours in just a few weeks.

Younger people have been hit particularly hard. Youth unemployment rose to 16.1 per cent in May, up from 11.6 per cent in March. On top of that, more than 20 per cent of Australian workers aged 15-24 are underemployed, meaning they would like more hours of work. In contrast, unemployment among Australians aged 45+ barely moved between March and May (Figure 3.1 on the next page).

#### 3.1.2 Weak demand continues to bite

Job and income losses combined with significant uncertainty have hurt demand across the economy.

Consumer confidence fell to a record low in March, before recovering to near pre-pandemic levels by June.<sup>28</sup> Consumers kept their money in their pockets, with total spending down 1.1 per cent in the March quarter, but spending on discretionary goods and services down 3.9 per cent. The household savings ratio increased sharply to 5.5 per cent of disposable income, as people took the precaution of saving more or simply weren’t able to spend because of restrictions on going out.<sup>29</sup> Unprecedented emergency supports, especially JobKeeper and higher

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23. A 0.3 per cent quarterly decline in real GDP: ABS (2020a).

24. Year-average for 2020. The peak-to-trough decline in GDP is expected to be about 10 per cent, mostly concentrated in the June quarter: RBA (2020a).

25. ABS (2020b).

26. In the 1980s recession, about 235,000 people lost their job over 15 months. In the 1990s recession, about 330,000 people lost their job over 2.5 years: ABS (2020c, Table 1).

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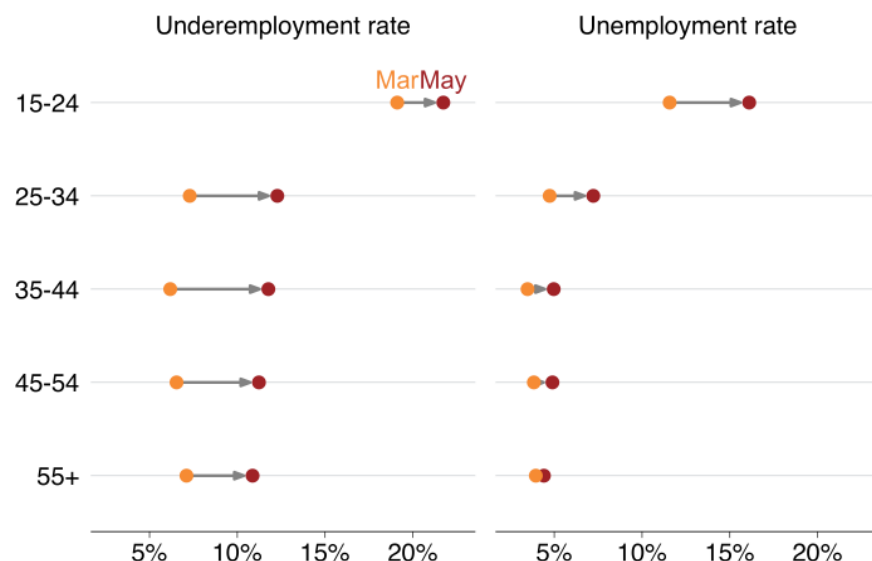
27. Cowgill and Coates (2020).

28. ANZ-Roy Morgan (2020). The survey has been taken for nearly 50 years. See also: Grattan Econ Tracker (2020).

29. ABS (2020a). Some of the extra savings are likely to be spent due to pent up demand once social distancing regulations are wound back. However, aggregate demand is likely to be deficient for some time to come.

**Figure 3.1: Younger people have been hit hardest by the shutdowns**

Underemployment and unemployment, per cent of labour force



Source: ABS (2020d).

JobSeeker payments, helped spending recover from April to June, but consumer spending still remains below pre-crisis levels.<sup>30</sup>

In most sectors – including very large ones such as education, manufacturing, healthcare, and construction – more than half of businesses have suffered a reduction in demand as a result of the crisis (Figure 3.2).

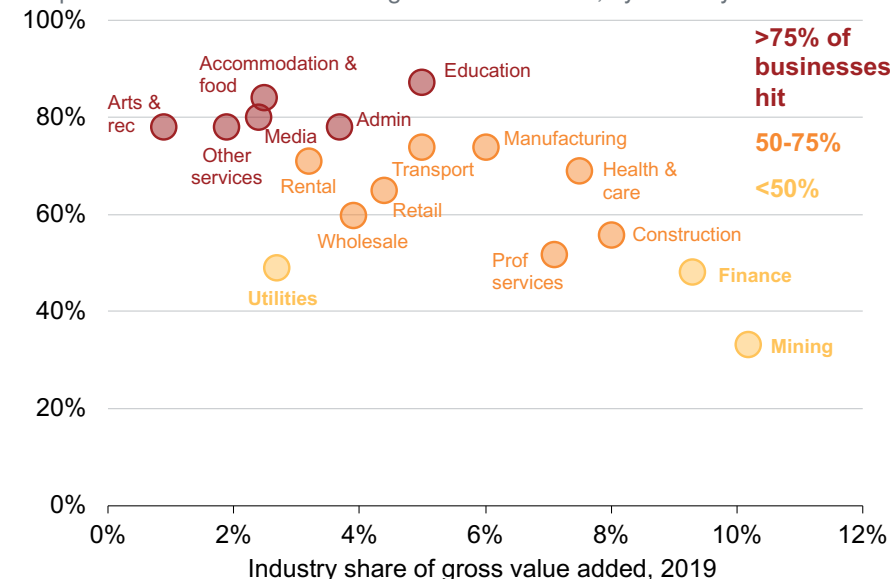
In these difficult trading conditions, business confidence fell to record lows in March and April, but recovered slightly in May.<sup>31</sup> The outlook

30. According to AlphaBeta (2020), spending was still 3-to-5 per cent below pre-crisis levels in mid-June.

31. NAB (2020). See also: Grattan Econ Tracker (2020).

**Figure 3.2: The demand shock has hit all sectors of the economy**

Proportion of businesses suffering reduced revenue, by industry



Notes: The ABS surveyed businesses between 10 June and 17 June 2020 on the impacts of COVID-19. Changes in revenue are compared to the same time last year.

Source: Grattan analysis of ABS (2019a) and ABS (2020e).

for business investment remains weak. Investment went backwards in the March quarter, and businesses expect their capital investments to decline further in coming months.<sup>32</sup> Construction activity on existing projects has so far held up, but the pipeline of future projects is drying up.<sup>33</sup>

Challenges for businesses, including cashflow problems, are discussed in more detail in Chapter 4.

32. ABS (2020f).

33. RBA (2020a); and ABS (2020f).

### 3.2 Governments responded quickly to help businesses and households survive the shutdown

Governments responded to these challenges with announcements of more than \$160 billion of extra spending, which has largely insulated households from the economic pain. Financial instability has been prevented – for now.

#### 3.2.1 The government response has been large

Over the past three months, the Federal Government has announced an unprecedented fiscal injection of \$136 billion (about 7 per cent of GDP) to support businesses and households through the COVID-19 shutdown.<sup>34</sup> This amounts to more than \$5,300 per Australian, on par with responses in other developed nations (Figure 3.3).

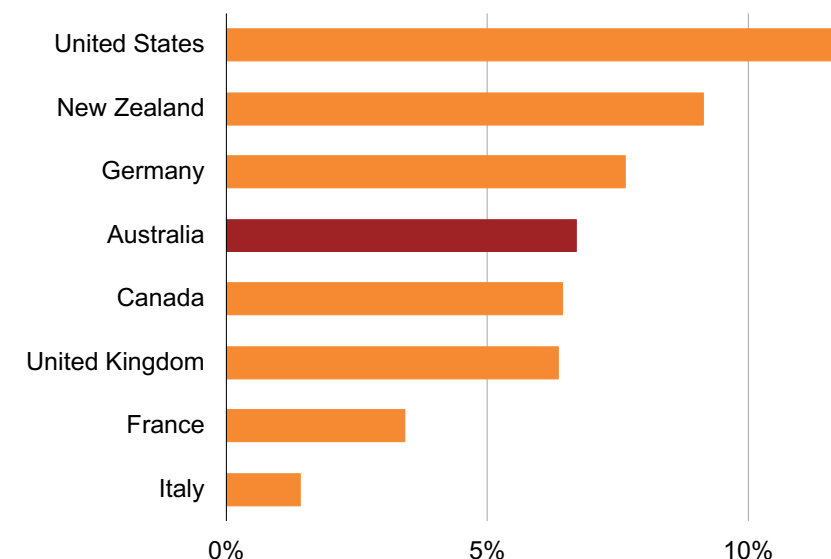
The speed of the response was also unprecedented. The Government announced its first response package on 12 March – less than seven weeks after Australia’s first coronavirus case. Following that announcement, one-off payments of \$750 were paid in a little over a month. During the government’s response to the Global Financial Crisis, comparable payments took 55 days to land in people’s bank accounts. Getting the money out the door quickly meant the Government gave priority to speed over design perfection. This was the right choice in the circumstances, but there now need to be improvements to the design of key programs (see Chapter 4).

The single largest component of the Government’s fiscal response is the JobKeeper wage subsidy program, which provides support to workers via their employers, at a cost of \$70 billion over six months. This critical support helps keep workers and employers connected through the crisis – reducing the likelihood that people are stood down without pay or dismissed entirely (see Chapter 4).

34. Not including \$3.5 billion in federal support for the health system: D. Wood et al (2020c).

**Figure 3.3: Australia’s fiscal response is comparable to other developed nations**

Fiscal measures in response to the COVID-19 shutdown as a per cent of pre-crisis GDP



*Notes: Excludes monetary policy, loans without forgiveness, guarantees, and direct state holdings. We calculate the ratio of the 2020 measures to 2019 GDP because of uncertainty in the 2020 forecast. The chart assumes that all coronavirus stimulus spending occurs within the current year; this is a close approximation given that almost all the packages announced to date concentrate on responding to the immediate economic fallout from the crisis. The standing of the United States is higher here than in some other reporting because we include the Paycheck Protection Program (while it is a loan, the program is designed to forgive the debt at conclusion). JobKeeper was originally announced as a \$130 billion program, which would have made Australia’s fiscal response the second-largest among developed nations, see D. Wood et al (2020a).*

*Sources: Spending from various government sources, GDP from IMF and [exchangerates.org.uk](https://www.exchangerates.org.uk).*



A further \$39 billion has been budgeted for other business measures,<sup>35</sup> \$26 billion in household stimulus and support,<sup>36</sup> and just over \$1 billion in community and local government support<sup>37</sup> (see Figure 3.4 on the following page). Household resources have been further boosted as about 2 million Australians have withdrawn \$16 billion through the superannuation early-release scheme.<sup>38</sup>

Every state and territory government in Australia has also announced a spending response to the COVID-19 crisis. These measures – including loans, tax deferrals, and health spending – so far total almost \$25 billion (Figure 3.5 on the next page).<sup>39</sup> That puts the collective commitments of Australian governments at over \$160 billion.

Meanwhile the Reserve Bank has reduced the cash rate to 0.25 per cent and commenced unconventional monetary policies, such as yield curve control, to ensure interest rates remain low for the duration of the crisis.<sup>40</sup> The Reserve Bank has also established a term fund facility to support credit to businesses, especially small and medium-sized businesses.<sup>41</sup> Despite these steps, inflation is expected to remain well below the Bank's target, and therefore it may be appropriate to further loosen monetary policy (see Section 3.5.3).

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35. Including boosting cash flow for employers (\$32 billion) and accelerated depreciation deductions (\$3 billion), among other measures.

36. Including the Coronavirus Supplement for JobSeeker recipients (\$14 billion) and the \$750 stimulus payments (\$9 billion).

37. Including the Local Road and Community Infrastructure Program (\$500 million).

38. As of early June, APRA (2020a).

39. As at 12 June, see also D. Wood et al (2020b).

40. Yield curve control involves the central bank outright purchasing assets from the private sector by creating 'central bank reserves'. The Reserve Bank is purchasing Australian Government bonds on the secondary market with a target yield of 0.25 per cent on three-year bonds. It expects the target 'to remain in place until progress is being made towards the goals for full employment and inflation': RBA (2020a).

41. Under this facility, banks can borrow at least \$90 billion at a fixed interest rate of just 0.25 per cent, for lending to businesses: P. Lowe (2020a).

### 3.2.2 Governments have insulated many Australian households from the economic pain caused by COVID-19

JobKeeper and the temporary doubling of JobSeeker have gone a long way to insulating Australians – particularly low- and middle-income households – from the economic costs of COVID-19.<sup>42</sup>

The JobKeeper wage subsidy covers about 70 per cent of the typical wage in Australia and about half the typical full-time wage (Figure 3.6 on page 21).<sup>43</sup> Many part-time minimum-wage workers and eligible casuals have actually received a pay rise under the scheme.<sup>44</sup>

For unemployed Australians, the JobSeeker payment is currently paying about half of median earnings,<sup>45</sup> well above the previous unemployment benefit known as Newstart (see Figure 3.6).

For people on higher incomes who have been stood down – for example, any of the 20 per cent of Australian workers who earn more than \$115,000 a year – the JobKeeper payment replaces one-third or less of their normal earnings.<sup>46</sup> These families will be relying more on their savings, reduced spending, and early access to superannuation (see Box 1 on page 22) to get through the crisis.<sup>47</sup> Those with a mortgage may have delayed payments to their bank, but high-income

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42. Workers who are now on JobKeeper or JobSeeker will also receive tax refunds come July, and workers with children will become eligible for greater Family Tax Benefit. Many renters will also qualify for Commonwealth Rent Assistance.

43. The JobKeeper payment is about \$39,000 a year, compared to the median wage of about \$58,000 a year and median full-time wage of about \$78,000: see Coates and Cowgill (2020a).

44. Cassells and Duncan (2020) estimate that about 80 per cent of part-time workers are receiving more than they were previously paid.

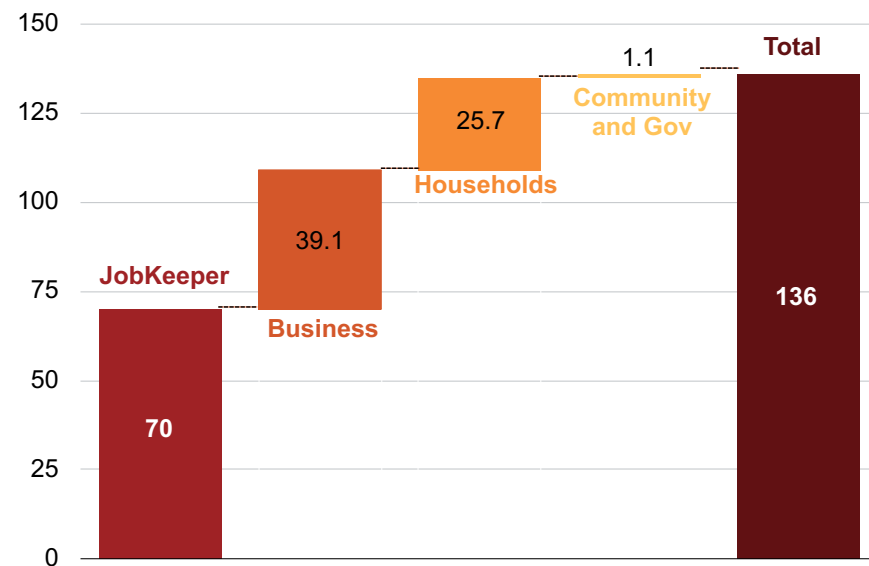
45. About \$29,000 a year, including the temporary Coronavirus Supplement.

46. Coates and Cowgill (2020a).

47. While many higher-income Australians have substantial savings (and can now withdraw up to \$20,000 from their superannuation), others don't. About 40 per cent of the highest fifth of income earners had less than 4 weeks' income in the bank at the beginning of COVID-19 shutdowns: Coates and Cowgill (2020b).

**Figure 3.4: JobKeeper dominates the Government's fiscal response**

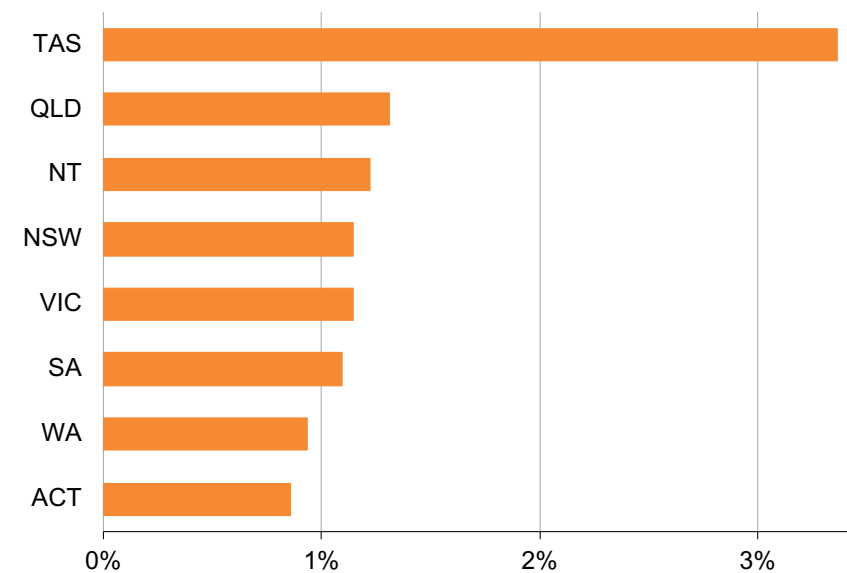
Total fiscal response by target, \$ billions



Source: Grattan analysis of government announcements.

**Figure 3.5: Fiscal measures in most states exceed 1 per cent of economic output**

Fiscal measures in response to COVID-19 as a percentage of pre-crisis GSP



Source: Grattan analysis of government announcements.

renters may have to make big changes to their lifestyles to make it through to Christmas.<sup>48</sup>

Given the scale of fiscal support, many households have more income than before the crisis, and there are signs that they are starting to spend it as restrictions are lifted.<sup>49</sup> But spending is likely to tighten up again when support programs are wound back (Section 3.3).

### 3.2.3 Policy makers have prevented financial instability for now

The speed and size of the economic hit raised early concerns about financial instability, because of the risks of widespread loan defaults and a seizure of credit, as witnessed during the Global Financial Crisis.

But policy makers moved quickly to reduce these risks. The shift to unconventional monetary policy in late March – by targeting the yield on three-year government bonds – as well as the introduction of a term credit facility for the banking sector and measures to support liquidity have becalmed financial markets.<sup>50</sup> Deferrals on mortgage repayments (‘holidays’) offered by the banks, hardship provisions for energy bills, early access to superannuation, and JobKeeper and JobSeeker payments, have forestalled large increases in arrears, at least for now.<sup>51</sup>

These actions have settled financial markets for the time being. Economic uncertainty was very high in March but is now much lower, albeit still above pre-COVID levels.<sup>52</sup>

48. Most people’s financial commitments – especially rent and mortgage repayments – match what they earn: ABS (2019c).

49. Clifton (2020) shows that total credit card spending is now back above pre-crisis levels, although such trends are inflated by the switch away from cash transactions and towards spending via electronic means since the onset of COVID-19.

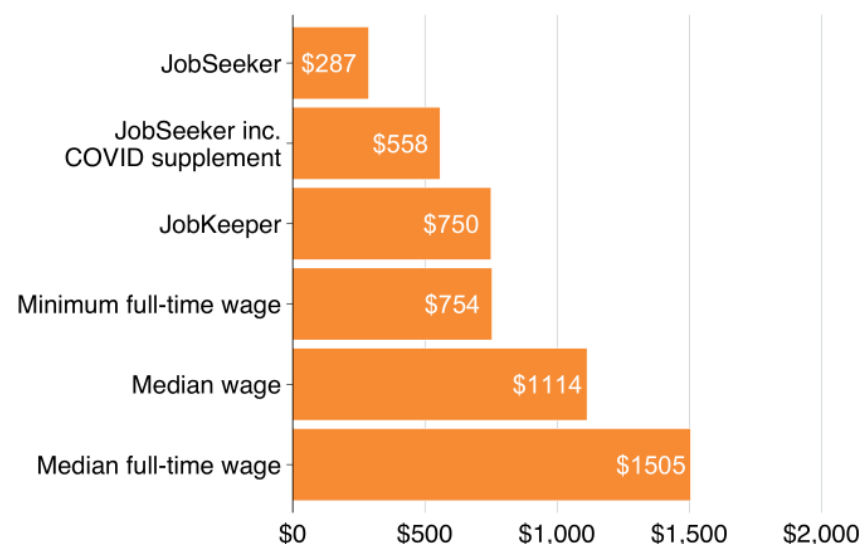
50. RBA (2020a).

51. RBA (2020b).

52. For example, the S&P/ASX 200 VIX, commonly referred to as the ‘investor fear gauge’, hit its highest level in 10 years on 18 March. See Chen and Coates

**Figure 3.6: JobKeeper largely insulates low- and middle-income earners from the economic costs of COVID-19**

Weekly maximum payment



Notes: Income support payment rates are for singles without children. JobSeeker includes Energy Supplement. Median wages are for people aged 15+. Minimum wage is for people aged 21+. All values are pre-tax.

Sources: Morrison (2020a), Services Australia (n.d.) and DSS (2020a). Median wages data from Coates and Cowgill (2020a) analysis of ABS (2019b).

### 3.3 But there are many economic risks in the recovery phase

The re-opening of businesses does not mean the economy is out of the woods.

A second wave of the virus<sup>53</sup> (see Chapter 2) could derail the economic recovery. The OECD estimates that a second wave would stall real GDP growth in 2021 at 1.0 per cent, compared to 4.1 per cent under a single wave scenario.<sup>54</sup> Treasury estimates that reimposing restrictions would cost the economy more than \$4 billion a week.<sup>55</sup> The hit to consumer and business confidence could be even more significant.<sup>56</sup> Victoria has already had to re-impose some restrictions in response to an increase in local transmissions.

But even if things go to plan, and we see an initial bounce-back, big parts of the economy are still likely to be sluggish for some time yet. Even as restrictions are lifted, Australia is likely to find itself in a ‘conventional’ recession, with insufficient aggregate demand.<sup>57</sup> In past recessions it has taken years for employment to bounce back (Figure 3.7 on the following page).<sup>58</sup> Jobs growth is likely to be rapid in the initial phase of recovery, but is expected to slow after this initial burst.

Most of the world has not fared as well as Australia in limiting deaths and the spread of the virus. Other countries were forced to impose far-stricter lockdowns with much larger economic costs. While many countries are now lifting those restrictions, the rate of new COVID-19

(2020). Australian money market and corporate bond spreads have also returned to more normal levels: RBA (2020a).

53. Or even just the fear of it: N. Smith (2020).

54. OECD (2020a).

55. Frydenberg (2020).

56. Deloitte (2020).

57. Economists have shown how supply shocks can result in large shocks to demand: Guerrieri et al (2020).

58. Coates et al (2020a).

#### Box 1: The superannuation early release scheme should be revised before the second tranche is released

The Government’s early release scheme allows eligible Australians to take up to \$20,000 from their super accounts – \$10,000 this year and another \$10,000 next year.<sup>a</sup> About 2 million Australians have withdrawn \$15.9 billion through the scheme.<sup>b</sup>

The scheme has helped many Australians to manage the income hit due to COVID-19, while also providing an important boost to aggregate spending. Spending data suggests about one-third of the money was spent within the first fortnight, mostly on discretionary purchases.<sup>c</sup>

Most individuals who remove \$20,000 from their superannuation accounts can still look forward to a comfortable retirement, even if investment returns are lower over the coming decades.<sup>d</sup>

But there are concerns that as many as 40 per cent of people dipping into their super did not actually suffer a drop in income.<sup>e</sup> Withdrawals are currently approved based on a declaration from the applicant; there is no independent verification by the ATO.<sup>f</sup>

The Commonwealth Government should therefore revise the scheme before the second tranche of withdrawals, to require applicants to demonstrate they meet the eligibility criteria before the money is released.

a. Applicants are eligible provided they are unemployed, are eligible for JobSeeker or similar payments, or suffered a 20 per cent reduction in working hours or sole trader turnover: ATO (2020a).

b. As of early June: APRA (2020a).

c. M. Wade (2020). Less may have been spent because many households received JobKeeper and JobSeeker at about the same time.

d. Coates and Nolan (2020, p. 62).

e. M. Wade (2020).

f. Although breaching these rules does carry a penalty: Roddan (2020).

cases remains higher than in Australia, and therefore consumers are cautious. All this means global economic activity and demand will be weak for some time. In June the World Bank forecast that global growth will shrink by 5.2 per cent in 2020, and 7 per cent among advanced nations.<sup>59</sup> Such a decline would make this the worst recession since the Great Depression (global economic output fell by just 0.1 per cent in 2009 after the Global Financial Crisis).<sup>60</sup>

The World Bank predicts a moderate recovery of 4.2 per cent in 2021, but expects that global output will not return to previously-expected levels.<sup>61</sup> With exports accounting for more than 20 per cent of Australia's GDP,<sup>62</sup> sluggish global growth will drag on our economic recovery.<sup>63</sup> The one bright spot may be commodity exports, especially iron ore. If the Chinese government continues to invest heavily in infrastructure to support their economic recovery, commodity prices and volumes will recover more quickly than otherwise.<sup>64</sup>

59. World Bank (2020). The OECD forecasts a global decline of 7.6 per cent, and the IMF forecast a global decline of 4.9 per cent in 2020 with 8.0 per cent decline in advanced economies: OECD (2020b) and IMF (2020a). Previous Grattan work has criticised the IMF for assuming a 'V-shaped' recovery: D. Wood and Coates (2020).

60. Gopinath (2020).

61. World Bank (2020). The IMF is more optimistic, predicting 5.4 per cent global growth in 2021: IMF (2020a). The OECD considers two scenarios – 5.2 per cent global growth for 2021 in a 'single hit' scenario, and 2.8 per cent in a 'double hit' scenario where a second wave of infections hits before the end of 2020: OECD (2020b).

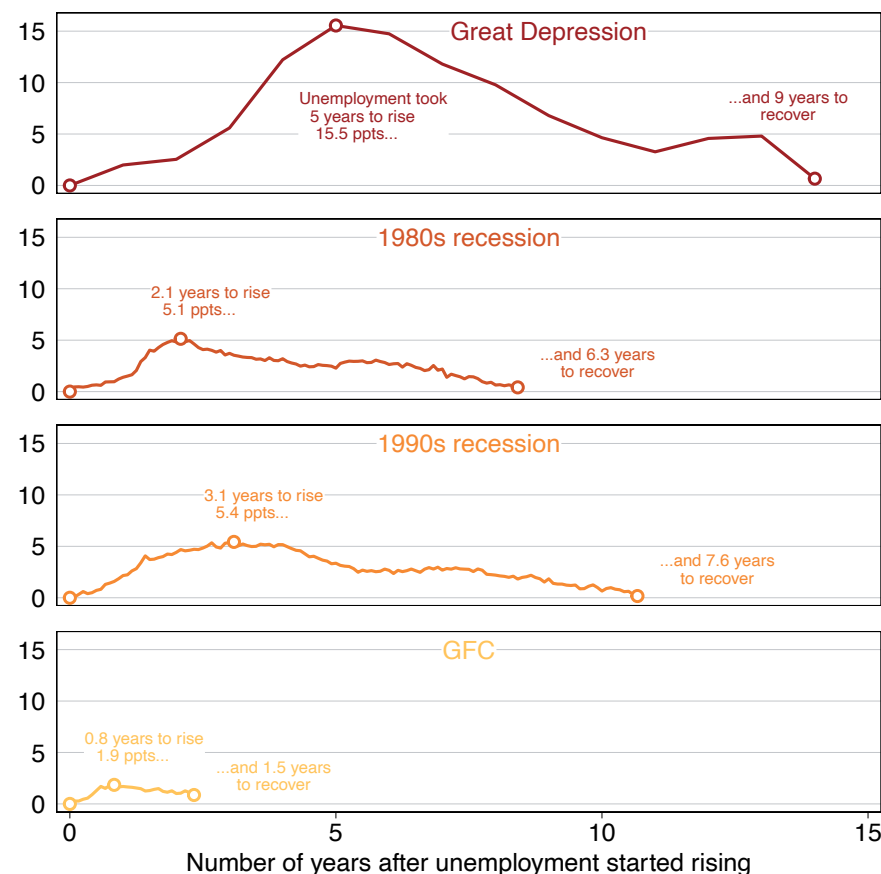
62. Australia's exports reached nearly \$470 billion in 2018-19, equivalent to 24.1 per cent of GDP: ABS (2019d).

63. Although weak imports (from weak domestic demand) will show up as a positive contribution to GDP in accounting terms.

64. China's fiscal stimulus has been more muted than other large economies, at about 5 per cent of GDP, and credit easing has been far smaller than after the GFC in 2009-10: Fitch Ratings (2020). However, other major exporters of commodities, such as Brazil and South Africa, have suffered supply disruptions due to COVID-19 Smyth and Hume (2020).

**Figure 3.7: Unemployment rises quickly in recessions, but takes a long time to come down**

Rise in the unemployment rate (percentage points)



Notes: Data are annual for the Great Depression. Data for the other episodes are seasonally adjusted monthly data. After the GFC, the unemployment rate did not fully recover to its pre-crisis low before beginning to rise again.

Sources: Butlin (1977) and ABS (2020d).



Businesses and consumers are likely to be cautious, even if restrictions are lifted. Investment and discretionary spending may take longer to come back. Much of China has been free of most government restrictions for months. Business activity there has largely returned to pre-COVID-19 levels. But consumer activity generally remains at only about 90 per cent of pre-COVID-19 levels, and it is drifting up only slowly.<sup>65</sup>

This will be compounded in Australia by the ‘debt overhang’ – many households and businesses deferred loans and rental repayments during the shutdown. At least \$234 billion in loans have been deferred, according to the Australian Banking Association in June, mostly mortgages.<sup>66</sup> As these deferral schemes come off, starting from October, higher outgoings to cover the capitalised loan interest and missed rental repayments will mean softer household and business spending. Some borrowers will be unable to service their loans long-term, with business lending to sectors such as retail and hospitality, as well as commercial property, key areas for concern.<sup>67</sup> Australia’s already-high level of household debt exacerbates these risks.<sup>68</sup>

Finally, construction and overall economic activity is expected to be hit by a decline in population growth. High population growth through high immigration has supported economic activity, particularly housing construction,<sup>69</sup> in Australia for the past seven years.<sup>70</sup> But this year population growth will slow sharply because of the outflow of temporary

migrants.<sup>71</sup> International borders are unlikely to be reopened for some time (Chapter 2), and even when borders are reopened, history suggests that migration tends to be subdued when economic activity is weak<sup>72</sup> – people don’t get on planes if there are no jobs at the other end.<sup>73</sup>

### 3.4 Government missteps could scupper the recovery

With weak underlying demand, slow growth in the rest of the world, a household and business debt overhang, and slow population growth, Australia’s economy is fragile. Governments could make it worse by withdrawing government spending too fast, and proceeding with the planned increase in the superannuation guarantee, which would leave an enormous hole in economic activity and business and household incomes.

#### 3.4.1 Withdrawing government supports quickly risks a second downturn

The major government fiscal supports – including the JobKeeper program and regulatory supports for businesses and households – are all scheduled to come off by the end of October (Figure 3.8 on the next page). Under current arrangements, Australia faces a ‘fiscal cliff’ as the additional \$14 billion per month (almost 9 per cent of GDP) in emergency income support through JobKeeper and the higher rate of JobSeeker are almost simultaneously cut off.

Turning off the tap could leave many households struggling to pay their bills (Chapter 5) and many of the businesses in slow-to-recover sectors,

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65. RBA (2020c).

66. One in 14 mortgage holders have had their repayments deferred: van Onselen (2020), see also Crowe (2020). Deferred mortgages account for just under 10 per cent of all housing loans by value, as measured by APRA (2020b).

67. Banks are setting aside capital, see Evers et al (2020).

68. Daley et al (2017).

69. Daley et al (2018a).

70. Colebatch (2019).

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71. Rizvi (2020).

72. Terrill et al (2018); and Rizvi (2020).

73. History suggests that *relative* economic performance will be an important driver of migration; even if unemployment is elevated in Australia, people may wish to move here if our economic performance is better than elsewhere. A similar dynamic occurred during the GFC.

such as tourism and hospitality, unable to survive (Chapter 4). It would also put a hand-brake on the recovery as households anticipate the income shock by saving, and businesses try to minimise avoidable costs by holding back on employing workers.

Household saving will help moderate the ‘cliff’ a little, because consumers will spend some of the additional support beyond September.<sup>74</sup> But they are a long way from perfect income smoothing and the shock to spending will still be significant.

The IMF has warned against sudden withdrawal of wage subsidy schemes like JobKeeper, recommending that the exit from such schemes ‘should proceed gradually to avoid precipitating sudden income losses and bankruptcies just as the economy is beginning to regain its footing.’<sup>75</sup>

A strong recovery will require a slower transition off these payments. Specific recommendations to do so are outlined in Chapter 4 and Chapter 5.

Fiscal stimulus and strong monetary policy supports will also be needed to support economic activity in this ‘danger zone’, and for the months and years beyond.

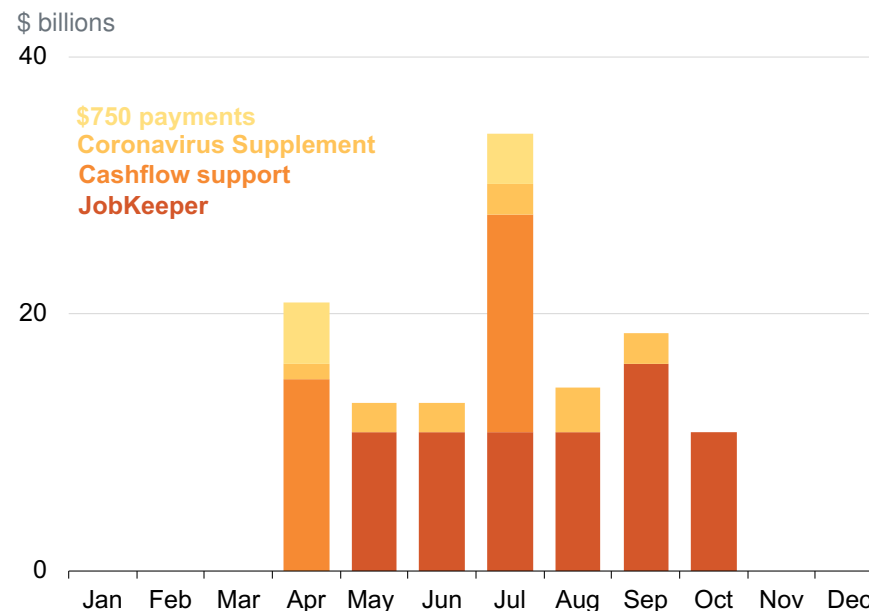
### 3.4.2 Increasing compulsory superannuation would further dampen spending

Legislated plans to increase the rate of compulsory superannuation contributions incrementally to 12 per cent of wages between 2021 and July 2025 would also exacerbate the economic problems caused by COVID-19, and should be abandoned.

74. Commins (2020).

75. IMF (2020a, p. 11).

**Figure 3.8: Major fiscal supports are all scheduled to come off in October**



Notes: Amounts reflect payment timing. JobKeeper runs from late March to late September but is paid in arrears.

Source: Grattan analysis of government announcements.

At least 80 per cent of the cost of higher compulsory super contributions comes at the cost of lower wages for workers, typically within two-to-three years.<sup>76</sup> Consequently, any increase in the Superannuation Guarantee will result in reduced consumer spending. As noted in Section 3.1.2, household saving has already spiked sharply in response to COVID-19, and consumers and firms are likely to remain cautious in the months and years ahead.<sup>77</sup>

And the policy justification for increasing the Superannuation Guarantee is weak anyway. The vast bulk of retired Australians have an adequate income and feel financially comfortable, and the vast bulk of working-age Australians can already look forward to a standard of living in retirement at least the equal of their standard of living while working.<sup>78</sup> Increasing the Super Guarantee as planned would effectively compel most people to save for a higher living standard in retirement than they enjoy in their working lives. It will do little to boost the retirement incomes of middle-income earners, while draining government tax revenues.<sup>79</sup>

The cost of tax breaks on higher compulsory contributions – growing to an extra \$2 billion a year by 2025 – would be better spent providing stimulus to the economy, and funding permanent increases in JobSeeker and Rent Assistance.

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76. Coates et al (2020b). Our finding is conservative: it ignores the prospect that employers pass on some of the cost of super into higher prices, or by reducing other non-wage benefits to workers.

77. The seasonally adjusted household savings ratio rose during the GFC from 0.8 per cent in March 2007 to a peak of 10.9 per cent in December 2008: ABS (2020g).

78. Coates and Nolan (2020).

79. Coates and Nolan (ibid).

### 3.5 Governments need to do more to boost the economy

The priority for Australian governments must be to do more to boost the economy over the next 6-to-12 months.

The size and scale of the required fiscal and monetary response are discussed in the remainder of this chapter. In subsequent chapters we discuss the best way to execute key elements of this response, particularly phasing out JobKeeper more slowly (Chapter 4), supporting household demand during the transition, and strengthening the safety net (Chapter 5).

#### 3.5.1 Further fiscal and monetary stimulus is needed to support the economic recovery

Fiscal and monetary policy should aim to restore economic activity to its potential level over the next 18 months to two years. This will involve reducing unemployment to its lowest sustainable level, and restoring inflation and inflation expectations to at least 2.5 per cent.<sup>80</sup> Without fiscal and monetary stimulus, aggregate demand is highly unlikely to be sufficient to achieve these goals.

Official forecasts anticipate substantial slack in the labour market through to the end of 2021 and beyond. In its baseline scenario, the Reserve Bank forecasts unemployment to peak at about 10 per cent by June 2020, before falling to 9 per cent by December 2020, 8.5 per cent by June 2021, and 7.5 per cent by December 2021.<sup>81</sup> In its more optimistic scenario, unemployment is forecast to decline to 6.5 per

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80. A period of inflation in the upper half of the target band – or even slightly above the target band – is required to hit the target of *average* inflation between 2 and 3 per cent. See Section 3.5.3 on page 33.

81. RBA (2020a). These forecasts are based on current levels of government spending, including JobKeeper remaining in place until September as announced.

cent by June 2021 and remain at 5.7 per cent by December 2021.<sup>82</sup> In contrast, the OECD expects unemployment to rise from an average of 7.4 per cent over 2021 to 7.6 per cent over 2021.<sup>83</sup>

Unemployment has long-lasting effects for people directly affected by it. People who suffer unemployment can be ‘scarred’ by the experience, particularly if they’re out of work for a long time – their skills erode, their experience becomes less relevant, they lose touch with professional networks, and become less attractive to employers.<sup>84</sup> Young people who graduate during recessions also suffer long-term consequences, with worse average labour market outcomes over their lifetimes than cohorts that graduate into booming labour markets.<sup>85</sup>

Sustained periods of high unemployment also have long-lasting effects on the economy as a whole. There is now considerable evidence that recessions reduce the productive capacity of the economy in the long term.<sup>86</sup> Recessions are not just cyclical deviations from a stable long-run growth path – recessions themselves can affect the long-run growth path. Other things equal, a higher unemployment rate in 2021 is likely

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82. More recent statements from Reserve Bank Governor Philip Lowe and Treasury Secretary Steven Kennedy suggest more optimism about the pace of economic recovery post-COVID, such that the RBA’s optimistic scenario is more likely. P. Lowe (2020b). Treasury now expects unemployment to reach 8 per cent in September, rather than 10 per cent as previously forecast: Wright and Powell (2020).

83. OECD (2020a).

84. There is an extensive literature on this; see for example: Arulampalam et al (2001) and Rothstein (2019).

85. International studies of scarring commonly find that entering the labour market at a time when the rate of unemployment is 3-to-4 percentage points above average causes a decrease in annual earnings from 3-to-6 per cent per year for a decade: Borland (2020a). In Australia, a study comparing pre- and post-GFC cohorts of young Australians found that even among those who found employment, the post-GFC cohort had less job security, fewer hours of work, and lower earnings: Watson (2018).

86. See a recent review of the evidence in Cerra et al (2020).

to mean a higher unemployment rate a decade from now, when the COVID-19 crisis has (presumably) long passed, than would otherwise have been the case.<sup>87</sup> Stimulus alone cannot reverse damage done to the economy’s productive capacity by the virus itself. But stimulus can prevent the additional long-run damage that would be done to the economy’s potential by a long recession.

Fiscal and monetary policy can and should aim to boost aggregate demand to restore economic activity to its potential level. There is always substantial uncertainty about the level of potential output, and the level of unemployment that corresponds to full employment. These things are even less certain in the current crisis. Nonetheless policymakers should aim to bring unemployment down to 4-to-5 per cent – the level typically recognised as being required to trigger faster growth in wages.<sup>88</sup> Unless and until wages and prices begin rising at a more rapid pace we can be confident that the economy still has unused capacity.<sup>89</sup>

Fiscal and monetary policy operates with a lag: it takes months, and sometimes years, for the full effects of policy changes to pass through

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87. Fatas and L. H. Summers (2015) found that every 1 per cent reduction in GDP brought on by tight fiscal policy translated into a 1 per cent decline in potential output five years later. Ball (2014) similarly found that countries with deeper downturns after the GFC suffered bigger falls in long-run potential output. Yagan (2019) found that each extra percentage point of unemployment in 2007-09 reduced the employment rate by 0.3 per cent in 2015, nearly a decade later.

88. Reserve Bank estimates in 2019 put the non-accelerating inflation rate of unemployment (NAIRU) at 4.5 per cent, with a two-thirds probability of being between 4 and 5 per cent: Ellis (2019). However RBA Governor Philip Lowe has suggested the NAIRU may rise ‘back towards 5 per cent’ in the wake of the COVID-19 crisis: Hansard (2020, p. 6).

89. In 2012, as the US recovered from the Great Recession, the US Federal Reserve adopted the ‘Evans Rule’. This stated that the US central bank would not increase interest rates until unemployment fell below 6.5 per cent or inflation rose above 2.5 per cent, well above the bank’s target of 2 per cent inflation: Federal Reserve (2012).

to the economy. And the potential output of the Australia economy will very likely be lower in the wake of the COVID-19 crisis than was previously expected, at least until a vaccine is widely available. Inevitably that means some risk of inflation exceeding the upper end of the RBA's target band of 3 per cent, at least for some period. But the costs of doing too much to stimulate the economy are small relative to the costs of doing too little. And if the economy does start to overheat, the RBA can still raise interest rates.

There are few alternatives to stimulus to reduce unemployment. Structural reforms to boost productivity can and should help support economic growth in the long term. But they often do little to boost demand and create jobs in the short term.

### 3.5.2 Substantially more fiscal stimulus is needed

Australian governments should be prepared to introduce substantially more fiscal stimulus policies to boost aggregate demand.<sup>90</sup> The Reserve Bank can and should ease policy further (Section 3.5.3). However, there is not enough scope for further easing to return Australia to full employment, with inflation at target, within an acceptable time frame. For the time being, fiscal policy will therefore be the primary tool of macroeconomic stabilisation in Australia.

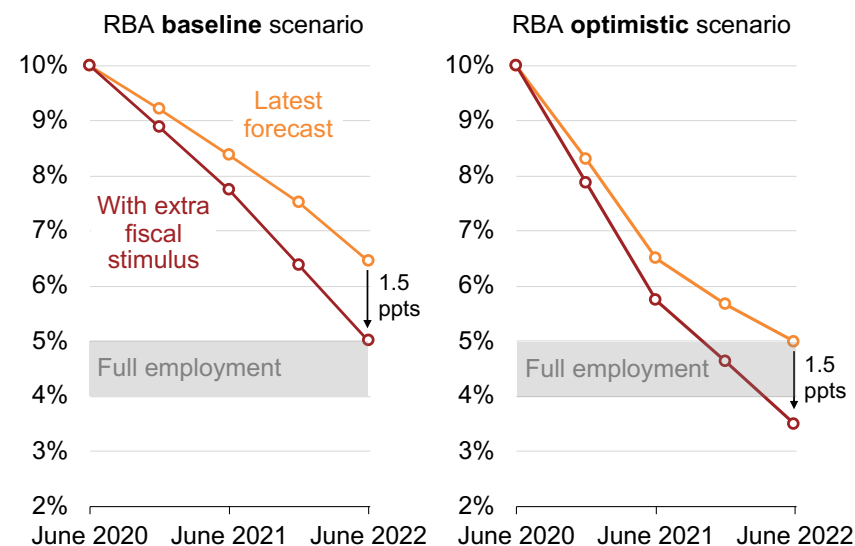
Based on current economic forecasts, returning the economy to full employment will require sizeable fiscal support: in the order of **\$70-to-\$90 billion in additional stimulus** over the next two years, equivalent to around 3-to-4 per cent of GDP.<sup>91</sup> Such stimulus should be deployed with an aim to reduce the unemployment rate by about 1.5

90. Hamilton et al (2020).

91. Economic forecasts are taken from RBA (2020a). The economy may perform better than previously predicted if the additional savings during the recent shutdown period is spent as pent up demand. However, demand is likely to be deficient for some time to come, as previously forecast. See Section 3.1.2 for a discussion of these issues.

**Figure 3.9: A substantial fiscal stimulus program could return the economy to roughly full employment by June 2022**

Projected unemployment rate with and without additional fiscal stimulus



Notes: RBA forecasts are linearly interpolated between six-month increments. 'Full employment' corresponds to the RBA's pre-COVID estimate of the minimum sustainable unemployment rate, plus or minus one standard error band.

Sources: RBA (2020a) and Ellis (2019).



percentage points below current forecasts by June 2022.<sup>92</sup> This could mean between 430,000 and 510,000 extra Australians back in work by mid-2022.<sup>93</sup>

On the RBA's current forecasts, pushing down the unemployment rate by 1.5 percentage points would be sufficient to push the unemployment rate down to about 5 per cent on the RBA's baseline scenario by mid-2022, or below 4 per cent on the RBA's upside scenario (Figure 3.9). Such stimulus would also boost GDP by about 3-4 percentage points over the next two years. In practice, more or less stimulus may be required depending on Australia's success in containing COVID-19, the pace of the economy recovery here and globally, the level to which unemployment can fall without triggering higher inflation, and the efficacy of the precise stimulus measures adopted.

Not all of this spending need take the form of traditional discretionary stimulus: much of the extra spending could be achieved by extending

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92. Estimates calculated using an average boost to GDP in year one of the stimulus of between 80 cents and one dollar for each dollar of stimulus spending, and an Okun's law relationship which suggests that increasing GDP by 1 per cent decreases unemployment by 0.38 per cent using the RBA's baseline economic forecasts. The Okun's law coefficients come from an updated version of Borland (2013), shared through personal correspondence with Jeff Borland. The Commonwealth Treasury used similar 'reduced form' relationships during the GFC to estimate the effect of stimulus: Gruen (2009). While Makin (2016) criticised the multiplier analysis undertaken by Treasury during the GFC, these comments were addressed by Treasury (2014). Furman et al (2020) also apply a similar multiplier-based approach to estimate the impact of COVID-19 recovery programs in the US, assuming multipliers of between 0.8 for tax cuts for individuals, through to 1.5 for aid to directly affected individuals.

93. Estimate includes both Australians in work due to the lower rate of unemployment, as well as Australians who are currently out of the labour force returning to work. Participation impact based on Evans et al (2018), which suggests that a 1 per cent increase in the cyclical component of GDP leads to a 0.4 percentage point increase in the participation rate over the following two quarters.

existing emergency supports and adopting new ones. In particular, temporary spending should include:

- Extending JobKeeper beyond September for businesses still in strife and reshaping the scheme to include temporary migrants and casuals (Chapter 4).
- Phasing down the Coronavirus Supplement more gradually *after* JobKeeper is removed (Chapter 5).
- A 'catch-up' loading for schools to provide intensive tuition programs for disadvantaged students hurt by school shutdowns (Chapter 8).

Taken together, these reforms would cost the Federal Budget about an additional \$30 billion over 2020-21. In addition, permanent fixes should include:

- Increasing the JobSeeker unemployment payment and Commonwealth Rent Assistance (Chapter 5).
- Increasing childcare subsidies to improve incentives to work (Chapter 5).

Permanently higher rates of Jobseeker, Rent Assistance and the Child Care Subsidy would provide at least another \$7 billion in stimulus in 2020-21 and \$14 billion in stimulus in 2021-22 (Table 3.1).<sup>94</sup>

On top of these emergency and long-term supports, additional discretionary fiscal stimulus of about \$20-to-\$40 billion over the next two financial years – around 1-to-2 per cent of GDP combined – would be required to reduce unemployment by 1.5 percentage points, and return Australia quickly to something like full employment. This stimulus

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94. Although given lags, the full effect of some of this spending may not be felt until later in 2022.

would need to be delivered mostly in the next 12-to-18 months, since the full effect of a stimulus package would only feed through to the economy with a lag.<sup>95</sup> And further support may be required if the economic outlook is worse than expected, especially in the event of a second wave of COVID-19 in which case emergency supports may need to be extended further and further stimulus deployed.

This additional stimulus will need to be announced soon to support confidence in the coming months – in or before the next Federal Budget scheduled for 6 October. Further discretionary stimulus could also be designed to be deployed, or scaled back, depending on whether unemployment remains higher (or lower) than forecast.

While state governments should deploy what stimulus they can to support the economic recovery, and should avoid premature fiscal tightening, the Federal Government will need to fund the lion's share of any stimulus. Such spending would not impair the Federal Budget in the long term. Even assuming no boost to GDP from the spending, public debt by 2029-30 would be only 3-to-4 per cent of GDP higher than otherwise.<sup>96</sup> In practice, accelerating the pace of economic recovery, and preventing the long-term costs of sustained high unemployment, would result in stronger economic growth in the long term, and therefore debt-to-GDP would be lower than presented here.<sup>97</sup>

Failing to provide this support will condemn many Australians to unemployment for longer. During the Great Depression, and in many

95. Fiscal multipliers on most types of stimulus are typically larger in the second year than the first. See: OECD (2009).

96. Assumptions as per Figure 3.12.

97. For instance Fatas and L. H. Summers (2015) found that every 1 per cent reduction in GDP brought on by tight fiscal policy translated into a 1 per cent decline in potential output five years later.

**Table 3.1: Fiscal stimulus measures**

Estimated total spending in 2020-21 and 2021-22 fiscal years

| Measure                                                                             | 2020-21      | 2021-22            |
|-------------------------------------------------------------------------------------|--------------|--------------------|
| <b>Emergency supports</b>                                                           |              |                    |
| Extend JobKeeper for 3 months; re-test in September                                 | \$12-\$15b   |                    |
| Lower JobKeeper part-time rate, for the 3-month expansion                           | -\$0.5b      |                    |
| Expand JobKeeper to include casuals and migrant workers, for the 3-month expansion  | \$3b         |                    |
| Extend JobSeeker supplement to December; phase down to March 2021                   | \$10-\$15b   |                    |
| Intensive tuition programs for disadvantaged students                               | \$1.2b       |                    |
| <b>Subtotal</b>                                                                     | <b>\$30b</b> |                    |
| <b>Permanent fixes</b>                                                              |              |                    |
| Raise JobSeeker by at least \$100 per week (from April 2021)                        | \$2b+        | \$8b+              |
| Childcare subsidy reforms (from Oct 2020)                                           | \$4b         | \$5b               |
| Lift Rent Assistance by 40% (from Oct 2020)                                         | \$1b         | \$1.5b             |
| <b>Subtotal</b>                                                                     | <b>\$7b+</b> | <b>\$14.5b+</b>    |
| <b>Additional temporary stimulus over next two years, front-loaded into 2020-21</b> |              | <b>\$20b-\$40b</b> |

*Notes: Figures in this table assume that one third of businesses will qualify for JobKeeper after October. The additional costs of expanding JobKeeper to temporary migrants and casuals from the beginning of the program, across all firms, would have been higher. Subtotals are calculated using the mid-point of spending ranges.*

*Source: Grattan Institute estimates.*

advanced economies in the past decade, premature moves to austerity held back recoveries and, in some cases, created new recessions.<sup>98</sup>

### What form should discretionary fiscal stimulus take?

The best fiscal stimulus spending is **timely** such that it is rolled out quickly using established policy infrastructure where possible, **targeted** in ways that are most likely to be spent immediately and therefore boost demand, especially to help those most adversely affected by COVID-19, and **temporary** such that most spending is not baked into the budget for the long term.<sup>99</sup> Since required stimulus spending is likely to be substantial, and be sustained for some time, stimulus should also involve ‘no regrets’ – in other words, the spending should have a solid policy rationale and provide good value for money to the community.<sup>100</sup>

The Federal Government should extend **direct cash payments** to households to boost spending.<sup>101</sup> Estimates suggest that each dollar of cash payments made to low-income or liquidity-constrained households boosts GDP by between 60 cents and one dollar (the ‘fiscal multiplier’), with more recent estimates being higher, and most of the benefit derived in the first few months after the payments are made.<sup>102</sup>

98. See L. H. Summers (2013) for a general discussion of the economic effects of austerity. Elliott (2017) describes the negative impacts of austerity after the Great Depression. Krugman (2012) argues that austerity measures after the GFC hampered economic recoveries in England, Italy, and Spain. Similarly, House et al (2017) find that austerity measures implemented by European countries after the GFC negatively affected performance.

99. Elmendorf and Furman (2008).

100. Coates and D. Wood (2020).

101. Ibid.

102. During the GFC, Treasury assumed multipliers of 60 cents for each dollar of cash payments made to households: Gruen (2009). However, Blanchard and Leigh (2013) and Gruen and Stephan (2014) note estimates of fiscal multipliers during the GFC may have been too low. Furthermore, multipliers are likely to be higher during periods where monetary policy is constrained. See Gruen and Stephan

And recent evidence shows such payments are effective in boosting spending, thereby supporting employment and economic activity.<sup>103</sup> However, one-time payments to retirees tend to be less effective as fiscal stimulus because the payments are more likely to be saved rather than spent.<sup>104</sup>

In general, **personal income tax cuts** tend to be less effective as fiscal stimulus. Such tax cuts are less likely to be spent than direct cash payments, because the benefits are hidden in each pay cheque and because less of the benefit flows to low-income earners who are more likely to spend but pay less income tax in the first place.<sup>105</sup> Bringing forward the start date of the Government’s already-legislated ‘Stage Two’ personal income tax cuts by one year to 1 July 2021 would cost around \$6-to-\$7 billion a year.<sup>106</sup> Bringing forward the ‘Stage Three’ personal income tax cuts, scheduled to start in 2024-25, would cost about \$10-to-\$12 billion a year if implemented from 2021-22.<sup>107</sup> However, these tax cuts are less likely to be effective stimulus since they are not well targeted at cash-constrained households. The funds could be better spent as part of a broader tax reform package.<sup>108</sup> Government stimulus may provide an opportunity for other worthwhile tax reforms that are an upfront cost to the budget such as a land

(2014) and Ramey and Zubairy (2018). In assessing the US stimulus in 2009-10, CBO (2014, p. 5) estimated fiscal multipliers for direct household payments of between 40 cents and \$2.10 for each dollar spent. Furman et al (2020) estimate multipliers of \$1.50 for every dollar in aid provided to hard-hit households.

103. Data from AlphaBeta (2020) suggests that recent stimulus payments and supplements have supported higher levels of consumption.

104. CBO (2014, p. 5).

105. For example, Tulip (2014) estimates fiscal multipliers of 50 cents for tax cuts. In the US, CBO (2014, p. 5) estimates multipliers of between 30 cents and \$1.50 for each dollar in tax cuts to low-to-middle income earners, but just 10 to 60 cents for each dollar in tax cuts to high-income earners. Furman et al (2020) assume multipliers of 80 cents for each dollar in personal income tax cuts.

106. D. Wood et al (2019a, p. 7).

107. Ibid.

108. Ibid (p. 23).

tax/stamp duty swap<sup>109</sup> or transitioning to a corporate cash-flow tax.<sup>110</sup> The transition to these new tax arrangements would see tax collections decline in the short-term, boosting the economy and leaving Australia with a more efficient tax system in the long run.

**Government spending on services** to deal with the fallout from the COVID-19 health crisis should also be a priority. Estimates suggest such government spending typically boosts GDP by between 80 cents and \$1.50 dollar for each dollar spent – in part because there is a guarantee the funds will be spent, rather than saved.<sup>111</sup> For example, the Commonwealth and state governments should increase funding for mental health and domestic violence services, because demand for those services has risen during the lockdown and is expected to remain higher.<sup>112</sup> State governments should also fund programs to help disadvantaged students catch-up on learning lost as a result of school closures (Chapter 8).<sup>113</sup>

**Boosting infrastructure spending** is often nominated as an attractive form of economic stimulus.<sup>114</sup> Estimates typically suggest increased government spending on infrastructure would provide the biggest boost to the economy per dollar spent: each dollar spent on government infrastructure boosts GDP by at least one dollar.<sup>115</sup> And high-quality infrastructure adds to the productive potential of the economy.

But much infrastructure spending typically arrives too late to fill any hole in the economy.<sup>116</sup> And if projects do not produce benefits to the community that exceed their costs, they make everyone poorer in the long run.<sup>117</sup>

Therefore governments should tread cautiously on infrastructure stimulus (see Chapter 6). Similarly, ‘innovative’ policies that are hard to design and implement should not be on the list. The 2008 stimulus spending on new school halls and pink batts was plagued by implementation problems and took too long to roll out.<sup>118</sup>

But some other forms of infrastructure should be priorities.

First, federal, state, and territory governments should fund the building of more **social housing**.<sup>119</sup>

The number of social housing dwellings has barely grown over the past two decades, while Australia's population has increased by 33 per cent.<sup>120</sup> Building 30,000 new social housing units today would cost between \$10 billion and \$15 billion.<sup>121</sup> The Federal Government should fund the states to build social housing units directly or to engage community housing providers as housing developers. A similar initiative during the GFC resulted in 19,500 social housing units being built and another 80,000 refurbished over two years, at a cost of \$5.2

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109. Coates and Nolan (2019).

110. Garnaut et al (2018).

111. Tulip (2014, p. 5) and Coenen et al (2010, p. 32). CBO (2014, p. 5) estimates multipliers of between 50 cents and \$2.50 for a dollar of government consumption in the US.

112. See Towell and McCauley (2020) and Bavas (2020).

113. Students tend to learn less when their schooling is done remotely rather than in the classroom. The longer they are away from school, the worse the damage can be. Sonnemann (2020) and D. Wood and Mackey (2020).

114. For example, see IMF (2020b).

115. OECD (2009) and Holland et al (2013).

116. For example, much infrastructure spending after the 1990s recession did not get started until the economy was already recovering: Kennedy (2009).

117. Previous Grattan research has found that much of the infrastructure spending in the past decade has been spent on projects with weak business cases. See Terrill et al (2016).

118. ANAO (2010) and Harrison (2010).

119. Social housing – where rents are typically capped at no more than 30 per cent of household income – provides a safety net for vulnerable Australians. OECD (2020a) also recommends that Australia invest in social housing as fiscal stimulus.

120. Coates et al (2020c, Figure 3.4).

121. Coates (2020).

billion.<sup>122</sup> The boost to residential construction was nearly immediate: public residential construction approvals spiked within months of the announcement.<sup>123</sup>

A similar investment today would provide a big boost to the construction industry, which accounts for nearly one in 10 Australian workers. Around 6 per cent of all construction workers were out of work as of 30 May this year, and forecasts point to a severe downturn in the sector in the coming months.<sup>124</sup> The Victorian, Western Australian, and Tasmanian governments have already announced funding to construct new social housing and upgrade existing homes as part of their responses to COVID-19.<sup>125</sup>

Building social housing would also help tackle the growing scourge of homelessness. More than 116,000 people were homeless in Australia on Census night in 2016, up from 90,000 a decade earlier. Half of the tenancies housed in the 2008 program were already homeless, or at significant risk of becoming so.

Second, state and federal governments should give priority to **small-scale infrastructure spending and maintenance** (see also Section 6.1.2 on page 72). State and federal governments could fund local councils to bring forward new projects, or to ramp up maintenance spending. Funding should be allocated based on transparent criteria, rather than Ministerial discretion. For example, more than \$1.1 billion was made available to local government for local community infrastructure projects during the GFC. Nearly 71 per cent of projects

were completed by mid-March 2011.<sup>126</sup> State governments should also bring forward planned school maintenance.

Governments should also consider initiatives and investments consistent with a low-emissions future, such as mandatory roll-out of smart meters, subject to a technology review (Chapter 6).<sup>127</sup>

### 3.5.3 Monetary policy should do more to guard against deflation

Low and falling inflation expectations are a warning sign about a possible slide into deflation. Deflation would be disastrous for Australia: it would depress economic activity further, while increasing the debt burden for many households.<sup>128</sup>

Inflation has persistently undershot the Reserve Bank's inflation target in recent years. Over the five years to March 2020, the price level rose by just 9.2 per cent – meaning that inflation over the half-decade before COVID-19 averaged just 1.8 per cent a year.<sup>129</sup> This is below the Bank's target band of between 2 and 3 per cent, on average.<sup>130</sup>

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122. Coates and Horder-Geraghty (2020).

123. Ibid.

124. ABS (2020h) and Knight (2020).

125. The Victorian Government has committed \$500 million to construct new social housing and upgrade 23,000 existing homes: DHHS (2020). The Western Australian Government is spending \$319 million to build, buy, or renovate social housing: McGowan et al (2020). The Tasmanian Government has committed \$100 million for social housing: Gutwein (2020).

126. The formula for allocating funding did not give any priority to particular geographic areas. Rather, it gave preference to councils in growth areas, and councils with larger numbers of residents: ANAO (2011, p. 15).

127. For example, OECD (2020a) argues that Australia should invest in energy efficiency as part of fiscal stimulus measures.

128. With deflation, nominal debts would rise over time relative to prices, rather than falling as with inflation.

129. Grattan calculation based on ABS (2020i). Underlying or 'core' inflation was even lower; 'weighted median' inflation averaged 1.6 per cent over the past five years, while 'trimmed mean' averaged 1.7 per cent: calculations based on ABS (ibid).

130. The Bank has targeted inflation since the early 1990s, formalising the target by agreement with successive Treasurers since 1996: Costello and Macfarlane (1996). The target remains in the latest agreement between the Treasurer and RBA Governor, albeit watered down; the latest Statement on the Conduct of Monetary Policy elevated the prominence of 'financial stability' as a monetary policy goal: Morrison and P. Lowe (2016).



Figure 3.10 shows the yawning chasm that is set to open up between inflation and the RBA's target.<sup>131</sup> The RBA itself forecasts that headline inflation will grow at an average of just 0.8 per cent between December 2019 and June 2022, with underlying inflation at 1.4 per cent.<sup>132</sup> Union officials and market economists also expect inflation to be below target over the next two years.<sup>133</sup> Financial markets expect inflation to be well below the target for years to come, pricing in expected 0.95 per cent annual inflation over the next five years.<sup>134</sup>

The longer inflation remains below 2 per cent, the further we get from the target of achieving *average* inflation of 2-to-3 per cent. This is a problem. Persistently below-target inflation suggests the economy has not been running as hot as it could – the level of economic activity and employment is lower than we could sustainably achieve. Even before COVID-19, the unemployment rate was nearly a percentage point higher than the RBA's estimate of full employment,<sup>135</sup> suggesting that many thousands of Australians were out of work because monetary policy was too tight.

The Reserve Bank responded quickly and aggressively to the COVID-19 shock, loosening policy by cutting the cash rate, buying three-year government bonds to target a yield on them of 0.25 per cent, and making clear that it expects interest rates to remain low for an extended period. But the Bank is not out of ammunition. With inflation expectations so far below the Bank's target band, any remaining scope for loosening monetary policy should be used.

131. Research suggests that actual inflation may exceed measured inflation in some countries during the COVID shutdown, due to changes in the composition in spending, but this effect is temporary: Cavallo (2020).

132. Compound annual rates calculated from forecasts in RBA (2020a, p. 89).

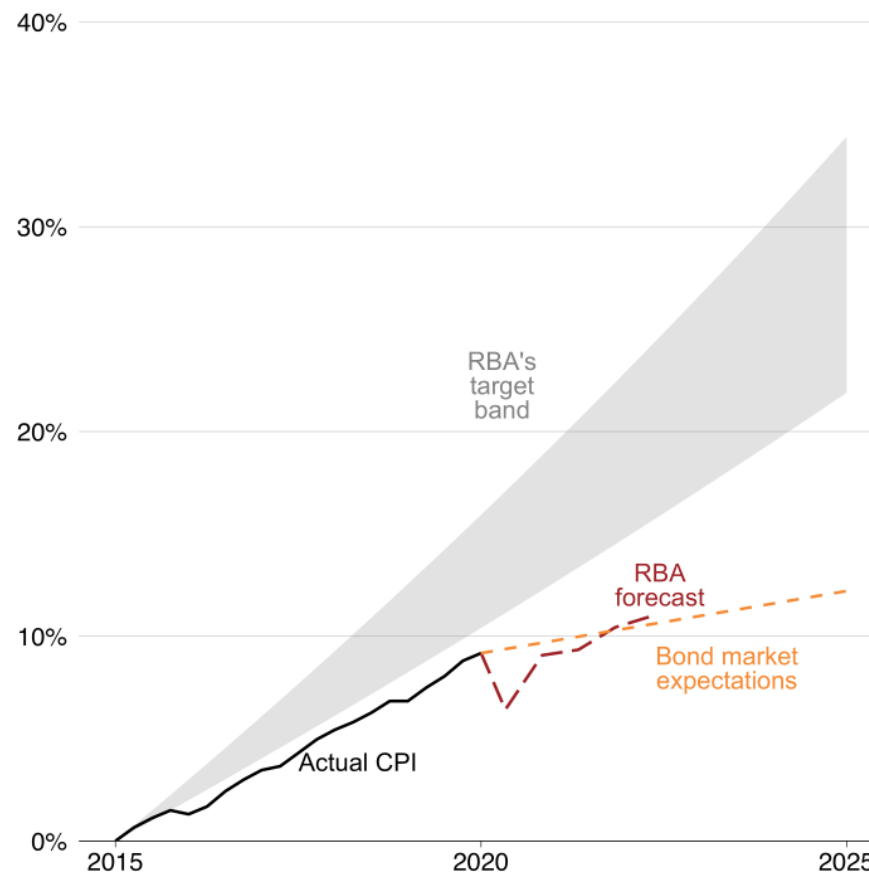
133. RBA (2020d).

134. Grattan calculation based on bond market yields reported in RBA (2020e) as at 23 June 2020.

135. Ellis (2019).

**Figure 3.10: The RBA was undershooting its inflation target before COVID-19, and is now expected to miss the target by more**

Cumulative total inflation since March 2015



Notes: Bond market expectations refers to the compound average rate over five years. Calculated based on yields for Australian government securities. Yields at five-year maturity were imputed. Yields current as at 23 June 2020.

Sources: Grattan calculations based on RBA (2020a), ABS (2020i) and RBA (2020e).



The RBA should be prepared to use unconventional policy tools more aggressively.<sup>136</sup> This may include reducing the overnight cash rate below zero, as several central banks have done.<sup>137</sup> The Bank could purchase foreign currency-denominated assets to lower the exchange rate, or could purchase a broader range of financial assets beyond three-year government bonds.

The RBA can exert a powerful influence on inflation by making clear that it will take whatever actions are necessary to lift inflation back to target and boost economic activity. If businesses and others expect inflation to be higher in future, this reduces real interest rates and can boost economic activity.<sup>138</sup> For a given *nominal* interest rate, higher inflation implies lower *real* interest rates.

Some have expressed concerns that the side-effects of looser monetary policy may not be worth it.

First, there is the claim that unconventional monetary policy will not boost economic activity. This is not supported by the evidence from overseas.<sup>139</sup> In any case, the RBA is already pursuing unconventional policy in the form of yield curve control. The question is therefore how much unconventional stimulus to do, not whether to do any at all.

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136. The Canadian experience shows that unconventional monetary policy can be effective in small, open economies: Macdonald and Popiel (2017).

137. A survey by the Bank for International Settlements reported that 'central banks judged that negative policy rates contributed to the achievement of their policy goals and that their side effects have been contained': Potter and Smets (2019, p. 15). However, there is not consensus in the academic literature about the efficacy of negative interest rates.

138. L. E. O. Svensson (2003).

139. See the summary in Collins and Gagnon (2019). A BIS survey of central banks that had used unconventional monetary policy tools found that they have broadly achieved their goals: Potter and Smets (2019). In Australia, Gross (2019) uses the RBA's own economic model 'MARTIN' to suggest that a large scale quantitative easing could boost economic growth, and decrease the unemployment rate by 0.3 percentage points.

A second claim is that unconventional policy may raise the risk of financial instability. But the Bank, as Chair of the Council of Financial Regulators, has influence over other policy levers to ensure financial stability, such as strengthening bank lending rules or capital requirements, and there are compelling reasons to use these levers rather than keeping monetary policy too tight to maintain financial stability.<sup>140</sup>

A third argument is that, by boosting asset prices, monetary stimulus will exacerbate inequality. While it's true that looser monetary policy will raise asset prices, this is also true of conventional monetary policy – cuts to the cash rate. To the extent that looser monetary policy boosts employment, this tends to *reduce* inequality. Higher inflation also tends to benefit debtors at the expense of creditors, which on average reduces inequality. The net effect of monetary stimulus on inequality is an empirical question – much empirical work finds that tighter monetary policy increases inequality, and that monetary stimulus reduces it.<sup>141</sup>

After the acute crisis phase has passed, the inflation targeting framework should be reviewed. The 'neutral' interest rate is low and has steadily fallen – in Australia and around the world – which makes it more likely that the Bank will find itself unable to fight future recessions with interest rate cuts. Inflation has been persistently below-target. These same concerns motivated the US Federal Reserve to initiate a review of its framework.<sup>142</sup> The RBA Governor has acknowledged that a review of the target may be worthwhile.<sup>143</sup>

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140. See L. E. Svensson (2017) and Saunders and Tulip (2019).

141. See: Coibion et al (2017), Furceri et al (2018) and O'Farrell et al (2016) and discussion in Bernanke (2015). Recent RBA work found that lower interest rates increases housing wealth inequality, but only temporarily: C. He and La Cava (2020).

142. Brainard (2019).

143. Kehoe (2020).

### 3.6 Now is not the time for debt panic

The fiscal response to manage the fallout from coronavirus has been huge. But rushing too quickly to consolidate the budget position would be an economic ‘own goal’ – hampering job creation, growth, and ultimately the bottom line.<sup>144</sup>

Australia has the fiscal space to borrow to support the economic recovery, having come into this crisis with low debt levels by international standards. Australia’s net debt was about 23 per cent of GDP, compared to net debt of 75 per cent in the UK, 85 per cent in the US, and more than 150 per cent in Japan (Figure 3.11).<sup>145</sup>

And it has never been cheaper to borrow. The Australian Government 10-year bond rate is now less than 1 per cent. Adjusted for inflation, the *real* interest rate at which the Federal Government can borrow is below zero.

Governments can lock in these low interest rates by issuing longer-dated bonds, reducing the risk that debt will have to be rolled over at higher rates in future.

Even if gross debt reaches over \$800 billion by 2021-22 – as the Parliamentary Budget Office suggests it could<sup>146</sup> – interest payments associated with the additional ~\$300 billion would be only about \$3 billion a year. This means the Government has the space to do ‘whatever it takes’ to boost employment.<sup>147</sup>

Over the medium-term, the Government will need to act to ensure debt is sustainable and does not continue to rise as a share of the economy (Box 2).

144. DeLong and L. Summers (2012).

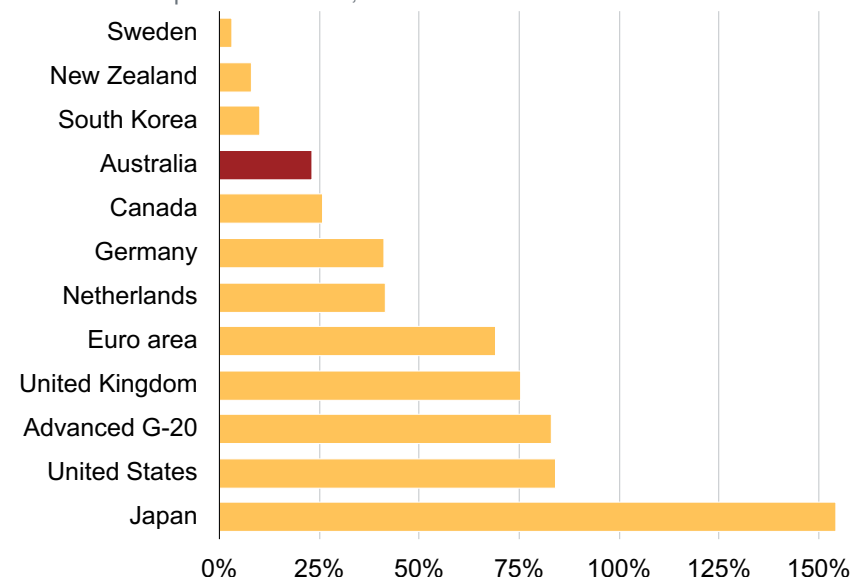
145. Public debt is usually expressed as a percentage of gross domestic product to account for a country’s capacity to service its borrowing.

146. PBO (2020).

147. See also Preston (2020).

**Figure 3.11: Australia has low debt by international standards**

Net debt as a per cent of GDP, 2019



Source: IMF Fiscal Monitor.

The Government has signalled it will manage the debt by seeking to increase the size of the economy over time.<sup>148</sup> Healthy GDP growth allows debt to shrink as a share of the economy without the need for tax increases or spending cuts. And closing the output gap to ensure the economy is operating at potential, with a pickup in inflation, would also support debt sustainability in the medium term, as would a return to higher population growth.

Figure 3.12 highlights the importance of growth. Under a higher-growth, higher-inflation scenario (nominal GDP growth of 6.5 per cent) the ratio of debt-to-GDP shrinks even if the government continues to run substantial budget deficits of \$50 billion a year (around 2 per cent of future GDP). But in a low-growth, low-inflation scenario, where nominal GDP rises by just 3 per cent each year, debt would rise as a share of the economy over time.

Australia ‘shrunk’ high levels of debt after World War II through very high economic growth. But in the next decades, Australia is unlikely to enjoy the economic tailwinds of the post-war years. Nominal growth through the 1950s averaged more than 10 per cent a year because of high population growth and inflation.<sup>149</sup> Nominal growth between 2010 and 2019, on the other hand, averaged about 4.5 per cent.<sup>150</sup> And in a world with COVID, population growth is likely to be slower, reducing the headline growth rate.

Government policies in areas such as tax, workforce participation, energy and climate policy, land-use planning, competition, and innovation can help create the preconditions for strong sustained economic growth and rising living standards on the other side of the COVID-19 crisis. Future Grattan Institute work will address these issues in greater detail.

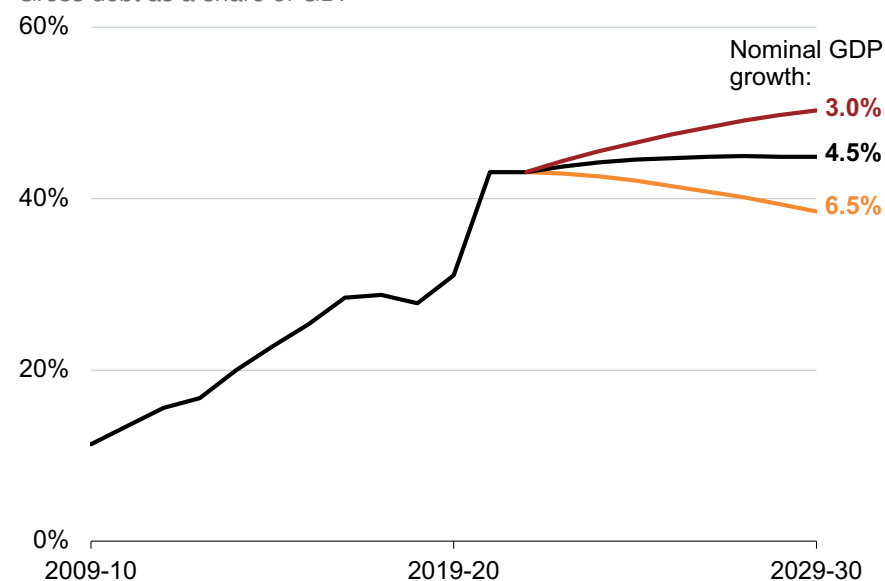
148. Frydenberg (2020).

149. Treasury (2001).

150. Average annual nominal GDP growth June 2010 to June 2019: ABS (2019a).

**Figure 3.12: Debt sustainability depends a lot on economic growth**

Gross debt as a share of GDP



Notes: Projection from an estimated three-year shock resulting in \$837b AGS on issue and \$1.94t GDP at the end of 2021-22. This is based on Parliamentary Budget Office mid-point scenarios which imply underlying cash balance estimates of \$62 billion, \$185 billion and \$48 billion from 2019-20 to 2021-22: PBO (2020). The figure assumes deficits of \$50 billion per year from 2022-23 to 2029-30 and debt costs averaging 1.5 per cent.

Source: Grattan analysis.

But even with reforms to boost growth, the Commonwealth Government will likely need to embrace structural budget reforms over the medium-term to consolidate the budget position. This should be done following a review of the medium-term fiscal strategy to determine whether it is still fit for purpose.

State and territory governments also face substantially higher debt levels. Fiscal stimulus totalling almost \$25 billion by state and territory governments, alongside falling revenue, means that the \$426 billion in total liabilities<sup>151</sup> held across all eight jurisdictions will spike in 2020. As with the Commonwealth, states should be looking to spread the cost of coronavirus over an extended period; stabilising debt-to-GSP ratios in the short-term, combined with a strategy to stabilise or reduce the burden in the long-term.

### 3.7 Who pays?

The COVID-19 crisis has come at an enormous cost – both in terms of the hit to incomes and the fiscal response. The federal Treasurer has been keen to remind Australians that ‘there is no money tree’.<sup>152</sup>

Some recommendations in this book – such as an increase to the JobSeeker payment and boost to the Child Care Subsidy – will lock in higher spending.

So who pays?

The choices governments make on economic reforms and the nature and timing of any budget consolidation will ultimately determine who pays for the COVID-19 hit. These are difficult, values-laden questions. But when an attitude that ‘we are all in this together’ has guided the health response, it seems reasonable that the same attitude should also guide the economic response.

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151. ABS (2020j).

152. Frydenberg (2020).

The costs of COVID-19 to date have hit some groups harder than others. Younger workers are more than twice as likely to have lost their jobs due to COVID-19,<sup>153</sup> as are people on lower incomes,<sup>154</sup> including many casuals who were deemed ineligible for the JobKeeper program. Many have no paid leave and little savings. And we know from past recessions that younger people are most likely to be ‘scarred’ by unemployment.<sup>155</sup>

The costs of COVID-19 should be shared broadly across Australians of all ages as well as over time. As governments consolidate budgets, we should not rely on bracket creep, increasing inefficient taxes like stamp duties, or welfare tightening to do the heavy lifting.

If we do, the young and the vulnerable will pay twice: first in the initial employment shock, and second with a higher tax burden, slower growth and a weak safety net (Chapter 5).

There are other ways to pay down the debt and reform taxes that would share the burden more broadly. For example, abolishing stamp duties and replacing them with a broad-based property tax would significantly reduce the economic drag from the tax system and provide a much more stable foundation for state government budgets.<sup>156</sup>

Winding back some of the generous tax breaks for older Australians that serve little policy purpose<sup>157</sup> would also help to ensure that the economic cost of coronavirus doesn’t fall disproportionately on the shoulders of the young.

Delivering the promised \$300 billion of income tax cuts over the next decade will be incredibly difficult against the backdrop of large deficits

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153. See Figure 3.1 on page 17: ABS (2020c).

154. Coates et al (2020a).

155. See section Section 3.5.1 on page 26.

156. Daley et al (2018b); and Daley et al (2019).

157. See D. Wood et al (2019b, Chapter 5) and Daley et al (2016) for a more detailed discussion.

### Box 2: Public debt – when should we care?

There are three main reasons that governments have historically worried about debt.

First is that government debt could ‘crowd out’ private sector investment and therefore reduce future output and consumption.

Second is that high debt can reduce a government’s capacity to borrow when it needs to. Governments with limited ‘fiscal room’ can face credit rating downgrades and higher debt costs when they need to borrow.

Third is that future generations shouldn’t pay the price for spending today. Borrowing to fund recurrent spending asks future generations to pay the interest costs for past spending from which they received little benefit. This argument is less salient where debt funds productive investments that benefit future generations.

Historically low interest rates and sluggish investment have led some economists to rethink the blanket aversion to public debt. Some such as Olivier Blanchard and Larry Summers have noted that there are no fiscal costs to holding debt when nominal economic growth exceeds the

rate of interest, since debt as a share of the economy will shrink over time without the need to run budget surpluses. Further, in a world with very low risk-adjusted returns to capital – essentially a surfeit of savings to fund productive investments – the welfare costs of crowding out are probably small. Finally, the risk premium faced by countries with high debt is currently low: Japan can borrow at a 10-year nominal interest rate of 0.1 per cent despite gross debt of 240 per cent of GDP.

Of course this doesn’t mean that nations should release all fiscal shackles – there remains some welfare cost to debt, there is a risk that interest rates will rise again, and there remains the possibility that investors will reassess their views on the risks of high public debt levels. Maintaining fiscal room for the next crisis is still important.

Governments with high debt levels should look to bring them down as a share of the economy when times are good. But while the economy remains weak, governments should seize opportunities to support economic growth through stimulus to support long-term productive capacity.

and growing debt. But the Government should not abandon income tax cuts altogether. There is scope to be smart: packaging income tax cuts with removing or reducing tax concessions that have little economic justification (including negative gearing, the 50 per cent capital gains tax discount, and some workplace deductions) could help the budget while making sure that bracket creep doesn't reduce work incentives over time.

There are also good options to reduce spending that don't disproportionately hit the vulnerable.<sup>158</sup>

Infrastructure decisions, many measured in the billions of dollars, are too often based on politics rather than proper economic assessment. Institutions such as Infrastructure Australia and its state equivalents exist to provide advice on project priorities; governments should listen to them.<sup>159</sup> In health, Australia spends too much on medicines and devices. The cost of providing the same procedure often varies widely from hospital to hospital, with no good reason.<sup>160</sup> And the fact that the Age Pension assets test continues to exclude owner-occupied housing means taxpayers are subsidising inheritances for those lucky enough to have parents who own a valuable home.<sup>161</sup>

Done well, these sorts of reforms would improve the efficiency of tax and spending for decades to come, as well as ensuring that the costs of this crisis are more evenly shared.

Future Grattan work will look at these and other options to help consolidate government budgets when the economy is back on track.

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158. Welfare payments are first in line for governments looking to consolidate their fiscal position. For example, tighter spending in the decade after the GFC resulted in a winding back of support for single parents, tighter activity testing on the Disability Support Pension, and a freeze in the rate of Newstart and Rent Assistance in real terms.

159. Terrill and D. Wood (2018).

160. Daley et al (2019).

161. D. Wood et al (2019b).

But for the next two years, stimulus rather than austerity should be the priority.



## 4 Getting back to business

The COVID-19 lockdown delivered an overnight hit to the revenues of Australian businesses. The shockwaves are still reverberating even as some businesses reopen their doors.

Unprecedented cashflow and regulatory supports from the Commonwealth and state governments have assisted many businesses to survive the shutdown. Government rightly gave priority to speed over design perfection in rolling out these measures but, as a consequence, some refinements are needed.

Most of the major support measures will expire in the next three months. With the cashflow of most businesses still squeezed, turning off these supports all at once would be a mistake. Some can be removed as scheduled, but the JobKeeper program and rental codes should be extended for businesses that face a sustained hit to their revenues. The aim should be to preserve businesses that are likely to have a long-term future, and encourage restructuring of those that don't.

Corporate bailouts should be avoided, except in the rare circumstances where the firm underpins capacity in a vital industry and there are no alternative buyers of the assets. Even then, governments should favour loans over cash assistance or equity stakes.

The ACCC will also have an important role to play in the recovery phase. Mergers should be approved only where it is satisfied that they won't be detrimental to competition under more normal economic conditions. And authorisations put in place to help facilitate the lockdown should be reviewed, and removed as soon as sensible to reduce the risks of longer-term harm to competition and consumers.

### 4.1 The immediate shock is easing but Australian businesses are not out of the woods

Government-mandated lockdowns to control the spread of coronavirus resulted in revenues temporarily dropping overnight to zero for many Australian businesses, something not seen in previous economic crises.

In the sectors at the frontline of the social distancing, a significant share closed their doors within a week of the stage 3 lockdowns – arts and recreation (53 per cent), food and accommodation services (31 per cent), and retail trade (24 per cent).<sup>162</sup>

But even sectors not 'brick walled' by the health response have suffered substantial hits to their revenues. For many businesses, the 'second round effects' – the reduction in demand as consumers lose income and fear the future, and other businesses use their services less (see Chapter 3) – have had a bigger impact on the bottom line than the effect of the direct lockdown measures.<sup>163</sup>

Even with recent easing of restrictions, many businesses are not able to operate at full capacity. In May, most businesses in most industries were still hampered by government restrictions on trading and travel, or by social distancing (Figure 4.1 on the following page).

The biggest barrier other than government restrictions is weak customer demand.<sup>164</sup> Demand has not 'snapped back'; two-thirds of

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162. ABS (2020k).

163. Chen and Coates (2020).

164. In response to the question 'Aside from relaxing government restrictions, what is needed for businesses to return to pre-COVID-19 trading conditions?', 35 per cent of businesses reported 'increased or returning customer demand', compared with 'nothing else' (29 per cent), increased cash flow (14 per cent),

businesses were still reporting reduced revenue in June – and of those businesses, about a third were still reporting revenue losses of 50 per cent or more.<sup>165</sup>

The demand shock hurts all industries, even many of Australia's larger industries such as construction that escaped the tougher restrictions imposed on the hospitality and tourism sectors (Figure 3.2 on page 17).

This means the cash flow squeeze is still on. Many small and medium shopfront businesses – cafes, gyms, hairdressers, etc – only hold enough cash to cover a few months of expenses.<sup>166</sup> While their main labour costs can be avoided during the shutdown or are significantly supported by the JobKeeper program, many months of paying unavoidable costs, including rents, with zero or heavily reduced turnover means that many will be reaching the end of their buffers, even with government support packages.

This is why the next six months is the high-risk period for insolvencies. The decisions governments make in coming months will be pivotal to building on the success of the rescue packages in preserving viable businesses.

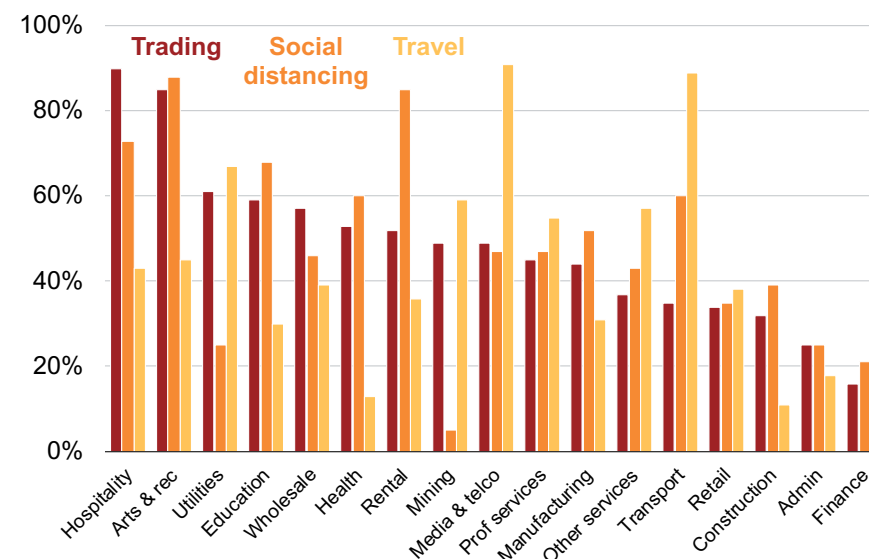
further government support (13 per cent), and 'access to additional funds' (11 per cent): ABS (2020l).

165. ABS (2020e). Of the businesses that reported lower revenue compared to this time last year, 26 per cent had lost up to 25 per cent of revenue, 37 per cent had lost 25-50 per cent of revenue, and 31 per cent had lost 50 per cent or more. The remaining 6 per cent did not know. The survey was conducted by the ABS from 10-17 June.

166. In an ABS survey in June, 29 per cent of all businesses reported their operations would last less than 3 months based on currently available cash on hand (42 per cent for hospitality businesses). Another 19 per cent said only 3-to-6 months, and 16 per cent did not know: ABS (ibid).

**Figure 4.1: Most businesses in most industries were still affected by government restrictions in May**

Proportion of trading businesses affected by government restrictions on ...



Note: The ABS surveyed businesses between 13 May and 22 May 2020 on COVID-19 impacts.

Source: Grattan analysis of ABS (2020l).

## 4.2 Governments have provided significant cashflow and operating support for business

During the initial ‘rescue’ phase of the crisis, government interventions focused on providing liquidity and regulatory support to businesses to enable them to keep trading (Table 4.1).

This was the right response given the nature of the crisis. Firms have a huge amount of embodied productive capacity – including technical know-how, trained staff, and relationships with suppliers and customers. None of these things can be replaced overnight. Letting large swathes of otherwise viable businesses go under would hurt the productive capacity of the economy.

## 4.3 Supports have largely been effective but refinements are needed

To date, this combination of policies has largely been effective in keeping businesses above water. About 900,000 businesses are getting JobKeeper payments, supporting about 3.5 million employees (Box 3 on the next page). About 690,000 businesses have received emergency cashflow assistance from government, and 38 per cent of businesses still trading have renegotiated their rent arrangements.

About 1.6 million people have been stood down or are working fewer hours than usual<sup>167</sup> – and the JobKeeper program has kept many of them from unemployment.<sup>168</sup> Crucially, it maintains genuine links between employers and employees, even when the employee is not working.

It also created an incentive for businesses to continue operating in some form, by subsidising work hours that would otherwise be

167. ABS (2020d).

168. Borland (2020b).

**Table 4.1: Major business support measures during the crisis**

| Measure                                           | Description                                                                                                                                                                       | Duration                      |
|---------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------|
| <b>Fiscal supports</b>                            |                                                                                                                                                                                   |                               |
| JobKeeper payment                                 | \$70 billion wage subsidy program that provides \$1,500 a fortnight payment to workers in eligible businesses                                                                     | 27 Sep                        |
| Cash flow support for business                    | Businesses with turnover under \$50 million receive a payment equal to 100 per cent of their salary and wages withheld, minimum payment of \$10,000 and maximum of \$50,000       | 2 payments: 28 Apr and 28 Jul |
| Coronavirus SME loan guarantee scheme             | Government will guarantee up to 50 per cent of loans issued to SMEs (up to \$20 billion in total)                                                                                 | 30 Sep                        |
| State tax and fee relief for JobKeeper businesses | All states have offered payroll tax and other relief for businesses on the JobKeeper scheme                                                                                       | 27 Sep (with JobKeeper)       |
| <b>Regulatory and other supports</b>              |                                                                                                                                                                                   |                               |
| Rental agreements                                 | Moratorium on tenancy evictions and mandatory code of conduct for SMEs and businesses on JobKeeper                                                                                | 27 Sep (with JobKeeper)       |
| Bank holidays on loan repayments                  | Many banks offering businesses the option to defer loan repayments                                                                                                                | Up to six months (~Sep)       |
| Temporary Corporations Act amendments             | e.g. temporary higher thresholds and more time to respond to statutory demands from creditors; company directors temporarily relieved of personal liability for insolvent trading | 24 Sep                        |
| Fast-tracking approvals                           | State ministers fast-tracking planning and development                                                                                                                            | Until powers revoked          |

*Note: SME = Small to mid-size enterprise.*

*Source: Grattan analysis of government announcements.*

unaffordable to employers,<sup>169</sup> encouraging innovation and supporting the recovery.<sup>170</sup>

About 200,000 businesses, mainly small businesses, had stopped trading in response to the crisis by the time JobKeeper was announced.<sup>171</sup> Given the speed and scale of the crisis, many more would have closed had the Government not introduced JobKeeper.

The Government's overall response in support of businesses in the rescue phase can be judged as a success. The Government rightly gave priority to speed over design perfection – getting supports out to businesses quickly was necessary given the extremely sharp nature of the shock.

But there are a number of design flaws – some of which may bite in coming months – that should now be fixed as a matter of priority.

#### 4.3.1 JobKeeper should be reshaped

JobKeeper should be paid in advance rather than in arrears, and the program should be expanded to cover short-term casuals, temporary migrants, and university workers. To partially cover the additional cost of these changes, a part-time rate could be introduced, rather than the present flat payment to everyone regardless of their previous or current work hours.

169. JobKeeper replaces 70 per cent of the median wage. That means employers can retain 70 per cent of work hours for someone earning the national median salary at no wage cost. Even if a business can't operate as normal, that's almost 30 hours a week where employees can innovate and develop the business to help it accelerate into the recovery.

170. In June, 43 per cent of businesses reported having implemented some form of innovation in their operations (having changed the types and range of products or services offered or the way they are delivered to customers): ABS (2020e).

171. About 9 per cent of all businesses, on top of the normal monthly exit rate of about 1 per cent: ABS (2020m). About 160,000 businesses cited COVID-19 directly and another 70,000 businesses shut because of the drop-off in demand: ABS (2020k).

#### Box 3: The JobKeeper payment

The JobKeeper program, announced on 30 March, provides a wage subsidy to encourage and assist employers to retain their workers. The program pays employers \$1,500 a fortnight for each eligible employee. Employers must in turn pay their employees at least \$1,500, even if their ordinary wage is less than this amount.

The scheme was originally expected to cover 6 million Australians for 6 months from 30 March, but this estimate was revised down on 22 May to 3.5 million employees, reducing the expected cost of the scheme from \$130 billion to \$70 billion.

The scheme was designed to include people currently working for their employer, as well as employees who were stood down or fired any time after 1 March, as long as they remain with or re-attach to their employer.

To be eligible, a business must have suffered a revenue drop of at least 30 per cent; or 50 per cent if it has annual turnover greater than \$1 billion. The threshold for charities registered with the Australian Charities and Not-For-Profits Commission is 15 per cent. Major banks are ineligible, as are public sector employers.<sup>a</sup>

Both full-time and part-time staff are eligible. Casuals are eligible if they have worked for their employer for at least 12 months.<sup>b</sup> Most temporary migrants are ineligible.<sup>c</sup> Workers are only eligible for the subsidy for one job, even if they hold multiple jobs.

a. For the full eligibility criteria, see ATO (2020b).

b. Morrison (2020a).

c. Holders of a 'special category subclass 444' visa – New Zealand citizens living and working in Australia – are eligible for the scheme.

### JobKeeper should be paid in advance

One barrier to the effectiveness of JobKeeper is the fact it is paid in arrears. Payment in arrears makes it easier to ensure that the payment is going only to workers who are kept on the books, but it is not essential to the integrity of the scheme.<sup>172</sup>

Payment in arrears was initially a barrier to take-up of the scheme, because it required businesses – including those that had shut their doors – to pay five weeks of JobKeeper payments to staff before reimbursements started.

Businesses without sufficient cashflow were encouraged to take advantage of government-backed loans to get through, but for many the process was too slow or was seen as unacceptably risky.<sup>173</sup>

These cashflow issues probably contributed to the take-up of the JobKeeper scheme being lower than expected.<sup>174</sup>

JobKeeper payments remain in arrears, so many businesses need to borrow on an ongoing basis to fund their payroll. Given it is now known how much will need to be paid for businesses that are in the scheme, it would be very easy to switch to payment in advance by paying double with the next payment – effectively advancing for the next month of wage subsidies. The Government should do this as a matter of priority.

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172. Any discrepancies between the amount received and the number of workers actually on the books can be monitored via the ATO's Single Touch Payroll system, and payment can then be adjusted for the next month.

173. Moullakis (2020). In May, one in 10 Australian businesses reported they had sought additional funds as a result of COVID-19. Additional funds were mostly in the form of loans from financial institutions, but a quarter of businesses that sought additional funds reported having drawn on the business owners' personal line of credit or savings: ABS (2020I).

174. D. Wood (2020a).

### JobKeeper eligibility should be broadened

Another big limitation of the scheme is the coverage – it excludes short-term casuals, temporary migrants, and university workers.

There are many reasons to extend JobKeeper to temporary visa holders. These visa holders are not eligible for the normal safety net payments such as JobSeeker, and in many cases there are no affordable options for them to return to their home country.<sup>175</sup>

Leaving people 'high and dry' leaves them in poverty, damages Australia's reputation as a good global citizen, and makes it harder to attract skilled workers and international students in future. The Tasmanian Government has recognised this and introduced a suite of support measures for temporary migrants.<sup>176</sup> Most other countries have included temporary migrants in their job support schemes.

It also means that JobKeeper is a far less generous scheme for those businesses in sectors that rely more on temporary visa holders – including hospitality, retail, healthcare, and aged care.<sup>177</sup> If temporary visa holders go on the scheme proportionally to residents, then including them for six months would cost about \$10 billion.<sup>178</sup>

Similarly short-term casuals – those who have worked for their employers for less than a year – have been excluded from JobKeeper. The Government has pointed to the need to 'draw the line somewhere', and it is true that perhaps the benefits of maintaining links between employers and employees are less compelling for short-term casual

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175. Root (2020).

176. Tasmanian Government (2020).

177. Grattan analysis of employed temporary visa holders by industry, excluding NZ citizens: ABS (2019e).

178. This is an upper bound estimate, based on the number of temporary visa holders pre-crisis – many may now have returned home. Alternatively, JobSeeker could be made available to temporary visa holders through to the end of 2020.

workers. And unlike temporary visa holders, casual workers are eligible for the JobKeeper payment.

But on balance it makes sense to extend JobKeeper to short-term casuals.<sup>179</sup> Their exclusion has left big holes in support for some of the worst-hit sectors – including arts, recreation, and hospitality. And including them over six months would also spread the broader economic benefits of the scheme by providing an additional \$6 billion or so in income support to mainly lower-paid workers.<sup>180</sup>

It appears the Government has refined the eligibility test for JobKeeper to ensure that the staff at ‘public’ universities are excluded.<sup>181</sup> While superficially in line with the Government’s intention that employees at public-sector institutions should not qualify for the scheme,<sup>182</sup> it makes little sense for universities that receive only about half their funding on average from government.<sup>183</sup>

Universities are major export businesses and large employers that have suffered a significant hit to their revenues due to the lockdown. The policy rationale for the JobKeeper scheme – to support jobs and the private sector recovery – would seem better served by including universities. One way to do so would be to make JobKeeper available

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179. Especially those who have a longer-term relationship with their employer, such as those in regular seasonal employment, and long-term casuals who may have had a holiday at the wrong time.

180. Duke and Bagshaw (2020).

181. Universities are not explicitly excluded, but several changes have been made to the JobKeeper rules that are specific to them and in effect exclude most universities (universities listed under Table A of the *Higher Education Support Act 2003*), while explicitly including ‘private’ universities (Table B universities), despite there being little meaningful distinction, see Norton (2020a).

182. Karp (2020a).

183. Department of Education (2020). Particularly when private universities – some of which receive a substantially higher share of their revenues from government – are able to qualify. See Norton (2020b) and Norton (2020c) for a detailed discussion of the issues.

to universities for the second semester of 2020, if they pass the usual turnover reduction thresholds. This would recognise that universities’ mid-year intake is likely to be hit even harder by government restrictions than their first-semester enrolments.<sup>184</sup>

### The JobKeeper rate should be lower for part-time workers

The JobKeeper scheme pays all eligible workers at a flat rate regardless of the hours they worked before coronavirus hit, or subsequently. This has meant that many lower-paid, part-time workers have received a pay rise. Indeed, we estimate that about 80 per cent of part-time workers on the JobKeeper scheme are receiving more than their pre-crisis incomes (Chapter 5).

Offering more than 100 per cent income replacement for a large group of workers means the scheme costs more than it needs to. It also raises questions about fairness between employees within businesses, because a part-time worker is paid the same amount as an otherwise equivalent full-time worker.

It is likely the Government chose a flat rate to simplify the program. Paying a percentage of pre-coronavirus salary may have meant more complicated paperwork for employers<sup>185</sup> and difficult judgments about what period to assess income for people who work irregular hours.

A simple way to adapt the scheme would be to follow the New Zealand approach and adopt a lower rate for part-time employees working less than 20 hours a week.<sup>186</sup> For example, full-time employees on JobKeeper could continue to receive \$1,500 a fortnight, while

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184. See Norton (2020d).

185. Some have suggested the single touch payroll system should have made this relatively easy, but the Government may have been reluctant to rely on a new system.

186. This could be based on average weekly work hours over the previous month, where there is week-to-week variability.



employees working less than 20 hours a week could receive \$800 a fortnight.<sup>187</sup> The saving, about \$2 billion on the cost of JobKeeper per quarter, could fund some of the extensions to the scheme suggested above.

#### 4.3.2 The states should strengthen the commercial tenancy code

The commercial tenancies code agreed by the National Cabinet sets out a series of good-faith leasing principles for commercial tenancies during the crisis. The principles include that landlords should negotiate rental reductions in line with the tenant's reduction in turnover (Box 4). The code was designed to strike a balance between the interest of landlords, and helping tenants survive the shutdown.

But in enacting the code through their own legislation, most state governments have significantly watered down the main principles (Box 5). The changes by state governments substantially increase the risks of business failures in coming months.<sup>188</sup>

For businesses on the frontline of social distancing restrictions over the past few months, rent is the biggest unavoidable cost.<sup>189</sup> And the

187. A lower part-time payment raises some complications because of the way JobKeeper and JobSeeker interact, but these issues are temporary and can be resolved by employers and individuals if they choose. First, a part-time payment of \$800 a fortnight is low enough to potentially qualify the recipient for JobSeeker as well, which could leave some part-time JobKeeper recipients with more income than full-time JobKeeper recipients if employers do not top up their pay. Second, part-time JobKeeper recipients who do *not* claim JobSeeker could be earning less than JobSeeker recipients (but individuals can remedy this by applying for JobSeeker).

188. All states and territories have offered some form of tax relief to commercial landlords who reduce the rent of COVID-affected tenants, but it is unlikely this provides a sufficient incentive for landlords to provide rent reductions proportionate to turnover declines. For details on state and territory proposals, see [business.gov.au](https://business.gov.au) (2020).

189. D. Wood et al (2020d).

cost is substantial: the average retailer pays almost \$12,000 in rent a month; the average gym, \$10,000. Cafes and hairdressers pay on average \$3,000 to \$4,000 each month.<sup>190</sup>

#### Box 4: The national commercial tenancies code

The national commercial tenancies code provides a framework for businesses that are eligible for the JobKeeper scheme and have a turnover less than \$50 million to negotiate temporary rent reductions with their landlords.

For those businesses not able to operate due to coronavirus restrictions, these rents represent straight cash 'bleed'. And even now that many of these businesses have reopened, constraints on how they operate and a weak economy mean many continue to bleed cash.<sup>a</sup>

The principles underpinning the code were agreed by the National Cabinet and include:

- rental reductions will be proportionate to the reduction in turnover up to 100 per cent of the amount ordinarily payable;
- reductions will be a combination of waivers and deferrals, with waivers accounting for at least half of the reductions; and
- payment of rental deferrals will be amortised over the balance of the lease term or two years, whichever is longer.

a. As at May, the top concern for a quarter of businesses was cashflow, or access to additional funds: ABS (2020l).

190. IBISWorld (2020).

Reducing rent proportional to turnover helps stem the bleed – but does not stop it.<sup>191</sup>

Weakening the requirement for landlords to offer rent reductions will mean that more businesses, particularly shopfront business, will close their doors. And while it may seem like a superficial ‘win’ for landlords, losing these tenants means more empty shops.

High retail vacancies in shopping strips and some malls was already a problem pre-COVID.<sup>192</sup> And too many empty stores creates a death spiral – speeding up the drift of people away from bricks-and-mortar shopping areas – which affects all businesses and landlords.

Those state governments that have weakened the code should reinstate the main principles, to starve off the longer-term economic damage.

If state governments are concerned that doing so would cause too much short-term pain for landlords, they should compensate them for some of the lost rent. Governments could recover some of these costs over time as the economy picks up, through higher land tax on all commercial landlords.<sup>193</sup>

#### **4.4 Emergency measures should be wound back carefully to keep businesses alive**

The key challenge for getting back to business is the speed at which social distancing restrictions are lifted (Chapter 2) and how demand and confidence recovers as government supports are eased.

In determining the right time for the withdrawal of government assistance, governments are balancing competing risks.

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191. D. Wood (2020b).

192. e.g. Schlesinger (2019) and Ziffer (2019).

193. D. Wood (2020b).

#### **Box 5: The states have watered down the commercial rent code**

The key principles for helping share the income hit from coronavirus between landlords and tenants agreed to by the National Cabinet have been substantially watered down in the states’ implementation of the Mandatory Rental Code.

Queensland is the only state to enact the core principle that tenants can negotiate a rent reduction proportional to lost turnover. NSW and Victoria have retained the requirement that the majority of any negotiated rent reduction be in the form of a waiver rather than a deferral, and all states and territories have offered some form of tax relief to commercial landlords who reduce the rent of COVID-affected tenants,<sup>a</sup> but it is unlikely this provides a sufficient incentive for landlords to provide rent reductions proportionate to turnover declines.

Most state and territory versions of the code do limit or ban evictions and lifting rents for tenants who meet a requisite level of financial hardship. The Northern Territory and ACT versions failed to enact even this level of basic protection, although they do require landlords to negotiate in good faith with an impacted tenant. The final schemes in most states leave small businesses with little protection from landlords who fail to respond to the new economic reality.

a. business.gov.au (2020).

- Withdrawing too fast could result in large swathes of otherwise viable businesses closing, squandering benefits of the hibernation strategy.
- Leaving measures in place too long is costly for taxpayers and could delay inevitable restructuring of the economy (including job openings for unemployed people).

The first risk looms larger under the current timetable. Currently all the major cashflow and regulatory supports for businesses (Table 4.1) and households (Chapter 5) will cut out by October, creating a ‘danger zone’ for business and the broader economy.

Indeed, many businesses will face a ‘triple threat’: simultaneous withdrawal of government revenue support, falling demand as income support for households is also withdrawn (Chapter 5), and rising costs because loan deferrals and rent relief agreements expire.

On the Government’s current timetable, more than \$65 billion in income support in the September quarter will be withdrawn by the end of October.<sup>194</sup>

The Government should reconsider these timetables, especially for the businesses whose operations continue to be constrained by social distancing restrictions.

Two of the most significant supports – the JobKeeper payment and mandatory code of conduct for commercial leases – should be extended for businesses yet to see a significant improvement in their position. This would reduce the risk of mass bankruptcies, at manageable additional cost to taxpayers.

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194. D. Wood and Blane (2020). The figure of about \$100 billion for the September quarter has been revised to more than \$65 billion given the substantial downward revision in Treasury’s estimate of the cost of the JobKeeper program.

#### 4.4.1 JobKeeper should be extended for businesses that are still struggling

JobKeeper has been a critical lifeline for businesses and households. But it is rightly a temporary program. The Government should not subsidise wages indefinitely.

JobKeeper was enacted for six months and is scheduled to wrap up on 27 September. But a universal cut-off is blunt. It does not recognise the fact that businesses in different sectors and different parts of the economy will be released from social distancing constraints at different times and have differing capacity to ‘bounce back’.

Cutting assistance to businesses that still have significant constraints on their operations risks undoing much of the good work to date in preserving the productive capacity of the economy.

JobKeeper should be extended for those businesses and employees that are still severely affected by government restrictions, and abridged for others that no longer require support.

Businesses currently receiving JobKeeper should be required to re-test against the turnover requirement at the end of July and September.<sup>195</sup> Where a business’s turnover is now better than 20 per cent below pre-crisis levels, support should be withdrawn.<sup>196</sup> This will require at least one month’s notice, if the program continues to operate in arrears (see Section 4.3.1 on page 44).

The program should be available for an additional three months for businesses that still fall below the turnover recovery threshold in

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195. Hamilton and Edmond (2020) suggest businesses could even move to a month-by-month arrangement relatively easily, given they already have to report to the ATO every month both actual revenue and expected revenue for the next month.

196. i.e. businesses with turnover still 20 per cent or more below their pre-crisis level would continue to receive JobKeeper. Pre-crisis level refers to the turnover test and comparison period previously submitted to qualify for eligibility for JobKeeper.

September. But ultimately the program must end so that it does not preserve businesses that are unlikely to be viable in the longer term because the crisis has induced changes in habits and behaviours, and therefore changes in demand from consumers and businesses.

This would mean that businesses and employees move off JobKeeper in three phases (August, October, or January) depending on how their recovery is tracking. Those workers that become unemployed as JobKeeper ends would transition to JobSeeker, including the temporary Coronavirus Supplement, which should only be phased down gradually from early 2021. A new higher permanent rate of JobSeeker should also be introduced from April 2021 (Chapter 5).

As well as being more effective in maintaining productive capacity in struggling sectors, this approach would help ease the broader economic shock from all the major supports coming off simultaneously.

#### **4.4.2 The mandatory rental code should also be extended for businesses still on JobKeeper**

The mandatory code of conduct for commercial leases should also be extended beyond September for businesses that remain eligible for JobKeeper. The rationale is the same as for JobKeeper payments: if some sectors of the economy have not recovered, particularly because health restrictions are affecting the way they are able to operate their businesses, then the policy bridge is still required.

Restricting access to only those businesses that qualify for the extended JobKeeper ensures that firms that have substantially recovered come off supports.

If the scheme is extended, the Government should work with banks to extend loan deferrals to affected landlords, and state governments should also extend land tax and other supports.

Over the medium-term, if many businesses do not reopen their doors, then commercial space is likely to be less valuable than it was pre-crisis. Banks may need to reconsider valuations, and landlords may need to be willing to drop rents and renegotiate contracts if they want to fill empty shops and have long-term viable tenants.

#### **4.4.3 Given successful re-opening, other measures could be wound back as planned**

Removing the other financial and regulatory supports will also pose some risk to business. But provided the easing of social distancing regulations progresses successfully, without a 'second wave' of infections and more lockdowns, it is appropriate that some of these emergency settings be withdrawn.

For example, reinstating normal rules around insolvency will help reallocate productive resources away from businesses that will not be viable as the economy recovers.<sup>197</sup>

#### **4.5 Governments should embrace clear principles for bailing out firms and sectors**

The Federal Government has provided broad-based support for businesses through its JobKeeper scheme. It has also provided some industry-specific schemes for vital sectors such as aviation and childcare where businesses would have otherwise closed their doors.

Other sectors hit hard by social distancing – tourism, universities, and the arts – also have a case for support, particularly if the Government does not broaden and extend JobKeeper in ways that would give greater coverage to these sectors (Section 4.3.1 on page 44).

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197. ASIC data show insolvencies have slowed since the temporary relief from insolvent trading was introduced (ASIC (2020)), but many businesses will not be viable and an adjustment will be needed.

The Government to date has rightly resisted calls for bailouts of individual firms. But there will be many more lining up for support in the months to come. Government bailouts of individual firms should be rare. They should be countenanced only when the firm is otherwise viable, is of systemic importance, and all other private options for liquidity support have been exhausted. Even then loans should be favoured over grants or equity stakes.

#### 4.5.1 The case for sector-specific support

The JobKeeper scheme is designed to boost cashflow for businesses that have suffered a significant hit to their revenues from the coronavirus crisis. Extra financial support or regulatory changes have been provided for some sectors considered vital to keep operating during the shutdown.

Sector-specific packages were introduced for **aviation**, including cashflow assistance, waiving of fees, and underwriting of airlines' operating costs on selected routes, to keep skeleton flights on core routes.<sup>198</sup> Emergency **childcare** funding arrangements – including free childcare for parents – were introduced to keep childcare centres open through the crisis.<sup>199</sup>

Other sectors warrant additional support, because they have been hit particularly hard by the economic fallout, and the existing JobKeeper

scheme does not provide good coverage for these businesses. The rationale for support is the same as for the broader schemes: to maintain the productive capacity of business and to make sure the short-term shock does not become a long-term drag on the recovery of that sector.

**Arts and cultural businesses** are among the hardest hit by the pandemic. By their nature, many of these businesses make money from large groups gathering in close proximity. Accordingly, these businesses were among the first to close their doors and will be among the last to reopen. About 85 per cent of businesses in the arts and recreation industry have been hurt by trading restrictions,<sup>200</sup> and the industry was second only to hospitality in terms of job losses, losing almost 20 per cent of jobs lost between March and May this year.<sup>201</sup>

The nature of much arts work – moving between employers from production to production or festival to festival – means that many artists are ineligible for JobKeeper assistance. While some are sole-traders and so can apply for the scheme if they meet the eligibility threshold, many are employed at least some of the time as short-term casuals (Section 4.3.1 on page 44).<sup>202</sup> More than one third of Media Entertainment and Arts Alliance members surveyed were ineligible for JobKeeper.<sup>203</sup>

This also means that most arts businesses miss out on the cashflow benefits of the scheme enjoyed by businesses with more permanent employees. Closing some of the JobKeeper eligibility gaps would help, but there may still be a case for specific supports to keep museums, theatre, film companies, and festivals afloat. Cultural events and

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198. The Government initially announced a \$715 million relief package for the aviation sector, which refunded and waived various government fees. An additional \$300 million relief package was later announced for regional airlines to keep at least some flights operating for 138 regional communities that rely on aviation: Karp (2020b), Sullivan (2020) and Department of Infrastructure, Transport, Regional Development and Communications (2020).

199. Under the emergency scheme, the Government paid centres half their usual fees, instead of the normal childcare subsidy arrangements that hinge on demand for childcare. Centres were not allowed to charge parents, but most were able to get JobKeeper payments to help cover some of their remaining costs. See Morrison and Tehan (2020) and Klapdor (2020).

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200. ABS (2020l).

201. ABS (2020n).

202. Morrow and B. Long (2020).

203. Rigby (2020).

institutions will be an important part of rebuilding Australian life in the recovery phase.

Many other countries have offered significant support to the arts and cultural sectors,<sup>204</sup> in recognition of the challenges they face and their role in the rebuild.

**Universities and the tourism sector** are also likely to be squeezed for an extended period because of ongoing restrictions on international travel (Chapter 2).

Universities are receiving some government support for an expected small decline in domestic student enrolments in 2020, but this is nowhere near the scale of their international student revenue losses of around \$3 billion a year.<sup>205</sup>

The Government has recently proposed a substantial set of reforms to higher education funding.<sup>206</sup> While these reforms guarantee that universities can maintain domestic student revenue for the next three years, they are likely to exacerbate the financial problems of many universities in the years beyond.<sup>207</sup>

Universities could be assisted in the short-term by making them eligible for the JobKeeper scheme (Section 4.3.1 on page 44).

Beyond this year, the biggest support governments could provide for the sector would be to facilitate international students coming to

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204. For Europe see: Compendium (2020). For New Zealand see: Hall (2020).

205. Norton (2020e) and Marshman and Larkins (2020a). See also Hurley and Van Dyke (2020).

206. DESE (2020).

207. See Marshman and Larkins (2020b). From 2023, universities would have to enrol more domestic students to get their domestic student revenue back to current levels. There will almost certainly be students who want these additional places. Many who can't find work will instead want to study, and there is also a big increase in demand expected from 2022 corresponding to a big increase in birth rates about 16 years ago: Daley et al (2019, p. 116).

Australia (provided they go into two weeks' quarantine: see Chapter 2). Plans for bringing in international students on a trial basis are already well advanced.<sup>208</sup>

Australia may find itself a more popular destination than most, given its major competitors for international students – the US and UK – have fared far worse in this crisis and could be seen as risky destinations. Australian governments should help streamline visa applications and quarantine processes, and start promoting Australia as 'open for students' for 2021. Universities could cover all or some of the costs of quarantine for their students.

International tourists will take longer to return. Few people will be willing to go into two weeks' mandatory quarantine for a holiday. The tourism industry is suffering considerably – more than 80 per cent of businesses in the arts and recreation industries (including tourism) expect a fall in turnover through the crisis.<sup>209</sup> Domestic tourism will replace some of the lost income as state borders re-open. Pre-COVID, Australians spent more travelling overseas than international travellers spent in Australia.<sup>210</sup>

Government should promote local destinations.<sup>211</sup> Stimulus spending could also provide an opportunity to upgrade local tourism infrastructure (Chapter 3). More targeted support may be required for businesses that appeal particularly to the preferences of international tourists, provided those businesses are likely to be viable in the longer term.

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208. Derwin (2020).

209. ABS (2020o).

210. Ribeiro (2020).

211. The Federal Government committed to a package of \$76 million to promote local tourism after the 2019-20 bushfires: National Bushfire Recovery Agency (2020). This package could be expanded and broadened so it supports a wider range of destinations including those spared by the fires but hit badly by the loss of international tourists.



#### 4.5.2 Firm-specific bailouts should be rare

Firm-specific bailouts are rarely a good idea. Bailouts interfere with the process of ‘creative destruction’ – resources moving from one firm or sector to another where they will create more value for society. Bailouts are often a bad deal for the taxpayer. They are often driven by political considerations rather than dispassionate cost-benefit analysis.<sup>212</sup>

However, the highly unusual nature of the coronavirus shock – bigger than we would expect even well-run business to insure against<sup>213</sup> – means there might be limited circumstances in which a bailout could avoid significant national detriment.

##### Principles for bailouts

A government should satisfy itself of three major tests before proceeding with a bailout:

1. The business was profitable before coronavirus and is likely to be so again in future. Governments should not provide assistance to businesses that were struggling before coronavirus or to businesses that are unlikely to be able to ‘bounce back’ after the shock.<sup>214</sup> The government should satisfy itself that the business has a good chance of returning to viability as the economy returns to its long-term shape – including the long-lasting shifts in demand that may have been induced by extended lockdowns and persistent restrictions aimed at minimising the resurgence of COVID-19.

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212. This means firms that are more successful at galvanising public support are more likely to get bailouts. There is also a risk that firms with political connections get more support. For example, US bank bailouts during the GFC were criticised for favouring politically connected banks. See Casey and Posner (2016).

213. Triggs (2020).

214. Humphery-Jenner (2020).

2. There are no alternatives to preserve the business. Equity injections, debt raising, or selling the business or its key assets to another buyer should all be tested before resorting to government support. The underlying principle is that governments should look to preserve the productive capacity of a business, not the value of investments. A company kept alive through equity write-downs or re-capitalisations can still participate in the broader recovery even if its investors have taken a substantial hit.<sup>215</sup> The Federal Government’s refusal to assist Virgin, given the range of alternative buyers of the airline, was consistent with this principle.
3. Substantial broader economic benefits justify the costs of the bailout. The government should only support a business that can’t otherwise find support from private investors if there are nationally significant economic benefits or ‘spillovers’ from the business continuing to operate.<sup>216</sup> Examples of such ‘pie-expanding’ benefits might include:
  - the business is a significant competitor in an important market and its exit would result in a substantial reduction of competition and significant harm to consumers;<sup>217</sup>
  - the firm plays a vital role in a supply chain so that its exit would cause significant disruption to other businesses;
  - its failure would cause financial system contagion, causing credit to dry up and broader economic harm; or
  - the business is a major employer in an area where other businesses are unlikely to open or expand to employ those workers in future.

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215. Wilkes (2020, p. 25).

216. Casey and Posner (2016) refer to this as ‘ex-post efficiency’ of the bailout.

217. Asker and Holden (2020).

But even where supporting a business would have broader economic benefits, governments should not assist unless support *also* meets the first two tests.

### The form of a government bailout

If a business does meet the above criteria, there is a question about what form support should take. Cash subsidies might help the business survive but are an expensive form of support for the taxpayer – giving them nothing directly in return.

Equity injections cost less but are more complicated. Establishing a fair price can be difficult.<sup>218</sup> Government equity holdings, particularly in heavily regulated sectors, raise difficult concerns about conflict of interest and competitive neutrality.<sup>219</sup> This can be partly mitigated but not eliminated by placing equity holdings in the hands of an independently run entity such as the Future Fund.

Government loans or loan guarantees are generally a better middle ground. They are less costly than grants, although they still pose some cost to the taxpayer.<sup>220</sup> And they avoid the complexity and political difficulties of equity stakes. Loan terms and conditions can be varied depending on the bailout, for example by making loan terms concessional or making payback profit-contingent.<sup>221</sup>

## 4.6 Competition regulators need to keep their eyes on the long term

Responses by businesses to the short-term hit from coronavirus can also pose longer-term economic risks if markets become more concentrated and less competitive. The ACCC and other regulators

should continue to enforce competition laws robustly during the recovery period, with an eye to long-term market dynamics.

In the initial stages of the COVID-19 crisis, the ACCC received a rush of applications from firms seeking to coordinate their activities to help them through the crisis. Contracts, arrangements, or understandings between competing firms are illegal under the Competition and Consumer Act 2010. But the ACCC has the power to authorise otherwise illegal conduct on the grounds that the public benefits from the conduct outweigh the public detriment.<sup>222</sup>

The ACCC has provided more than 20 interim authorisations<sup>223</sup> for coordination in response to the fallout from the coronavirus lockdown. These include supermarkets cooperating on grocery supply to manage panic buying,<sup>224</sup> health insurance companies including coverage for COVID-19 treatments and tele-health services in their policies,<sup>225</sup> banks coordinating financial relief and assistance for their customers,<sup>226</sup> and private and public hospitals coordinating to manage hospital capacity.<sup>227</sup>

These decisions were appropriate given the highly unusual nature of the pandemic and the public interest case for firms to coordinate to contribute to the health response or address specific market disruptions. ACCC Chair Rod Sims likened the need for coordination to a ‘war response’.<sup>228</sup> Similar arrangements have been endorsed by competition authorities around the world.<sup>229</sup>

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218. Wilkes (2020, p. 30).

219. Triggs (2020).

220. Wilkes (2020, p. 30).

221. Triggs (2020).

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222. ACCC (2020a).

223. ACCC (2020b).

224. ACCC (2020c).

225. ACCC (2020d).

226. ACCC (2020e).

227. ACCC (2020f).

228. Butler (2020).

229. OECD (2020c).

The ACCC has signalled the authorisations will be revoked after the crisis has passed and things ‘go back to normal’.<sup>230</sup> Draft determinations on the authorisations are expected by the end of July, and final determinations by September. However, these authorisations should be discontinued as soon as the public benefit case begins to diminish.<sup>231</sup> The ACCC has already taken steps to scale back the authorisation for supermarkets, given some of the supply issues from panic buying have dissipated. Arguably, the same case could be made for hospitals authorisations, given the expected rush of coronavirus patients has also dissipated.

The longer coordination is officially sanctioned, the greater the risks that competitors glean information, or form agreements or understandings that reduce competition between them in the longer term.

Shifts in market structure and behaviour are inevitable in the recovery phase and these will also need to be strongly policed by the ACCC and other regulators to avoid locking in long-term harm to consumers.

There will be more merger activity in the next six months, as firms that have survived look to boost shareholder value by taking over weak or failing competitors. The ACCC has rightly signalled it will look beyond the short-term effects of the pandemic and consider the long-term impacts on market structures and competition from any proposed mergers.<sup>232</sup>

The ‘failing firm’ defence – that a merger would not be anti-competitive because the firm would otherwise fail – is often advanced by merger parties and even more so during economic downturns.<sup>233</sup> The ACCC,

like other competition regulators,<sup>234</sup> entertains these arguments only in a very narrow set of circumstances.<sup>235</sup> It should not lower the bar because of current economic dislocation: the decisions it makes now will have ramifications for market structures and competition for many years to come.

The risks of other forms of anti-competitive conduct also loom larger during an economic downturn. Firms are more likely to risk trying to form a cartel when they face falling prices triggered by reduced demand.<sup>236</sup> Pre-crisis prices can provide a focal point for coordination – with firms signalling a return to more ‘normal’ margins.

This is a greater risk in an environment where the regulators are constrained in their investigations. Some of the regular tools – undercover visits, dawn raids, witness interviews under oath – may be difficult in the short-term because of social distancing restrictions.<sup>237</sup>

Similarly there is a risk that firms with market power will use the downturn and the weakness of competitors as a chance to cement their dominance. The ACCC has already warned Qantas that it will take an unfavourable view of strategies such as swamping airline routes to artificially push down prices, or locking in exclusive deals with airports and suppliers to make it harder for the buyer of Virgin to gain a strong foothold in the market.<sup>238</sup>

The ACCC should continue to take a strong line on all forms of conduct that breach the Competition and Consumer Act, regardless of the short-term economic outlook. Robust competition and well-functioning markets provide a much better chance of a strong economic recovery.

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230. Butler (2020).

231. OECD (2020c).

232. Samios and Danckert (2020).

233. Noble et al (2020); and OECD (2020d).

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234. OECD (2020d).

235. ACCC (2008, p. 12).

236. Baer (2020).

237. OECD (2020e).

238. Khadem (2020).

## 5 Getting back to work

The COVID-19 crisis has thrown many hundreds of thousands of Australians out of work. The unemployment rate, adjusted to include people ‘stood down’ and not working any hours, reached 11.7 per cent in April, the highest since the Great Depression, before falling to 9.5 per cent in May.

As Australia emerges from the crisis, getting people back to work will be critical. As noted in Chapter 3, the more rapid the economic recovery, the quicker many Australians can do so. This is why avoiding a sudden withdrawal of existing fiscal supports such as JobKeeper, and ramping up traditional fiscal stimulus as those supports gradually come off, will be critical.

Nonetheless unemployment is likely to remain high for an extended period, making repair to Australia’s frayed safety net even more urgent. Australia’s unemployment benefit was inadequate before the crisis; the crisis highlighted its inadequacy. As JobKeeper is phased down from December, the temporary Coronavirus Supplement paid to unemployed Australians should be extended into 2021. After that, as it is phased down gradually, the permanent rate of the JobSeeker Payment should rise. The new permanent rate of JobSeeker should also be benchmarked to growth in wages, rather than inflation, to ensure it keeps pace with community living standards.

Childcare is crucial to enabling many Australians, particularly women, to engage in paid work. As the free childcare arrangements put in place during the crisis are unwound, a higher Child Care Subsidy should be introduced with a simpler, flatter taper. Under the previous system, childcare costs were still very high by international standards, discouraging secondary earners (usually women) from taking on more paid work.

COVID-19 has upended how Australians get to work, and what the workplace looks like. Public transport – particularly during peak periods – has become less attractive to commuters, and a greater proportion of commuters are likely to drive or cycle. Many more employees have worked remotely more often and their employers are likely to encourage them to continue to do so, at least some of the time. Governments should support our cities and workplaces to adapt to the changing world of work.

### 5.1 Looking after the unemployed

During the COVID-19 crisis, the Federal Government has provided substantial additional support to unemployed people in the form of the \$275-a-week Coronavirus Supplement. But the supplement is scheduled to be withdrawn in late September (Chapter 3). On current policy settings, unemployed Australians will suffer a sharp drop in their incomes from September, from the temporarily higher JobSeeker payment (\$557.85 a week) to the permanent rate of JobSeeker (just \$287.25 a week).<sup>239</sup> The gross incomes of other laid-off workers will fall by almost two-thirds, from the JobKeeper payment (\$750 a week), scheduled to be abolished from September, to JobSeeker (just \$287.25 a week).

Unemployment has jumped already, and it is forecast to go much higher. Long-term problems with the design of support for the unemployed are now even more urgent questions than ever.

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239. DSS (2020a). Includes Energy Supplement of \$4.40 per week. Fortnightly amounts have been converted to weekly.

### 5.1.1 The temporary higher JobSeeker rate should be withdrawn gradually

As discussed in Chapter 4, the JobKeeper wage subsidy should be extended for an additional three months through to the end of December for the workers of businesses that still fall below the turnover recovery threshold in September. Similarly, the Coronavirus Supplement should be phased down gradually over three months, starting from January 2021. Phasing down the supplement in this way would cost about \$10 billion to \$15 billion in 2020-21.<sup>240</sup> The schedule for the gradual phase out of the Coronavirus Supplement from early 2021 should also be revised if unemployment remains substantially higher than expected at the end of 2020.

### 5.1.2 The permanent JobSeeker rate should rise

The permanent rate of JobSeeker should be increased by at least \$100 a week for singles.<sup>241</sup> The base JobSeeker payment rate of \$287.25 a week<sup>242</sup> is so low that the payment is not adequately fulfilling its

240. This assumes the full supplement is extended to the end of December 2020, then reduced to \$212.50 a week in January 2021, \$150 in February, and \$100 in March. The supplement then ceases; a higher base JobSeeker payment is in place from April. If the number of supplement recipients remains constant at 2.3 million over the phase-out period (based on a DSS projection for September: DSS (2020b)), the cost would be about \$15 billion. This is likely to be an over-estimate, because unemployment is projected to fall over the period. However, individuals transitioning from JobKeeper may add to the recipient numbers, so there is some uncertainty about the cost. Note that not all supplement recipients are JobSeeker recipients.

241. Coates and Nolan (2020) previously proposed an increase in the then-named Newstart payment of at least \$75 per week. However the new analysis in this chapter suggests that the costs of increasing the rate of JobSeeker, in terms of reduced job search effort, appear relatively small at the levels of increase in the payment considered.

242. The payment rate is \$565.70 a fortnight, plus an Energy Supplement of \$8.80. Figures in this section are converted to their weekly equivalents. Figures pertain to single adults, unless otherwise stated.

core function of providing a minimum, adequate income. People on unemployment benefits have an income below the poverty line – using any reasonable definition of that line – as well as heightened levels of financial deprivation and stress.

An increase of about \$180 per week would be needed to lift the JobSeeker payment above the poverty line (See Figure 5.3 on page 61). This would also lift unemployment benefits to about the same level as the single Age Pension. The argument to lift the payment by this amount is compelling.

But an increase of more than \$126 per week would mean that a full-time worker at the minimum wage would be entitled to receive unemployment benefits.<sup>243</sup> This would represent a significant change to the nature of the payment. It would also cost a substantial amount of money and would raise questions about whether the incentive to obtain employment would remain strong enough.

The Henry Review also concluded that some gap between the pension and unemployment benefits could be justified given the different nature of the payments.<sup>244</sup>

The increase we recommend – of at least \$100 a week – should not be seen as the final step to fixing Australia's income support system; rather, this is the minimum that is necessary to ensure some basic level of adequacy pending broader reform. An increase of \$100 a week would result in an unemployment benefit at a similar level relative to

243. This would be the case if the current benefit withdrawal thresholds and tapers were to remain unchanged.

244. The Henry Review noted that 'some difference in the level of payments can be justified on the basis of differing needs and presenting different incentives to different groups. If a person is expected to take immediate full-time work whenever they can, it is important that they are much better off taking that work. If a person is never expected to work at all, then incentives for them to do so are irrelevant': Henry et al (Part 2, Vol. 2 2010, p. 501).

the full-time wages in 1994, but somewhat higher relative to full-time wages in July 2000, when the benefit was increased as part of GST compensation (see Figure 5.3 on page 61).

KPMG has also called for a \$100 a week rise.<sup>245</sup> Social policy expert, Professor Peter Whiteford has called for the payment to increase by \$185.<sup>246</sup> The Small Business Ombudsman has called for the base rate of JobSeeker to rise, as has the Australian Industry Group, and the Council of Small Business Organisations Australia.<sup>247</sup> The BCA recommends increasing JobSeeker to between 75 and 90 per cent of the Age Pension;<sup>248</sup> our recommendation would lift it to around 82 per cent of the pension.<sup>249</sup>

We also recommend a 40 per cent increase in Commonwealth Rent Assistance, which would raise the maximum weekly Rent Assistance payment for a single person by \$28, costing around \$1.5 billion a year.<sup>250</sup> Although a little less than half of JobSeeker recipients also receive Rent Assistance,<sup>251</sup> the two recommendations taken together would represent a substantial increase in the incomes of unemployed renters.

### A higher JobSeeker payment imposes material costs

The Parliamentary Budget Office (PBO) recently costed several proposals for higher JobSeeker payments of a similar magnitude as we recommend. One option – increasing the payment by \$95 a week

– was estimated to cost \$4.9 billion in 2021-22. This estimate was produced before the spike in unemployment induced by COVID-19 – the fiscal cost will be higher if there are more recipients. We expect that, given the increase in unemployment due to the crisis, the full-year cost of an increase to JobSeeker of \$100 a week would be about \$7.5 billion in 2021-22.<sup>252</sup>

In the short-run, the extra spending on JobSeeker will add to fiscal stimulus. But a permanently higher rate of JobSeeker also creates long-term fiscal costs. Government needs to consider how to finance them when the budget is back on track.<sup>253</sup>

### JobSeeker is inadequate compared to common measures of income poverty

Australia has no official poverty line.<sup>254</sup> A line commonly used in advanced economies is the ‘relative poverty line’, defined as half of median income.<sup>255</sup> The relative poverty line in 2017-18, the latest year for which data is available, was \$450 a week<sup>256</sup> – updated to the first quarter of 2020, the poverty line is \$466.11 a week.<sup>257</sup> The Henderson poverty line, an historically-prominent measure in Australia, is \$542.92

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245. KPMG (2019).

246. Whiteford (2020).

247. Karp (2020c).

248. Ibid.

249. Calculation includes Energy and Pension Supplements.

250. See Coates and Nolan (2020) and Daley et al (2018a). Costing revised up to reflect greater eligibility for rent assistance given higher unemployment over next few years.

251. Grattan analysis of ABS (2019c).

252. On the expectation that the number of recipients over 2021-22 will be about 20 per cent higher than anticipated by the PBO at the time it did its pre-COVID costing, and that a larger proportion of recipients will receive the full benefit. Figure is approximate. Does not include the cost of a phased reduction in the Coronavirus Supplement. If additional stimulus is not disbursed, the unemployment rate may remain higher for longer, which would increase the fiscal cost of a higher Jobseeker payment.

253. For a range of budget saving ideas, see: Daley et al (2019) and Section 3.7 on page 38.

254. Senate Community Affairs References Committee (2020, p. 24).

255. It is based on median income, after taxes and transfers, adjusted for household size.

256. ABS (2019f).

257. Indexed in line with household disposable income per capita: Grattan calculation based on ABS (2020g).



a week.<sup>258</sup> A single adult eligible for full JobSeeker receives \$287.25 a week. This is \$178.86 a week below the relative poverty line. Figure 5.1 shows the size of the gap between the poverty lines and the income of a single unemployed person in Australia. This gap has grown strikingly over the past 20 years.

There are other indications that JobSeeker is inadequate. Budget standards developed by the Social Policy Research Centre at UNSW estimate that a single adult, living alone, would have needed \$459.90 a week in mid-2019 to meet basic consumption needs.<sup>259</sup> This is slightly above the relative poverty line – well above the income of a person on JobSeeker.

Further confirmation that JobSeeker is inadequate comes from data on the financial stress suffered by households who receive allowances. About two-thirds (65 per cent) of households that rely on allowances such as JobSeeker report suffering at least three forms of financial stress. This compares to only 27 per cent of pensioner households and 12 per cent of working households. The proportion of allowance-dependent households suffering a high degree of financial stress has risen from about half – 49 per cent – in 2003.<sup>260</sup>

The single rate of JobSeeker is only 55 per cent of the amount paid to an unemployed couple. This relativity does not adequately reflect the extra cost of living alone compared to living with a partner. Single pensioners receive 66 per cent of the amount paid to pensioner couples, a relativity that was chosen after an extensive review.<sup>261</sup> The single rate of JobSeeker would need to rise by \$56 a week for the

258. Melbourne Institute (2020a). The Henderson poverty line was first set by a review into poverty in Australia in the 1970s, led by Professor Ronald Henderson (Henderson et al (1975)). The line is updated each quarter by the Melbourne Institute by inflating the original line by changes in household disposable income.

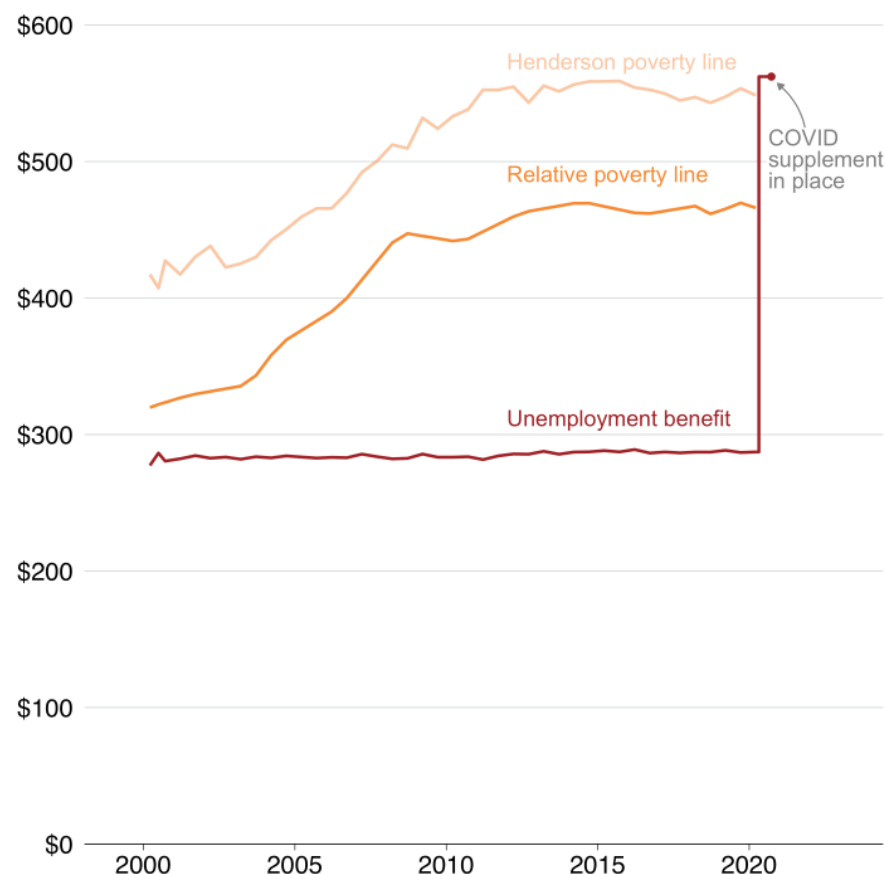
259. Senate Community Affairs References Committee (2020, p. 28).

260. Phillips et al (2019).

261. Harmer (2009).

**Figure 5.1: The unemployment benefit has fallen further and further below the poverty line**

Poverty lines and unemployment benefits per week, inflation-adjusted 2020 dollars



Notes: Unemployment benefit includes Energy Supplement. Poverty lines indexed to March 2020 using household disposable income per capita. Adjusted for inflation using the consumer price index. Unemployment benefits have at various times been called the unemployment benefit, the Job Search allowance, the Newstart Allowance, and the JobSeeker payment.

Source: Grattan analysis based on Melbourne Institute (2020a), ABS (2019f), ABS (2020i), DSS (2020a) and ABS (2020g).

payment to have the same relativity between singles and couples as pensioners receive.

The Henry Review recommended increasing the unemployment benefit and other allowances for single people,<sup>262</sup> because ‘a single working-age recipient living alone needs much the same proportion of working age recipient couple’s payment as a single age pensioner does of an age pensioner couple’s payment’.<sup>263</sup>

### JobSeeker has not kept pace with improvements in community living standards

Figure 5.2 on the following page shows that the value of the unemployment benefit – including Rent Assistance – has declined sharply relative to median and minimum wages, and to the pension for single people. Since 2000, the unemployment benefit has declined from about 25 per cent of median full-time wages to about 20 per cent. Restoring unemployment benefits to the same proportion of the median wage as in July 2000, after the introduction of the GST and in the middle of the Howard era, would take about \$58 a week.

Figure 5.3 on the next page shows the amount of money that would be required to lift the incomes of unemployed people up to a range of benchmarks. For example, it would take \$183 to lift unemployment benefits to equal the pension, and \$179 to equal the relative poverty line.<sup>264</sup>

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262. Henry et al (2010, p. 521).

263. Ibid (p. 511).

264. These calculations include the Energy and Pension Supplements, where applicable. They do not include Rent Assistance. Whiteford (2020) calculates that it would take \$185 a week to lift unemployment benefits to the same level as the single pension, taking all supplements into account.

### JobSeeker is among the least generous unemployment benefits in the OECD

Australia’s unemployment benefit is worth just 27 per cent of the average wage. No OECD country pays newly-unemployed people a smaller benefit, as a proportion of the country’s average wage, as shown in Figure 5.4 on page 62.

Unlike most OECD countries, Australia pays the same unemployment benefit regardless of how long a person has been unemployed – in most countries, benefits decline for long-term unemployed people. But even for long-term unemployed people, Australia’s benefit is below average for OECD countries.

### The incentive to find employment would still be strong with a higher JobSeeker

It is generally accepted that when unemployment benefits are very high, relative to wages, recipients have less financial incentive to seek work.<sup>265</sup> But some recent studies have found that increasing the generosity of unemployment benefits does not necessarily reduce employment or efforts to find a job.<sup>266</sup> It is undoubtedly true that at some point the payment could get so high, relative to wages, that the incentive to seek employment would be low. But the current payment level is so low that even with a substantial increase, recipients would still have real incentives to find work. With a \$100 increase, JobSeeker would still be only around half (51.4 per cent) of the full-time

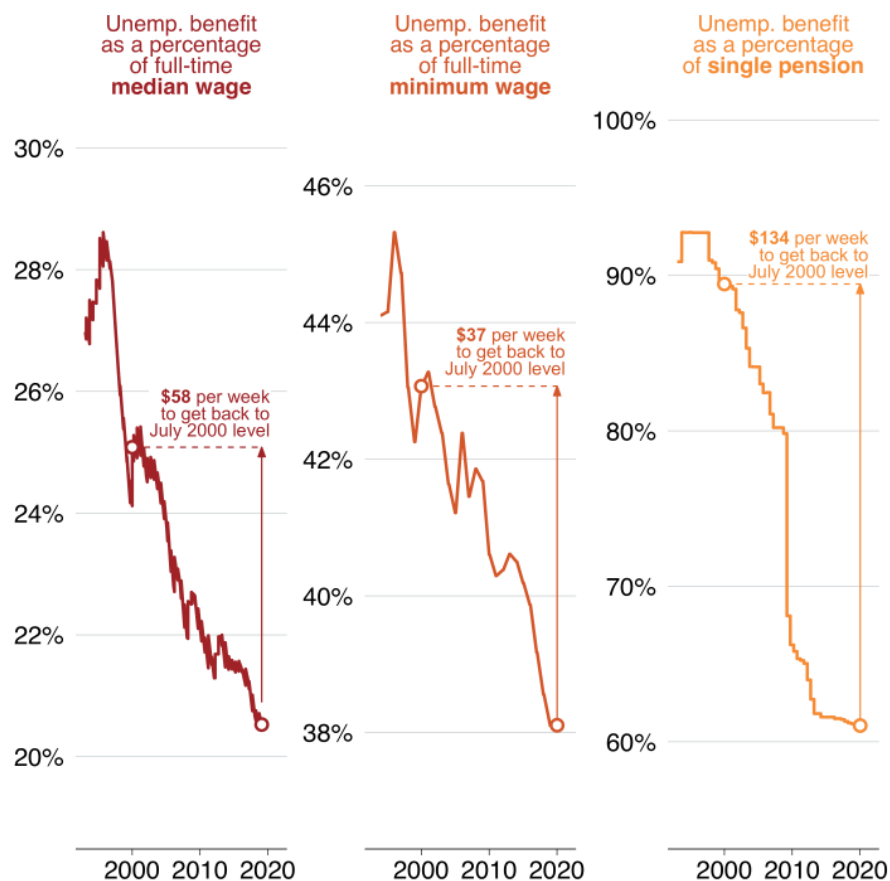
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265. For example, see overviews in Gruber (2005) and Krueger and Meyer (2002). Chetty (2008) finds that some of the increased unemployment duration that comes from a higher benefit level is welfare-enhancing.

266. Hussain et al (2020); and Boone et al (2016).

**Figure 5.2: A substantial increase to JobSeeker is needed to restore Howard-era relativities**

Unemployment benefit as a percentage of minimum and median full-time gross wages, and the single pension

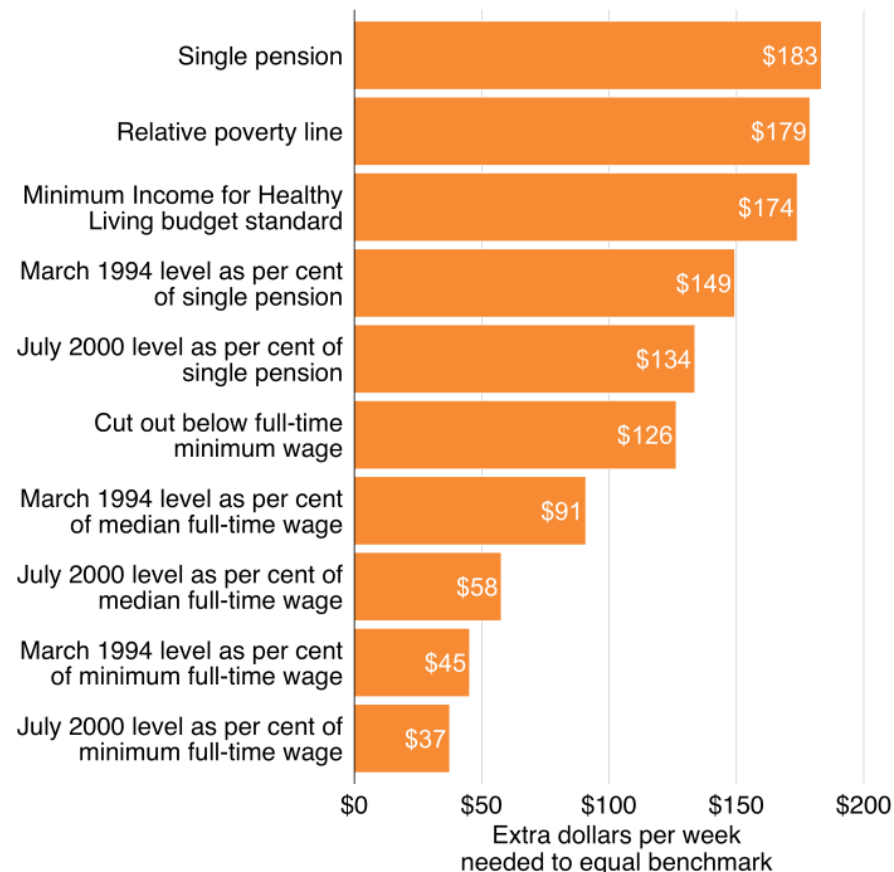


Note: Calculation includes Energy and Pension Supplements where applicable.

Source: Grattan analysis of ABS (2003), ABS (2019g), Bray (2013) and FWC (2020).

**Figure 5.3: A substantial increase in unemployment benefits is needed to hit most benchmarks**

Difference between unemployment benefits and benchmarks (\$ per week)



Notes: Includes Energy and Pension Supplements where applicable. Poverty line and budget standard updated to 2020 using household disposable income per capita.

Source: Grattan analysis of OECD (2020f), ABS (2003), ABS (2019g), ABS (2020g), Bray (2013) and FWC (2020).

minimum wage, meaning that an unemployed person would still have a substantial financial incentive to move into full-time work.<sup>267</sup>

The payment is also so low that it may *undermine* effective job search. The OECD has noted concerns that the low level of Newstart ‘raises issues about its effectiveness in providing sufficient support for those experiencing a job loss, or enabling someone to look for a suitable job’.<sup>268</sup>

Sub-par unemployment benefits can also lead to unemployed people taking jobs that are inappropriate for them – for example, jobs that require them to commute very long distances – which can often just lead to people ‘churning’ on and off unemployment benefits.

### A permanent higher rate of JobSeeker would help economic recovery

Increasing incomes for people relying on income support would help the economy. People would be better able to search for a job, and better equipped to commence employment.<sup>269</sup>

Increasing unemployment benefits would have positive macroeconomic benefits in some circumstances.<sup>270</sup> Unemployment benefits are an ‘automatic stabiliser’ – spending on them goes up when economic

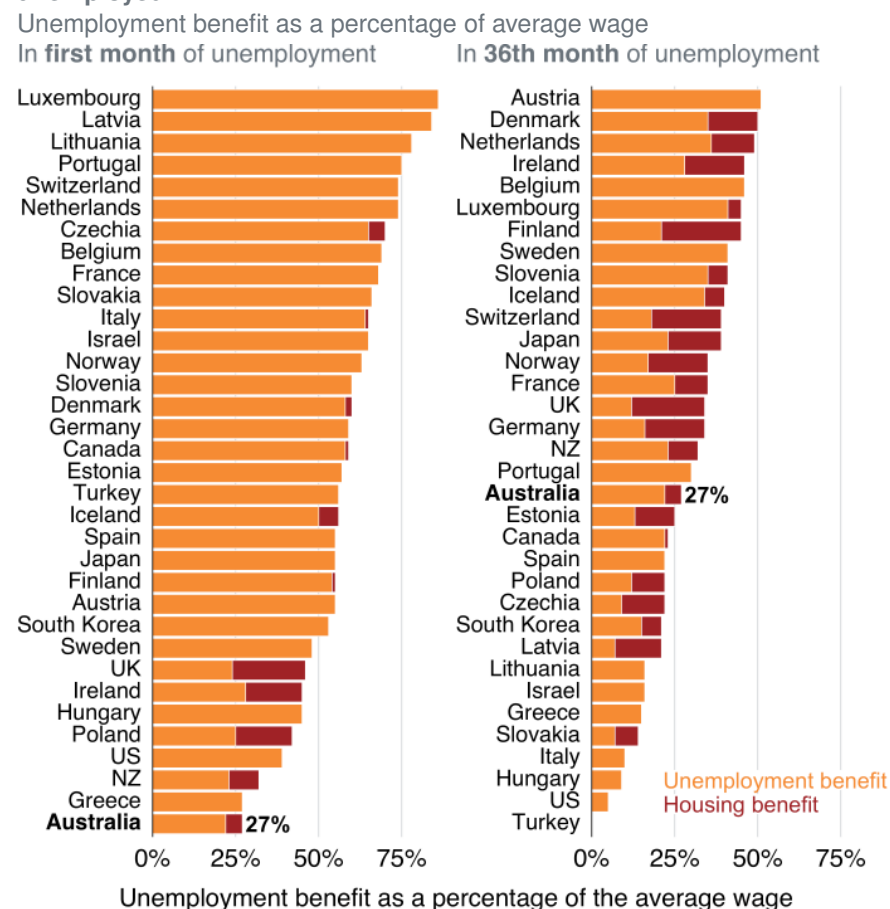
267. Grattan calculation based on National Minimum Wage of \$753.80, to take effect from 1 July 2020. Increases to some award wages will occur later in the financial year.

268. OECD (2010, pp. 127–28). The 2020 Senate inquiry into the adequacy of Newstart similarly found that ‘the income support system itself is acting as a key barrier to employment because of the inadequate payment rates that force people into poverty’: Senate Community Affairs References Committee (2020, p. xviii). In its submission to the inquiry, the Business Council of Australia noted that ‘job seeking is not costless and should be accessible. If a bus fare or a collared shirt become unaffordable, then getting to job interviews and presenting as a credible employee may move out of reach’: BCA (2019, p. 4).

269. Deloitte Access Economics (2018).

270. Boone et al (2016) show that a moderate fiscal multiplier from more generous unemployment benefits is sufficient to offset any reduction in labour supply.

**Figure 5.4: Australia’s unemployment benefit is the lowest in the OECD for newly-unemployed people and is below average for the long-term unemployed**



Note: Figures are from 2018-19; they do not include changes to benefit systems implemented in response to the COVID-19 crisis.

Source: OECD (2020f).

conditions deteriorate, and falls when conditions improve. This helps to smooth the business cycle, and does so without the decision and implementation lags inherent to many forms of discretionary fiscal policy, such as infrastructure spending.

### 5.1.3 JobSeeker should be benchmarked to increases in wages, not inflation

Pensions in Australia – the Age Pension and the Disability Support Pension – are increased in line with wages.<sup>271</sup> This ensures that living standards of people who rely on pensions rise in line with the living standards of the general Australian community. Allowances, such as the JobSeeker payment, are adjusted only in line with changes in the cost of living, as measured by the Consumer Price Index (CPI).

The first problem with this approach is that the CPI understates the change in the cost of living for allowance recipients.<sup>272</sup> The second, more important, problem is that CPI indexation means that a person on the unemployment benefit falls further and further behind other members of the community, including pensioners. This also creates incentives for people to seek to claim higher-paying disability pensions.<sup>273</sup> The JobSeeker payment should be indexed to wages in the same manner as the Age Pension.<sup>274</sup>

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271. The maximum single basic pension is effectively benchmarked to about 27.7 per cent of male total average weekly earnings; see DSS (2020a, Section 5.1.8.50).

272. The ABS reports a measure of the cost of living specific to benefit recipients. Between 1998 and 2020, the cost of living for government transfer recipients rose at an average rate of 2.8 per cent a year; over the same period, the CPI rose by 2.55 per cent. Grattan calculations based on ABS (2020p) and ABS (2020i).

273. Henry et al (2010, p. 505).

274. This would mean benchmarking JobSeeker to a certain percentage of Male Total Average Weekly Earnings (MTAWE). A future review of the income support system should consider the appropriate indexation arrangements for allowances and pensions, which should be common across payment types.

Calls for unemployment benefits to be indexed to something other than CPI inflation are not new. The Henderson Inquiry recommended in 1975 that payments be indexed to some measure of community living standards, suggesting either average earnings or GDP per capita.<sup>275</sup>

The Henry Review said some difference between the payment rate for pensions and allowances was justifiable, on the grounds that incentive effects are irrelevant for pension recipients who are not expected to work. But it also said:

Harder to justify is the fact that rates of pension and allowances are not merely different, but the gap between them is widening. . . If the current indexation arrangements remain in place it is likely that by 2040 a single pensioner would be paid more than twice as much as a single unemployed person. A continuous decline in Newstart Allowance against community standards would have major implications for payment adequacy and the coherence. . . of the income support system.<sup>276</sup>

The 2015 McClure Review also recommended that indexation arrangements be common across payment types – it recommended a six-monthly automatic cost-of-living adjustment, along with a ‘community living standards adjustment following a periodic review’ at least every four years.<sup>277</sup>

### 5.1.4 Access to JobSeeker should be less tightly restricted

During the COVID-19 crisis, the Federal Government acted quickly to broaden access to JobSeeker. This broader access should be extended in time, and the Government should consider permanently enabling more unemployed Australians to get timely access to benefits.

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275. The Henderson report stated that ‘it is most important that pensions and benefits be updated frequently and regularly by an amount that prevents the beneficiaries falling behind the rest of the population’: Henderson et al (1975, p. 67).

276. Henry et al (2010, p. 501).

277. Reference Group on Welfare Reform to the Minister for Social Services (2015, p. 18).

Under the liquid assets waiting period, applicants for JobSeeker must wait longer to receive their first payment if they have cash on hand.<sup>278</sup> The extra waiting period can be up to 13 weeks.<sup>279</sup> The liquid assets waiting period was suspended from 25 March, meaning that people with cash on hand no longer have to wait longer to receive unemployment benefits. The suspension should continue at least until JobKeeper and the Coronavirus Supplement have been phased out.

After the crisis, the waiting period should be reduced to no more than six weeks. The arrangements treat financial assets differently than other assets (for example, housing equity does not count towards the test) and undermine the insurance function of unemployment benefits.

During the crisis, the Government also substantially loosened the partner income test. Previously, each extra dollar earned by a JobSeeker recipient's partner would reduce the recipient's payment by 60 cents. Now, the payment only reduces by 25 cents. This means that people can receive a (partial) JobSeeker payment if their partner earns up to \$3068 per fortnight.

The loosened partner income test has created some problems. The interaction of various taper rates can mean that people in some circumstances face disincentives to earn extra income. The current arrangements are not a long-term solution. But the Government should keep the current, more generous partner income test in place until the Coronavirus Supplement is withdrawn.

Mutual obligation arrangements, too, were waived during the acute phase of the crisis, though they were re-introduced in limited form from 9 June.<sup>280</sup> Job Plan requirements should remain voluntary while the

Coronavirus Supplement is in place. Mutual obligation arrangements post-COVID should be reviewed.

## 5.2 Making childcare more affordable

Free childcare has been a huge support for working parents through the crisis. The Federal Government's short-term relief package, announced in April,<sup>281</sup> has provided childcare centres with a guaranteed stream of income and support for wage costs, helping them to stay open through the crisis.

For working parents, this meant their usual childcare centre remained available to them, and even if they chose to keep their children at home, they were able to keep their childcare place, at no charge.

The Government's package no doubt enabled many parents to stay in the workforce over the past few months, even at reduced hours.<sup>282</sup>

But the package was always intended to be temporary,<sup>283</sup> and is now set to wrap up on 12 July, with some additional support measures for centres continuing until early October.<sup>284</sup>

Maintaining the crisis arrangements indefinitely was never an option: the Government has been paying childcare centres only half their normal revenue, and centres were not allowed to charge parents. The situation has only been tenable because the Government's temporary JobKeeper payment has been filling some of the gap by covering most of the wages cost for eligible centres.

But a sudden stop to the scheme in July is likely to be tough for many parents, childcare centres, and childcare workers. Families who have held their jobs through the crisis should be able to manage. But families

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278. 'Liquid assets' include cash, bank deposits, shares, and a range of other financial assets: DSS (2020a, Section 1.1.L.50).

279. Services Australia (2020).

280. Australian Government (2020).

281. Morrison and Tehan (2020).

282. e.g. The Front Project (2020) and Duffy et al (2020).

283. Klapdor (2020).

284. Tehan (2020a).



working fewer hours, or where one parent has lost their job, may not be able to afford to keep their childcare place.

If demand for childcare declines, many centres could fall below the high occupancy levels required to stay afloat, which could lead centres to lay off workers and/or close their doors. Parents still working would then need to find new care or drop out of work themselves. It's a vicious cycle.

The move away from free childcare will need to be carefully managed, and the pre-crisis scheme is not necessarily the ideal end-state. Even before the crisis, Australia had some of the highest out-of-pocket childcare costs among OECD countries.<sup>285</sup> The high cost of childcare doesn't just drain family incomes, it has a big impact on workforce participation, particularly for women.

Childcare costs interact with other elements of our tax and benefit system to make additional hours of paid work financially unattractive for many 'second earners' (usually women).

Figure 5.5 on the next page shows the 'workforce disincentive rate' – the proportion of income from an additional day's work that is lost through higher taxes, reduced family payments, and childcare costs – for second earners in a couple. For example, consider a household with two young children where both parents would earn \$60,000 a year if working full time. Dad works full-time and mum three days a week. If mum decided to take on an extra day, she would lose more than 90 per cent of the additional pay for that fourth day in additional childcare costs, tax, and reduced family payments. That leaves her working for

about \$2 an hour on her fourth day – and for nothing on her fifth day. Is it any wonder that the '1.5 earner model' – where dad works full-time and mum part-time – has become the norm in Australia?

The biggest contributor to these high workforce disincentive rates is the cost of childcare.<sup>286</sup> Returning to the pre-crisis scheme won't solve these problems. And reducing barriers to work is likely to be more important than ever as Australia rebuilds post-pandemic.

Instead of reverting to the pre-crisis scheme, the Government should move to a higher, simpler Child Care Subsidy. A subsidy of 95 per cent of childcare costs for low-income families, tapering down slowly as family income increases, would cost about \$5 billion more than the pre-crisis scheme (Figure 5.6 on the following page).

A higher, simpler subsidy would lessen the shock to family budgets as parents start paying for childcare again. In addition to supporting the return of existing demand, a higher subsidy would improve incentives to work – supporting new demand. It would enable many women who want to increase their paid work to do so, supporting the post-crisis recovery and boosting GDP by about \$11 billion a year in the medium term through higher workforce participation.

As part of the transition arrangements, the Government is relaxing the activity test for some families until October.<sup>287</sup> This gives parents who have recently lost work access to some subsidised care, and helps families who are looking for work and/or getting fewer work hours in the wake of the crisis.<sup>288</sup> It may also help to boost childcare demand at a time when centres may be struggling to maintain sufficient occupancy.

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285. Full-time net childcare costs absorb about a quarter of household income for a typical couple with two young children in Australia, compared to the OECD average of 11 per cent: OECD (2019). Even with government subsidies of up to 85 per cent of the cost, a low-income family receiving the maximum subsidy still pays about \$9,000 a year to have two children in full-time care. For a family where each parent earns \$80,000, childcare costs are about \$26,000 a year.

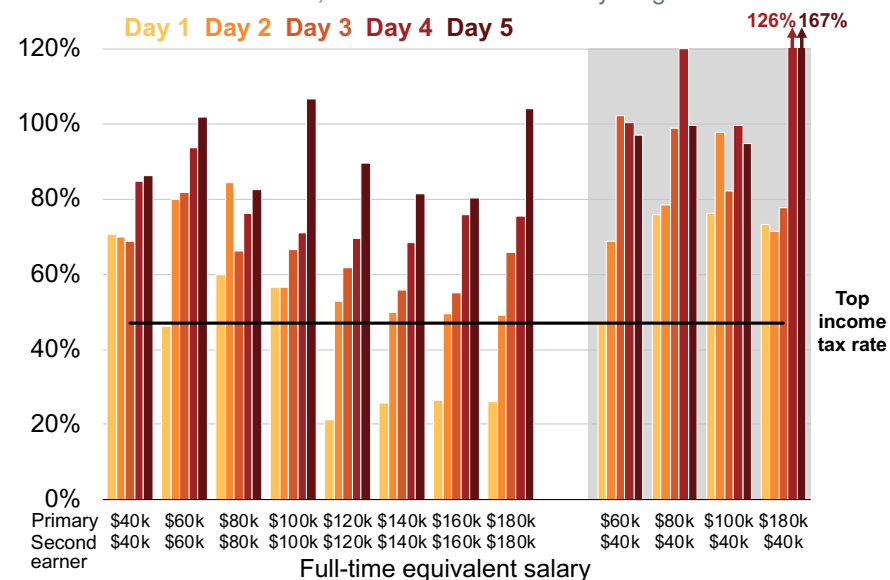
286. D. Wood et al (2020e).

287. Tehan (2020a). Normally access to the Child Care Subsidy requires both parents to complete a certain number of hours of approved activities, such as paid work, study, or volunteering: Department of Education Skills and Employment (2020).

288. Access to quality early childhood education and care also has benefits for child development, particularly for children from disadvantaged backgrounds: Tayler (2016); O'Connell et al (2016, p. 8); PC (2014, p. 148).

**Figure 5.5: Disincentives to work more are very high for second earners in couple families**

Workforce disincentive rate, second earner with two young children

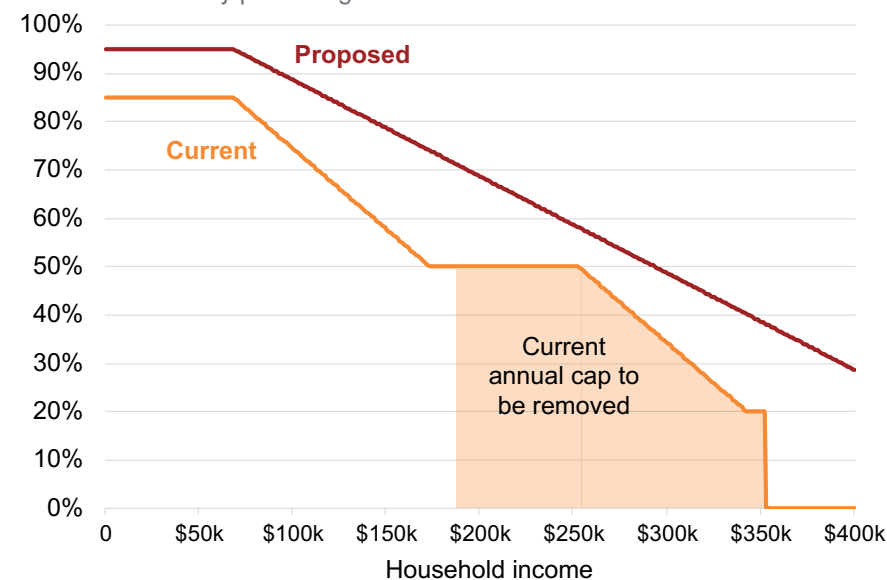


Notes: The workforce disincentive rate (WDR) represents the financial disincentive from the second earner working an additional day. Primary earner works full-time. Shaded area shows cameos of a primary earner with a higher hourly rate than the second earner. Two children, both require childcare. Every day of work for the second earner results in exactly one day of approved childcare. The cost of childcare is assumed to be \$110 a day. Renting, paying sufficient rent to get maximum Commonwealth Rent Assistance if qualifying under income test.

Source: Grattan analysis based on the 'daily rate' structure of Stewart (2018) and Ingles and Plunkett (2016).

**Figure 5.6: We recommend a higher Child Care Subsidy for everyone, with a flatter taper**

Child Care Subsidy percentage



Source: Grattan analysis.

Temporarily upending the Child Care Subsidy in response to the crisis provides a rare opportunity to improve the scheme. The Government's transition plan for childcare hinges on whether families can afford care at this time. Given that childcare costs were already a major constraint on workforce participation and family budgets pre-crisis, the Government should seize this chance to make childcare more affordable – which would boost economic growth in both the short and long term.

### 5.3 Getting to work

Australian commuters tend to drive. Before the pandemic, 64 per cent of journeys to work in Sydney were by private vehicle or taxi. Melbourne and Brisbane had even more, at 72 per cent and 76 per cent.<sup>289</sup> In large part, people were driving because most workplaces are highly dispersed across the major cities; only 15 per cent of Sydney and Melbourne's jobs are in the centre, and just 12 per cent of Brisbane's.<sup>290</sup> People drive because it's faster, more convenient, and they often have free parking when they get to work.

The CBDs are a different story. Before the pandemic, most CBD commuters took public transport: 77 per cent in Sydney, 65 per cent in Melbourne, and 61 per cent in Brisbane.<sup>291</sup>

Public transport is all about the efficient movement of large numbers of people – especially if they're headed to the CBD – an objective that's incompatible with social distancing.<sup>292</sup> Given this fundamental

incompatibility, what can governments do to make commuting work as well as possible? There are four spheres where they can act.

#### 5.3.1 Public transport needs distancing and hygiene measures

For those people who do take public transport, governments should make it as safe as possible. There are two aspects to this: social distancing, and hygiene measures. Social distancing on public transport is already in place in some parts of Australia; Sydney, for example, is limiting the number of passengers on a bus to 12 and in a train carriage to 32,<sup>293</sup> and is prepared to enforce these limits if necessary.<sup>294</sup>

Some jurisdictions are marking or removing seats to guide passengers on crowding limits, permitting bus boarding via the back door only, and installing full barriers between the driver and passengers.

State governments can, if needed, adopt some of the more stringent measures in use overseas. These range from issuing permits for peak-period travel, as in Paris,<sup>295</sup> to having staff on platforms to enforce distancing and mask-wearing, as in New York and Delhi,<sup>296</sup> to a reservation system for the Beijing subway.<sup>297</sup>

Hygiene measures are important to minimise the risks. As well as more frequent cleaning and sanitising of vehicles, many cities are modifying vehicles to minimise the number of high-touch points, such as door handles and card readers. Just as in shops and other businesses, many cities are installing hand-wash stations. It's common, particularly in Asian cities, to require people to wear masks on public transport, and some cities have temperature checks for everyone entering a station.

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289. Terrill et al (2018, p. 31).

290. Ibid (pp. 14–16).

291. ABS (2017); Sydney CBD defined as 'Sydney – Haymarket – The Rocks' SA2. Melbourne CBD defined as 'Melbourne', 'Docklands', and 'Southbank' SA2s. Brisbane CBD defined as 'Brisbane City' SA2. 'Public transport' includes the ABS categories 'Train', 'Bus', 'Ferry', and 'Tram'. The categories 'Worked at home', 'Did not go to work', and 'Not stated' are excluded from denominator.

292. Bi et al (2020).

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293. NSW Government (2020a).

294. Nguyen (2020).

295. The Local France (2020).

296. CBS New York (2020); and PTI (2020).

297. Zheng (2020).

All of these measures improve the safety of people who take public transport. There will be many, though, who seek other options.

### 5.3.2 Cyclists need protection from cars and trucks

Very few people cycled to work before the pandemic. Cycling and walking combined, known as ‘active transport’, accounted for just 4 per cent of journeys to work in Sydney and Melbourne, and between 2.7 per cent and 3.6 per cent in Brisbane, Perth, and Adelaide.<sup>298</sup>

But cycling has taken off around the world since the pandemic began. Not only that, but the wider availability of electric bikes means that even people who are unfit or don’t have shower facilities at work can cover reasonable distances on two wheels. Some people are going a step further and trying out electric skateboards and scooters, self-balancing roller skates, and unicycles.

The biggest barrier to cycling is that people don’t feel safe.<sup>299</sup> Governments should give priority to dedicated cycle lanes or paths, physically separated from motorised traffic where possible.

Many cities around the world are doing this. In Seattle, 32km of streets have been closed to most cars to allow more space for walking and cycling;<sup>300</sup> in Paris, 50km of roadway will be designated for bikes after the lockdown ends;<sup>301</sup> in Milan, 35km of streets will feature expanded cycling and walking space by the time the city re-opens after lockdown;<sup>302</sup> in Bogotá, 76km of temporary bike lanes have been opened to reduce crowding on public transport;<sup>303</sup> and it’s a similar story in many other cities – including Melbourne.<sup>304</sup>

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298. Terrill et al (2018, pp. 32–34).

299. See, for example, City of Sydney (2018).

300. McAuley and Spolar (2020).

301. Yiming (2020).

302. Broom (2020).

303. Moloney (2020).

304. City of Melbourne (2020).

### 5.3.3 Drivers need parking right now, and an incentive to avoid peak periods

People already tended to prefer driving before the pandemic. Now, with the risk of contagion, the appeal of driving has only increased.

It’s understandable that at the moment people are avoiding public transport and taking instead to their cars. But it’s a disaster in the making, if governments do nothing to manage the growth in peak-period driving. The results could be slow and delayed trips, longer morning and afternoon peaks, less predictable trip times, and heightened danger for cyclists and pedestrians.

Right now, governments should make temporary provision for more drivers. That means temporary car parks, and free shuttles to the CBD and other destinations where large numbers of people congregate.

Governments also need to start planning now to make sure these measures remain temporary. There are two ways to do this. First, they should introduce congestion charging. Congestion charging has always been politically difficult, but the case has become stronger and more urgent.

There is nothing to stop state governments implementing a cordon charge around the CBD of the major capital cities, charging drivers a fee to enter the CBD in the morning peak and a fee to leave in the afternoon peak. This strategy does not prohibit any specific trip, but it does give an incentive for those people who can be flexible about when, where, or by what mode of transport they travel, to save money by doing so. A charge imposed just around the CBD has a positive effect that ripples out through the middle and even outer ring of the city.<sup>305</sup>

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305. Terrill et al (2019a, Chapter 1).

In the longer term, governments need to give higher priority to more space-efficient forms of transport. One way to do this is to narrow road lanes, and dedicate the reclaimed space to cycling and walking; there is significant scope for this strategy, given that Australian engineering guidelines recommend 3.5-metre lanes on urban arterials, even though lanes of 3.0 metres or even less would be ample in many situations. Narrower lanes appear to be no less safe than wider lanes in urban environments.<sup>306</sup>

Governments should also give people incentives to buy smaller cars. Australians choose large cars by international standards, and this results in more congestion, and a less safe environment for cyclists, pedestrians, and people in smaller cars. With smaller cars, parking bays would not need to be so large, and state and local governments could introduce dedicated lanes for micro and light vehicles.<sup>307</sup>

Making registration fees for larger cars much bigger than for smaller cars would send a clear signal to car buyers about the costs to other road users as well as themselves of choosing large vehicles for city driving.

#### 5.4 Rethinking flexible and remote work

Before the pandemic, very few people worked from home. In Sydney, Melbourne, and Brisbane, about 5 per cent did, and in Perth and Adelaide it was about 4 per cent. Although the numbers were small, the trend was up; the rate of working from home increased by about half a percentage point between 2011 and 2016 in each of Australia's five largest cities.<sup>308</sup>

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306. Terrill et al (2019b, p. 21).

307. Ibid (Chapter 2).

308. Terrill et al (2018, Chapter 4).

The reality remains that most jobs don't lend themselves to working from home. In the US, an estimated 37 per cent of jobs can be done from home,<sup>309</sup> and Australia is likely to be similar.

But COVID-19 has forced many workers and businesses to rethink how and where we work.<sup>310</sup> While working from home has no doubt been challenging for many, our new widespread capability for remote and flexible work should not be lost on the other side of this crisis.

Where flexible and remote work is feasible, it can have big long-term economic and social benefits – including enabling people to participate more fully in the workforce, and to live where they choose, not necessarily where they work.

More widespread access to remote and flexible work may make it possible for many people to work who otherwise might not – including parents, carers, people living in regional and remote areas, and people who are mobility-impaired.

Lack of flexibility in working hours is a common barrier for many parents, particularly mothers, with young or even school-aged children. More flexibility in working hours may enable families to take on more paid work or redistribute the paid and unpaid workloads to better suit their preferences. Flexible work has long been seen as a woman's domain, but this crisis gives us a rare opportunity to reset that social norm.<sup>311</sup>

As Australia's inner cities become increasingly expensive to live in, remote work may enable access to a more affordable and/or desirable lifestyle.

Flexible and remote work policies are largely the domain of employers (including governments in their capacity as employers). Many

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309. Dingel and Neiman (2020).

310. Newport (2020).

311. Alon et al (2020).

employers have now adopted working-from-home and telecommuting options for the first time. They should continue to offer their employees these options where possible beyond the crisis. Businesses that do will have access to a much larger talent pool and could boost employee productivity, satisfaction, and retention too.<sup>312</sup>

Policies on their own are not enough. Workplace culture and social expectations play a much bigger role in take-up of flexible and remote work – but this is one area where expectations may already have changed.

## 5.5 Industrial relations reform

Some commentators and interest groups have called for reform to industrial relations law as part of the recovery from COVID-19.<sup>313</sup> The Federal Government has convened discussions with unions and business groups regarding IR reform. If they can identify opportunities to improve aspects of the system in a consensual way, this would be worthwhile. But there is scant evidence that wholesale IR reform would deliver substantial economic benefits.

Previous Grattan work found that attempts to demonstrate a connection between IR reforms and changes in the rate of productivity growth were ‘inconclusive or unconvincing’.<sup>314</sup> The Productivity Commission came to a broadly similar conclusion when it examined the workplace relations system in 2015. It concluded that the existing system, which remains in place, ‘is not dysfunctional’, needing only ‘repair’ rather than ‘replacement’. The PC’s recommendations generally represented refinements of the existing system rather than wholesale change.<sup>315</sup>

Prominent labour economist Jeff Borland also says government should not pursue IR reform: ‘There is no basis for thinking that extensive reforms to the IR system can provide major efficiency benefits to the Australian economy.’<sup>316</sup> Borland also noted the large adjustment costs for business associated with major IR changes.

Substantial IR reform would be controversial. It would take significant time and political capital to implement. In the absence of compelling evidence that IR reform would deliver large overall economic benefits, policy makers should focus elsewhere.

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312. e.g. Costa et al (2006), McNall et al (2010), Hayman (2010), Nous (2018) and Parents at Work (2019).

313. For example: Banks (2020) and BCA (2020).

314. Daley et al (2012, p. 23).

315. PC (2015).

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316. Borland (2020c).



## 6 Keeping a cool head on economic policy

The fear of sustained mass unemployment has led to a renewed push for governments to fast-track road and rail projects, re-establish a larger manufacturing sector in this country, invest directly in gas supply projects, and increase subsidies for big renewable energy projects.

The logic behind calls for public infrastructure spending and industry assistance in a recession is that a dollar of government spending increases GDP by more than a dollar, because it stimulates private activity beyond the immediate project (Section 3.5.2). Even those who contend that a dollar of government spending raises GDP by less than a dollar don't necessarily oppose stimulus spending, if it keeps people afloat during the crisis period of the pandemic, with their key economic relationships still in place and a better prospect of recovering more quickly.

But this recession shouldn't be treated just as a temporary demand shock. It has a specific identifiable cause – a cause that may be with us for a long time. Even with sufficient testing and tracing to deal with our rational fears of infection, we may still have social distancing restrictions that limit commerce even when consumers are keen, and our borders may remain largely closed to students, tourists, and temporary workers.

So what should governments do? In highly uncertain times, it is prudent to keep options open and invest only where there's a reasonable basis for believing it's worthwhile.

There are many interests, both commercial and ideological, seeking to align governments' post-pandemic investment priorities with their vested interest. Governments should be wary of such interests, and make decisions about public spending that maximise the value to the community as a whole.

### 6.1 Overhaul public infrastructure investment

Public infrastructure spending is a traditional recourse when the economy tanks. People jostle for their preferred government project, whether it's new or fast-tracked roads, rail lines, desalination plants, solar energy farms, or city beautification projects.

Public infrastructure is a traditional choice because it both has high fiscal multipliers (Section 3.5.2) and it can increase potential GDP, by making possible the efficient movement of people and goods, as well as other economically important activities. These activities lead to greater tax revenues down the track, which helps pay for the infrastructure.

But it's not a foregone conclusion that a public infrastructure project will be effective as stimulus. Details really matter: in particular, the net benefits of the infrastructure to the community, and especially the time-frame to get it going. Some projects are much more promising than others, as the following subsections explain.

#### 6.1.1 Pause large projects where the benefits are now in doubt

Australia can no longer be confident about future population growth. The Prime Minister says to expect a 30 per cent fall in overseas migration this year, and 85 per cent next year. After next year, who knows? Yet the existing infrastructure pipeline is predicated on the population growth we used to have.

Rather than putting the pedal to the metal, as some ministers are planning, state governments should thoroughly overhaul their infrastructure programs, and review the business cases of all major projects to see whether they are still a priority or indeed whether they are needed at all. Many may be able to be delayed or dropped.

It's not only uncertainty about population growth that makes it a good idea to review major projects. There's also great uncertainty about people's future travel and work patterns.

For as long as the virus lurks in the community, or is believed likely to revisit us from overseas, many people are likely to avoid public transport unless they're confident carriages won't be crowded and fellow passengers will keep their distance. If working from home continues at scale, it may mean delaying new freeways designed to deal with traffic peaks, and new aviation capacity. If people feel safest getting around by car, governments may need to consider congestion charging to ensure that the inner cities don't get gridlocked in peak periods.

At this time of great uncertainty, it makes little sense to forge ahead with projects conceived during a time of rapid population growth, and even less to commit to new ones.

### 6.1.2 Fast-track small projects to aid economic recovery

Some projects can be mobilised quickly. They are the projects that don't need time-consuming processes for approval, funding appropriation, or procurement.

Not only can smaller projects begin more quickly, but some can also directly aid economic recovery by facilitating emerging patterns of activity. Around the world, in cities as diverse as Seattle, Milan, and Bogota, city governments are re-purposing road space to accommodate the upsurge in cycling, as people avoid crowded buses and trains. There is large scope for such projects in Australian cities.

Other small and medium projects include upgrading key arterial roads, improving road surfaces, station maintenance and upgrades, sleeper replacement, and rail signalling upgrades.

What's important in selecting such projects, in addition to short lead times, is that they are robust to a range of future scenarios. It remains unclear how fast population growth might be over the medium term, and equally unclear is how sustained social distancing might turn out to be.

## 6.2 Invest in a low-emissions future

One long-term commitment that is not going away is to reduce CO<sub>2</sub> emissions, to meet the Federal Government's Paris targets and to achieve net zero by 2050, which is the common target of Australia's states and territories.

COVID-19 has one small silver lining: power use has dropped a little during the shutdown (Figure 6.1 on page 74), and the consistent downward trend in electricity emissions has continued (Figure 6.2 on page 74). These improvements have been driven by changes in the generation mix with coal plant closures and new renewable investments, and by lower prices for coal and gas.

Overall, major changes in energy policy are not urgent over the next 12 months. With the pressure of all the policy reform that is urgent, the priority for energy policy in the recovery phase should be to ignore calls for stimulus spending for infrastructure that is inconsistent with a low-emissions future.

One project that might provide effective stimulus spending in the short term, is a mandatory roll-out of smart meters. This would need to be contingent on a technology review and the parallel introduction of supporting tariff reform.

Smart meters deliver cost savings such as remote meter reading and connections. More importantly, they facilitate unwinding of unfair cross-subsidies<sup>317</sup> and unlock the major benefits that flow from

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317. T. Wood and L. Carter (2014).

household batteries and electric vehicle charging.<sup>318</sup> The current market-based roll-out is making steady but slow progress and contrasts with many countries such as the UK that have mandated the roll-out. An accelerated roll-out would provide an economic stimulus in a short period of time and would be consistent with longer-term market needs. Such a program should be designed with reference to the lessons learned from the poorly implemented Victorian program<sup>319</sup> and in close coordination with network and retail businesses to move to more cost-reflective pricing.

Otherwise governments should use the time to develop initiatives and investments for the longer term that are consistent with a low-emissions future. They should:

- Accelerate market reforms or bypass barriers to investments where the delivery of major economic value is being delayed.
- Establish clear criteria to support projects with clear economic value that could be brought forward to the first half of this decade.
- Not support or subsidise the introduction of more supply in markets where demand is already flat or falling.

Applying these principles in the energy sector means that governments should:

- Not introduce or extend subsidies for deploying solar panels, batteries, large-scale renewable energy projects, or storage.
- Remove barriers to cost-effective deployment of these technologies. These barriers, such as transmission and distribution network technical and regulatory constraints, are well understood but their removal is slow.

- Extend underwriting for priority transmission upgrades and renewable energy zones. This would be a low-risk investment.
- Consider funding early-stage technology projects to drive down the cost of low-emissions energy, renewable hydrogen, low-emissions transport, and grid integration technologies.
- Extend the mandate and funding for the Australian Renewable Energy Agency (ARENA) to fund such projects.
- Not fund projects that will have diminishing value in a low-emissions world, such as coal-fired power plants or a cross-continent gas pipeline.<sup>320</sup>
- Consider mandatory roll-out of smart meters, contingent on a technology review and the parallel introduction of supporting tariff reform.

The pandemic has provided an opportunity for a strategic assessment of sectors that provide essential supplies for the Australian economy. Each sector should be assessed on its merits against the benefits and risks of domestic manufacturing versus sourcing offshore. For example, rebuilding our oil refineries, manufacturing solar panels, or electrolyzers to produce hydrogen are unlikely to make strategic or economic sense for Australia.

Manufacturing built on an emerging Australian comparative advantage in large-scale solar and wind energy should be considered.<sup>321</sup> Australian governments should aim to grasp these opportunities without resorting to ongoing subsidies. Green steel looks to be one such opportunity where federal, state, and local governments could work together to provide targeted, limited support.<sup>322</sup>

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318. AEMC (2019).

319. Latimer (2018).

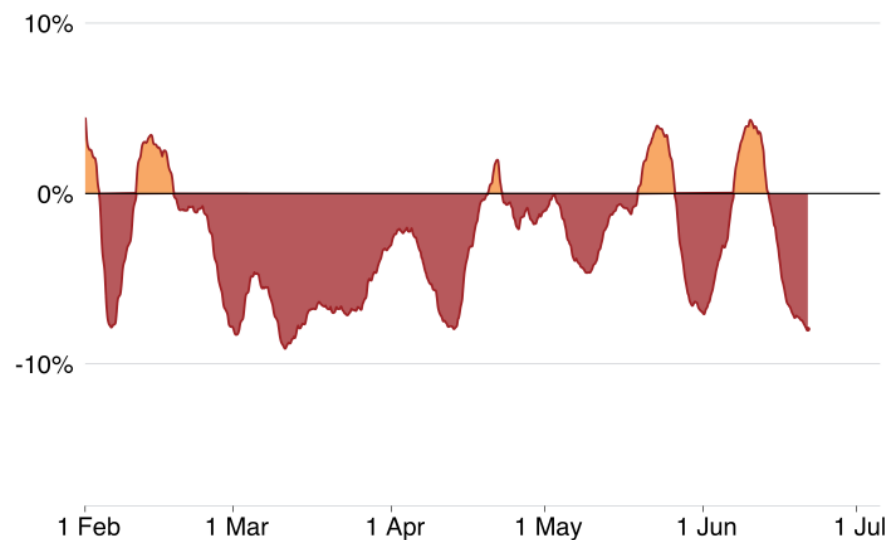
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320. Morton (2020a).

321. Garnaut (2019).

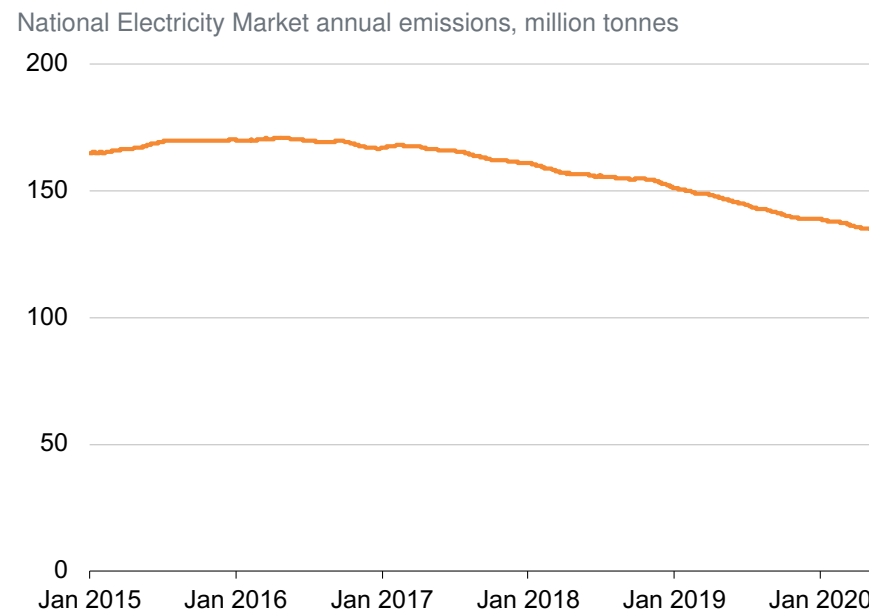
322. T. Wood et al (2020).

**Figure 6.1: Electricity use has dropped a little during the shutdown**  
National Electricity Market weekly demand, 2020 vs 2019



Source: Grattan analysis of AEMO (2020a).

**Figure 6.2: Electricity sector emissions have continued a downward trend**  
National Electricity Market annual emissions, million tonnes



Source: Grattan analysis of AEMO (2020b).

The Federal Government's 2020 Technology Investment Roadmap discussion paper<sup>323</sup> provides a comprehensive review of technologies that could qualify for similar support. Again, a robust process for project selection and management is critical to ensure public funding is cost effective.<sup>324</sup>

### 6.3 Don't abandon free trade

Coronavirus has exposed the fragility of global supply chains during times of crisis.<sup>325</sup> Around the world, governments are responding by engaging in protectionist behaviour.<sup>326</sup> In Australia, Industries Minister Karen Andrews has promised to use government procurement processes to increase Australia's manufacturing capabilities, and Opposition Leader Anthony Albanese has stressed the importance of domestic manufacturing.<sup>327</sup> Business leaders including Andrew Liveris and David Pratt have also called for more government support to encourage manufacturing.<sup>328</sup>

There are opportunities for growth in Australian manufacturing, particularly in energy intensive industries and to secure supplies of vital medical products.<sup>329</sup> But the pandemic should not be a reason for Australia to step back from globalisation and free trade.

By engaging in trade, Australian exporters gain access to a global marketplace, and as a result they can increase production levels and hire more workers.<sup>330</sup> Trade helps to make all sectors of the economy more productive, and makes products cheaper for Australian

consumers.<sup>331</sup> The crisis should not be used as an opportunity to indulge protectionist impulses that will slow growth and make Australians worse off in the long term.

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323. Department of Industry (2020).

324. T. Wood and Mullerworth (2012).

325. Bloom (2020) and Hutchens (2020).

326. Financial Times (2020).

327. Albanese (2020).

328. J.-a. Sprague and Bailey (2020); and Greber (2020).

329. Section 6.2 on page 72 and Duckett et al (2020, pp. 63–64).

330. Thompson et al (2012).

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331. Thompson et al (2012); and Banks (2003).

## 7 Managing the health system in transition

All Australians were affected by the coronavirus pandemic. For most, it was just the irksome restrictions as social distancing was used to drive down new cases. For many, it involved a loss of income. For some, it was mourning the death of a loved one, with the grieving made all the more painful by restrictions on the number of people who could attend the funeral.

The health system changed too. It embraced new ways of working because of the need to protect patients and staff from infection. Elective procedures were cancelled and health professionals took on new roles. Changes occurred across most parts of the health system, and were often embraced by consumers and providers alike.

It wasn't all smooth sailing. Coordination wasn't good enough and had to be built. Public health planning wasn't strong enough at the regional level. Primary care wasn't ready or properly supported to deliver the required frontline services. Telehealth wasn't ready and defaulted to telephone calls. Home care and home monitoring was not well prepared or well integrated with primary or tertiary care. The private and public hospital systems were not integrated. Rapid solutions to all these problems had to be found.

We are only part the way through the response to the pandemic and its consequences.

The experience of health care during the pandemic highlights the issues Australia needs to tackle for a more effective, efficient, and equitable health system. In this chapter, we discuss what a 'new normal' should look like, focusing on what is urgent. It would be a tragedy if lessons weren't learned from the pandemic. We argue that Australia should not 'snap back' to the old order, but rather that

the changes that occurred during the pandemic should inform what happens during the recovery period and beyond.

Some changes to the health system are needed in the next 18 months, such as changes to telehealth and out-of-hospital care, and to the interactions between the private and public health systems.

Other reforms will have to wait until there are fewer competing priorities. But the COVID-19 crisis has demonstrated the need for longer-term reform of the health system supply chain, the primary care system, public health preparedness, and overall system planning and coordination.

### 7.1 The process for change

Retaining some of the changes that were made during the lockdown is a no-brainer. But even so-called no-brainers require some thought. Almost every consumer and health professional has a story to tell about what worked and what didn't. Stewards of the system – the funders and the regulators – will also have their perspectives on how things worked, aware of the unintended or perverse consequences of policies implemented rapidly during the pandemic. All this knowledge should be tapped to design a better system, and this requires effective overarching change management processes.

The new normal will not just happen. Decisions need to be taken about what stays, and in what form, lest all the good changes be eroded by a drift back to the old, inadequate ways. States and territories, and the Commonwealth Government, should establish participatory processes to plan the transition to the new normal. These processes may be a



special-purpose review committee<sup>332</sup> or build on the task groups set up to manage the pandemic.<sup>333</sup> Whatever the structure, there should be opportunities for consumers and professionals to be involved.

COVID-19 appeared on the scene quickly, and there was a lack of evidence initially about what it was, its epidemiology, and how to treat it. The Commonwealth Government established a 'Rapid Research Information Forum' to provide evidence-based advice on topics such as the efficacy of serological tests and whether people can be reinfected.<sup>334</sup> This evidence-based approach should be carried over into the new normal. In particular, any policy changes should be informed by evidence about the impact on the most vulnerable.<sup>335</sup>

## 7.2 Improving access through telehealth

Primary care played a crucial role in the preparations to fight coronavirus, stepping up without adequate supplies of personal protective equipment, and facing changing guidance on who to test, where and when, all despite initial hits to practice revenue.<sup>336</sup> There was a silver lining for consumers: the introduction of telehealth, which should now become a permanent feature of health care in Australia.

Starting in mid-March 2020, the Commonwealth Government drip-fed changes to facilitate telehealth in primary care. Two groups of items were introduced: one for video-conference consultations, and one for telephone consultations if video was not available.

Telehealth consultations are a valuable virtual health service.<sup>337</sup> Others include remote imaging services, online secondary consultations, electronic scripts, remote monitoring, online team coordination, and electronic health records.<sup>338</sup> The COVID-19 experience shows that virtual health can and should be expanded to improve patient care.

Telehealth has been advocated for decades as a way of enhancing access to care for people living in rural and remote Australia.<sup>339</sup> But telehealth has faced numerous barriers,<sup>340</sup> not least equivocal Commonwealth government support,<sup>341</sup> and poor internet connectivity in rural and remote Australia.<sup>342</sup> Take-up was low.<sup>343</sup>

Telehealth should not be seen as a simple substitute for a face-to-face consultation, although it can do that. In the new normal, health professionals and their patients need to assess when telehealth should be the preferred medium given the nature of the presenting problem, distance to be travelled, and other factors. The 'digital divide' means that a patient's digital and health literacy will need to be assessed in customising care.<sup>344</sup> Funding should be provided to develop programs to lower or remove the barriers created by the digital divide. Primary Health Networks (PHNs) would be well placed to do this, linking as they do the primary care system and populations.<sup>345</sup> PHNs are able

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332. Such as Queensland has established, and in which Grattan's Health Program Director Stephen Duckett participates.

333. This latter is the approach adopted by South Australia.

334. Rapid Research Information Forum (2020a); and Rapid Research Information Forum (2020b).

335. Pineda and Corburn (2020); Wang and Tang (2020); J. A. Smith and Judd (2020); The Lancet (2020); and Ahmad et al (2020).

336. This section draws on Duckett (2020a).

337. We have used the term 'telehealth' in this section because it is the most common term in current use. Over time we would expect 'telehealth' to be replaced by a broader term such as digital health, virtual healthcare, or 'technology-enabled care'.

338. Fera et al (2020).

339. Bradford et al (2016); and Wells (1976).

340. Jang-Jaccard et al (2014).

341. Yellowlees (2001).

342. Broadband for the Bush Alliance (2018); and Park et al (2019).

343. V. Wade et al (2014).

344. Velasquez and Mehrotra (2020).

345. Declaration of interests: Stephen Duckett is chair of Eastern Melbourne PHN; and Grattan Health Fellow Hal Swerissen, another co-author of this report, is a member of the board of Murray PHN.

to tailor programs to different needs based on geography, or community characteristics such as differences in the number of people with diverse cultural or linguistic backgrounds.

The pandemic telehealth items initially did not include secondary consultations – discussions between a specialist and a general practitioner without the patient present. This service currently attracts no additional remuneration for either party, but should be expanded as part of a virtual health world. New streamlined specialist telehealth items – less complex than case-conferencing items – should be introduced to facilitate secondary consultations with general practitioners (with or without the patient present).

An emphasis on telehealth should be accompanied by 21st Century e-referrals<sup>346</sup> – abandoning the fax machine, which is still ubiquitous in health care but has been relegated to the recycling bin or the museum in all other industries, and getting My Health Record to be a trusted source of information for patients and clinicians alike.<sup>347</sup>

Telehealth is prone to a ‘woodwork effect’ – where demand comes out of the woodwork when a new benefit is available.<sup>348</sup> The risks of over-servicing,<sup>349</sup> misuse by some providers with predatory business models,<sup>350</sup> and fraud are real,<sup>351</sup> but the benefits of telehealth are undeniable. Especially in the context of increasing prevalence of chronic disease, telehealth items should enhance continuity of care,<sup>352</sup>

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346. Hughes et al (2018); and Love (2019).

347. De Mesquita and Edwards (2020).

348. L. Sprague (2014).

349. Viney and Haas (1998); and Van Gool et al (2002).

350. Knibbs (2020a); and Knibbs (2020b).

351. United States. Department of Justice (2019); United States. Department of Health and Human Services. Office of Inspector General (2018); Faux and Grain (2020); and Rajda and Paz (2019).

352. Including continuity of care between medical practitioners and pharmacists.

which benefits patients and reduces costs,<sup>353</sup> and avoids further fragment the primary care system.

New telehealth items ought to have been introduced long ago. It is a tragedy that it took a pandemic to get the policy ball rolling. The issue becomes how to ensure new items are not abused.

The particular COVID-19 items may not be suitable for the new normal. The Australian College of Rural and Remote Medicine has published a set of standards which could be used as a basis for developing revised items.<sup>354</sup> These standards include 11 core principles, one of which is:

The integrity and therapeutic value of the relationship between client and health care practitioner should be maintained and not diminished by the use of telehealth technology. Telehealth must enhance the existing clinician patient relationship (not fragment it). Telehealth arrangements should complement existing services (where available), build on rural workforce and referral patterns to avoid further service fragmentation, and address practicalities of coordination, scheduling and support from the patient’s perspective to improve their continuity of care.

Although framed for rural and remote practise, this principle is relevant to telehealth delivery anywhere. In line with that principle, specifically that telehealth ‘must enhance the existing clinician/patient relationship’, new telehealth items should be limited to patients with an established relationship to a practice, such as having at least half of their primary care visits in the past year being to that practice.<sup>355</sup> In the case of people over the age of 70, once enrolment is implemented,<sup>356</sup> telehealth should be limited to the practice in which the patient is

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353. Pereira Gray et al (2018); and Bazemore et al (2018).

354. Australian College of Rural and Remote Medicine (2020).

355. Practices should be able to contract with specialist telehealth providers for out-of-hours care, and it may also be appropriate to allow practice nurses to provide telehealth services for the practice.

356. As foreshadowed in the 2019 Budget.

enrolled.<sup>357</sup> New specialist telehealth items should be introduced for attendances other than the initial consultation.

The current items specify that telephone consultations are supposed to happen only if video is not available. Yet during the pandemic telehealth, at least in general practice, was primarily by telephone. The relative benefit of video compared to telephone consultations has not been evaluated, so governments should await evidence on the most beneficial balance for patients and providers before deciding if restrictions should be maintained.<sup>358</sup> There should be a financial incentive on practices to bulk-bill telehealth items, and these items should be subject to strict electronic verification requirements.<sup>359</sup>

During the pandemic the structuring of the telehealth items mirrored face-to-face items. In the new normal there might be quite different tiering, splitting the standard consultation item into two or three items as there can be more accurate automatic verification of consultation length.

Digital or virtual consultations can also be by email, although the evidence about e-consultations is mixed.<sup>360</sup> Nevertheless, practices should be encouraged to make e-consultations available to their patients. In the first instance, this might best be as a benefit for patients who are 70+ and who enrol with a practice. Standards for practices to be eligible to accept enrolments of patients aged 70+ should include requirements about e-mail consultations.

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357. In England all patients need to enrol with a general practice. The current payment contract between the NHS and general practice requires a phased expansion of telehealth, including that at least one quarter of consultations should be digital – and this was before the pandemic: see Iacobucci (2019).

358. Outcome Health (2020a) proposed a system-wide target of 50 per cent of telehealth consultations to use video by 2021.

359. Faux and Grain (2020). Anecdotal evidence suggests telehealth is more efficient for providers, including by reducing no-shows.

360. Mold et al (2019).

Telehealth is particularly useful in mental health care.<sup>361</sup> Unfortunately, during the pandemic spatial isolation often converted into social isolation, and this created anxiety and psychological distress for many,<sup>362</sup> leading to increased mental health presentations in general practice.<sup>363</sup> After the pandemic, there will be a further surge in demand for mental health services,<sup>364</sup> and this will put still more pressure on an already overloaded mental health system.<sup>365</sup> As with primary care, new technologies may help meet this future demand.<sup>366</sup>

Telehealth may have perverse effects too. Although a boon for rural and remote patients, if wider access to telehealth reduces the viability of – or trust in – specialists who are based in regional centres, it may be a net negative. Policies which limit telehealth access in a way which promotes continuity of care may reduce the risk to rural specialty practice.

### 7.3 Improving convenience and access with expanded out-of-hospital care

New ‘virtual hospitals’ were planned as part of the pandemic response.<sup>367</sup> A huge variety of telehealth and telemonitoring approaches were introduced very rapidly.<sup>368</sup> All this should become part of a new ‘business as usual’.

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361. This section draws on Hickie and Duckett (2020).

362. ABS (2020q); Biddle et al (2020); and Fisher et al (2020).

363. Pearce and McLeod (2020, pp. 12–13).

364. Reger et al (2020), Outcome Health (2020b) and E. Brown et al (2020). Torjesen (2020).

365. Duckett and Swerissen (2020). The Productivity Commission is preparing a report on mental health in Australia. A draft of the report has found that the cost of mental ill-health to the economy is substantial, and funding mental health services to better manage these problems will increase productivity and reduce the economic burden: PC (2019).

366. Torous et al (2020).

367. Mannix (2020); and Sweet (2020).

368. Wosik et al (2020).

Hospital-in-the-home is a well-established and effective alternative to in-patient care for many conditions.<sup>369</sup> Rehabilitation in the home, or as an out-patient, has been shown to be just as effective as in-patient rehabilitation for appropriately selected patients.<sup>370</sup>

The pandemic caused many nursing homes (residential aged care facilities) to go into lockdown and reduce visitors and transfers in and out for hospital care. There is now well-established evidence of the benefits of hospitals providing additional support to residential aged care facilities, including via telehealth,<sup>371</sup> to reduce hospital admissions.<sup>372</sup>

States should expand hospital-in-the-home and rehabilitation-in-the-home services, and outreach into residential aged care facilities.<sup>373</sup>

Medical practitioners cannot bill Medicare for services provided to public hospital hospital-in-the-home patients. However, involvement of a patient's general practitioner should be encouraged to ensure continuity of care. Public hospitals should contract with general practitioners to pay them for their services to those patients. This could be facilitated by Primary Health Networks.

States with plans to expand public hospital bricks-and-mortar should review those plans to assess to what extent out-of-hospital and telehealth expansion might obviate the need for some of these builds.

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369. Caplan et al (2012); and Kansagara et al (2016).

370. Schilling et al (2018).

371. Hui et al (2001).

372. Chan et al (2018); and H. Carter et al (2019).

373. Hospital-in-the-home services may need to be tailored to be culturally appropriate for all communities: Brett et al (2017).

Telemonitoring is an important aspect of hospital-in-the-home. It reduces costs,<sup>374</sup> and appears not to reduce quality of care for the most vulnerable.<sup>375</sup>

More telemonitoring will require viable business models, either through new Medicare Benefit Schedule items, again perhaps linked to enrolled patients, or as part of hospital outreach, with costs shared between the Commonwealth and states under public hospital funding arrangements, as a non-admitted service.<sup>376</sup>

#### **7.4 Improving efficiency by connecting public and private and managing elective procedures better**

Public hospitals were transformed during the pandemic as they responded to an anticipated tsunami of demand.<sup>377</sup> Beds were freed up as a near total shutdown of elective procedures was ordered. This latter strategy increased average total waiting times for surgery, and created a 'care debt' of delayed procedures, most of which will need to be performed in the future. This section discusses how this 'care debt' may be addressed.

##### **7.4.1 Use private hospitals better**

The private hospital system took a battering during the pandemic. Private hospitals were effectively closed for a month,<sup>378</sup> and their viability may be under pressure. But the pandemic showed that it was possible to integrate public and private. Every state and territory negotiated contracts for private hospitals to provide 'overflow' care in case public hospitals were overwhelmed.

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374. Michaud et al (2018).

375. Jennett et al (2003).

376. For example, as a 'clinical monitoring service'.

377. This section draws on Duckett (2020b).

378. Morton (2020b).

Unemployment has risen, which may cause people to reflect on whether they can afford to maintain their private health insurance. Funds' cash position has been improved by the slow-down in elective procedures, and in visits to health professionals covered by general (extras) insurance. But if younger people, hit hard by increased unemployment, decide to drop their insurance, the industry's 'death spiral' will accelerate.<sup>379</sup> Fewer people insured will mean less demand for private hospitals from private patients.

States should consider negotiating long-term contracts with private hospitals, so that procedures can be performed in these hospitals to help clear the elective surgery backlog. States should also consider this strategy to meet future demand for elective procedures.

#### 7.4.2 Manage demand for elective procedures

If there is to be increased public contracting of private care, it needs to be equitably managed.

A properly managed elective procedures system should have three key elements:

- there should be a consistent process for assessing a patient's need for the procedure, and ranking that patient's priority against others;
- the team performing the procedure, and caring for the patient afterwards, should be highly experienced in the procedure; and
- the procedure should be performed at an efficient hospital or other facility, so the cost to the health system is as low as possible.

Unfortunately, Australia sometimes fails on all three measures.

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379. Duckett and Nemet (2019a); and Duckett and Cowgill (2019).

There is no consistent assessment process across hospitals. Even different surgeons in the same hospital seeing the same patient sometimes make different recommendations about the need for a procedure. This means a patient lucky enough to be seen by surgeon A may be assigned to category 2, but the same patient seen by surgeon B might be assigned to category 3 and so have to wait longer. A patient's gender or level of education sometimes seems to have an inappropriate effect on categorisation decisions.<sup>380</sup>

Assessment is a core skill of specialists, and there will always be legitimate variation in recommendations for treatment to take account of the individual circumstances of each patient. However, the point here is to ensure that variations in assessment and prioritisation reflect patient-specific factors and are evidence-based.

States should develop agreed assessment processes for high-volume procedures, such as knee and hip replacements and cataract operations, and reassess all patients on hospital waiting lists. Reassessment could be done remotely using telehealth.

#### 7.4.3 Standardise care paths to improve care and equity

Specialists in each area, together with referring clinicians, should be invited to develop evidence-based criteria for setting priorities and for developing agreed care paths.<sup>381</sup> The care paths should cover pre-surgery care (e.g. what diagnostic tests should be done, what non-surgical treatments should be tried before the procedure),<sup>382</sup> and post-surgery care both in-hospital and at home.<sup>383</sup> Standardised care paths, such as the NSW Agency for Clinical Innovation's Osteoarthritis

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380. Smirthwaite et al (2016).

381. Breton et al (2020).

382. Schoch and Adair (2012); and Glasgow et al (2020).

383. Care paths should also specify who might do what as part of workforce reform, see Erhun et al (2020).

Chronic Care Program,<sup>384</sup> have been shown to lead to better outcomes and reduced admission rates.<sup>385</sup>

Care paths should build on the extensive work by Primary Health Networks, to help ensure smoother transition from primary care (general practice) to secondary care (hospitals) and back again.<sup>386</sup>

A substantial proportion of patients in even the most specialised medical centres can be treated according to a standardised care path.<sup>387</sup> Care paths should be developed by multidisciplinary teams, to ensure non-medical treatments are appropriately considered.<sup>388</sup>

Private health insurers should be empowered to participate in funding diversion options, so patients are able to have their rehabilitation at home rather than in a hospital bed.<sup>389</sup>

A new, coordinated, single waiting list priority system in each state would enable all patients to know where they stand.<sup>390</sup> A patient on top of the list would be offered the first available place, regardless of whether it was closest to their home. They could refuse the offer, without losing their place in the queue, if they wanted to wait for a closer location or be treated by a team with whom they have a relationship.<sup>391</sup> Queueing theory suggests that a single waiting list will lead to shorter average waiting times overall.<sup>392</sup> And 'single-entry' models appear to improve patient care.<sup>393</sup>

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384. New South Wales. Agency for Clinical Innovation (2020).

385. Deloitte Access Economics (2014).

386. Lee et al (2019); Gill et al (2019); and Love (2019).

387. Cook et al (2014).

388. Ackerman et al (2020).

389. Duckett and Nemet (2019b).

390. A similar proposal has been advanced for Canada, termed a 'single entry model', see Urbach and Martin (2020).

391. Or a particular surgeon or medical proceduralist if they are to be treated privately.

392. Breton et al (2020).

393. Damani et al (2017).

The single waiting list should include both regional and metropolitan patients, to ensure as much as possible that city patients do not get faster treatment than people in regional and remote areas, or vice versa. The system should be further centralised in metropolitan areas. The full range of elective procedures should not be re-established in every hospital.<sup>394</sup> Some surgeons would need to be offered new appointments if elective surgery in their specialty was no longer being performed at the hospital where they previously had their main appointment.

Patients with private health insurance can opt to be treated as a private patient in a public hospital. So the waiting list should include public and private patients, to prevent private patients gaining faster admission to public hospitals.

## 7.5 Four priorities for longer-term reform

In the longer term, governments will need to pursue other priorities highlighted by the COVID-19 pandemic. As detailed in our recent report,<sup>395</sup> these include:

- improving the resilience of the health system through supply chain reform;
- improving health system readiness by better planning;
- encouraging outreach and telehealth with new primary care funding models; and
- bringing it all together with integrated regional planning and system management.

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394. We discussed the benefits of concentrating procedures in high-volume centres in a previous report: Duckett and Nemet (2019b).

395. Duckett et al (2020, Chapter 4).



## 8 Going back to school

The rescue phase of COVID-19 required almost all students to learn remotely. Despite best efforts of teachers, students, and parents, most students are likely to have learnt less than they would have in the classroom. Disadvantaged students will need extra support to catch-up.

We recommend governments adopt a highly targeted strategy to help disadvantaged students across Australia recover learning losses. It would cost about \$1.25 billion to help one million disadvantaged students catch-up over the next six months.

The temporary package would also stimulate the economy by employing young people to work as tutors in disadvantaged schools. The long-term economic benefits would far outweigh the costs, boosting the future earnings of disadvantaged students by about \$3.5 billion.

Governments should also build on positive changes brought about by remote schooling. In some cases the disruptions improved how teachers' time is organised, for example with teachers collaborating more on common lesson designs and digital materials, potentially opening up more time for giving students individual feedback. Teachers and students have also become better at using digital technology for learning. Governments should carefully test and support new 'blended learning' approaches in coming years.

Bailing out private schools should not be a government priority unless there is a genuine risk to supply. If needed, money from the Federal Government's 2019 \$1.2 billion fund for Catholic and independent schools should be put toward these efforts.

### 8.1 Most students learnt less during COVID-19 disruptions, especially disadvantaged students

COVID-19 lockdowns forced schools to quickly switch to remote learning for parts of Terms 1 and 2 in 2020. Teachers were forced into new ways of working at short notice, with little technical training or time to develop remote lesson plans. Parents were also caught off guard, having to juggle work and other commitments with supporting children to learn at home.

Despite best efforts, most students are likely to have learnt less in remote schooling than in their regular class. Grattan's 2020 *COVID catch-up* report showed that Australian teachers believe most students learnt less.<sup>396</sup> In one survey of more than 2,500 teachers in NSW, only 35 per cent were confident their students were learning well in remote learning. In disadvantaged schools, only 15 per cent of teachers felt assured of student progress.<sup>397</sup>

The biggest losses will be among disadvantaged students. We find the achievement gap widens at triple the rate in remote schooling compared to regular class (see Figure 8.1).<sup>398</sup> Even if remote learning was working well, disadvantaged students are likely to have learnt at

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396. See Sonnemann and Goss (2020).

397. R. Wilson et al (forthcoming) conducted the survey from 17 April to 10 May 2020. A national survey by Pivot (forthcoming) of 320 teachers in May showed similar findings. Most teachers believed students learnt at about 50-to-75 per cent of their regular pace, with teachers in disadvantaged schools reporting it was closer to only 25-to-50 per cent.

398. We model these projections in our *COVID catch-up* report, see Sonnemann and Goss (2020). The estimated gap increase is based on findings from the Education Endowment Foundation (EEF) rapid literature review, see EEF (2020), as well as Grattan's Equivalent Year Level (EYL) metric approach from our 2016 report, see Goss and Sonnemann (2016).

about 50 per cent of their regular rate, losing about a month of learning over a two-month lockdown.<sup>399</sup>

The learning losses will be largest in the states and territories with the longest periods of remote schooling and student-free days. Victoria (nine weeks) and the ACT (eight) had the longest periods of remote schooling, followed by NSW (seven weeks), Tasmania (seven), and Queensland (six).

The COVID-19 learning losses are a concern but must be kept in perspective. The *existing* achievement gap is more than 10 times greater than the widening of the gap caused by COVID-19 (see Figure 8.2 on the following page). Governments must tackle deeper long-term problems affecting our most vulnerable students. Our proposed reform package provides an opportunity to test and evaluate what works for struggling students.

**Figure 8.1: The achievement gap grew three times faster during remote schooling**

Achievement gap between disadvantaged and advantaged students in months, average of reading and numeracy, Year 5 students, 2020 projection



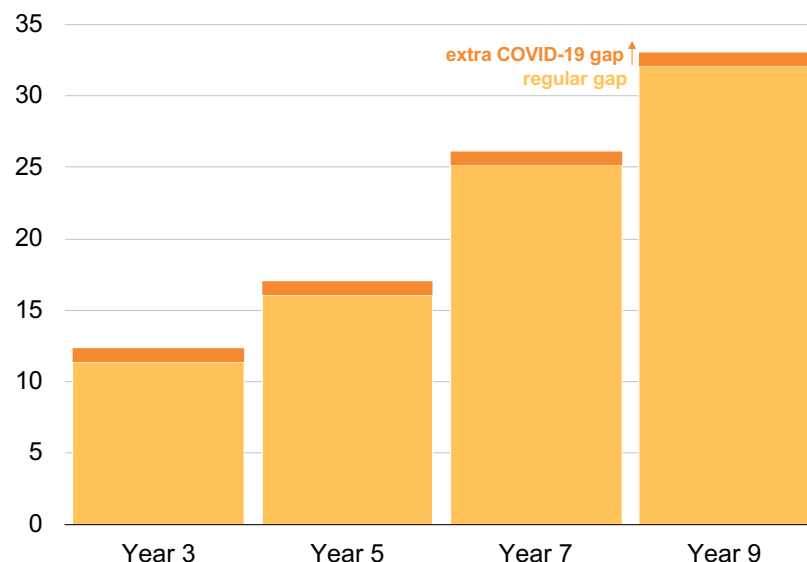
Notes: The 'gap' is defined as the difference in learning between disadvantaged students and all other students. Disadvantaged students are those whose parents (a) completed Year 11 or below, or (b) have a certificate. The proportion of students classified as disadvantaged is 38 per cent. The COVID-19 gap growth rate during remote learning is based on the estimate from EEF (2020). We estimate the 'gap in months' using the EYL methodology from Goss and Sonnemann (2016).

Source: Grattan analysis of NAPLAN data 2010 to 2019, source estimate from EEF literature review EEF (2020).

399. We infer the amount of progress made by disadvantaged students using historical data on learning progress and our estimates of the increase in the gap. See Sonnemann and Goss (2020, p. 16).

**Figure 8.2: The existing achievement gap is much larger than the extra gap caused by COVID-19 remote schooling**

Gap in months, numeracy, 2020 projection



Notes: The 'gap' is between disadvantaged students and all other students. The 'regular' gap is projected using average gaps over 2010 to 2019. The 'extra COVID-19 gap' uses estimate from EEF literature review 2020. The gap in months uses the EYL methodology from Goss and Sonnemann (2016).

Source: Grattan analysis of NAPLAN data (2010 to 2019), source estimate from EEF literature review EEF (2020).

## 8.2 A catch-up strategy for disadvantaged students is needed in 2020

As schools re-open, most students will recover without too much trouble. But disadvantaged students will need extra support.

We recommend a national targeted strategy to help disadvantaged students across Australia. It would cost about \$1.25 billion to help about one million disadvantaged students catch-up over the next six months, while helping to stimulate the economy at the same time.<sup>400</sup>

Schools should be given a 'catch-up' loading for the remainder of 2020, with guidelines on high-priority initiatives. To spend the money well, schools will need to closely assess the learning needs of their students. We suggest the national assessment body, ACARA, be responsible for creating a \$20 million package of suitable in-class assessment tools, to help teachers identify and monitor the progress of their students.

We recommend two initiatives. They are not necessarily the cheapest options, but they have the highest chance of success.

The first is small-group tuition programs. These involve small groups of three students, and can increase student learning by up to five months over one-to-two school terms. Small-group tuition is expensive, but large trials have shown that it works. Young university graduates and pre-service teachers should be hired as tutors where possible, because they will be hit harder by the recession than older Australians (see Section 3.1.1 on page 16) and are likely to spend the extra income quickly, stimulating the economy.

400. Our estimate of one million students is a rough guide only. It covers vulnerable students most likely to fail basic proficiency tests in PISA by age 15, namely students from low-SES families, rural locations, and Indigenous communities, as well as LBOTE students and students with poor mental health or others who may have especially struggled during the lockdowns.

The second high priority is tried and tested literacy and numeracy programs. These whole-class programs involve specific teaching techniques for certain skills or units, for example using phonics to teach reading, along with structured content, materials, and training for teachers in how to implement them.

Governments should also conduct small-scale trials of ‘targeted teaching’ with materials for students very far behind, and of training for teachers in teaching social and emotional skills.

Governments should give schools information on ‘quality assured’ providers, and should subsidise delivery partners where appropriate.

Governments should also spend \$95 million on evaluating recovery initiatives, so we can learn more about how to help disadvantaged students. We still know too little about how to close the much bigger existing equity gap – a serious problem that will remain after the pandemic subsidies.

The benefits of these initiatives would far outweigh the costs. Our recommended package would cost about \$1.25 billion, or about \$1,262 per disadvantaged student on average.<sup>401</sup> It would more than double the extra funding loading for disadvantaged students over a six-month period. The package would help to stimulate the economy over the next six months, and also provide longer-term economic benefits, generating about \$3.5 billion in future earnings for disadvantaged students.<sup>402</sup>

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401. The package would include about \$1.13 billion for small group tutoring, about \$70 million for literacy and numeracy programs, and about \$30 million for small-scale trials, as well as \$20 million for in-class assessments. For more detail on the costings, see Sonnemann and Goss (2020).

402. For more detail see Sonnemann and Goss (ibid, p. 29). This estimate is conservative because it does not include any benefits in higher taxes paid or lower welfare payments received.

### 8.3 Positive changes to teaching that emerged during remote schooling should be extended

The shift to remote schooling forced big changes in teachers’ practices and work routines. We identify two positive changes to teaching and learning that governments should now build upon.

#### Learn from the changes to how teachers’ work is organised

The crisis created a sudden need to teach lessons online. This exposed big cracks in the way teachers’ time is currently organised.

In Australia, teachers are expected to do a lot themselves. They sift through lots of materials to create their own lessons, and they often create their own in-class assessments for students to sit. There are some benefits in teachers doing all the groundwork themselves, but it comes at a cost to their time. Teachers then have less time for other important tasks, such as giving individual student feedback. They can also be in the dark about whether their selected materials or teaching approaches are better than others.

During the COVID-19 crisis, governments gave more direct guidance, through web platforms or other routes, on high-quality remote teaching tools and resources, while still allowing teachers to adapt or use their own where relevant. Teachers also reported giving more individual feedback to students, and collaborating more with their colleagues than normal.<sup>403</sup> These are important lessons for organising teachers to work better in ‘the new normal’.

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403. Wilson’s 2020 survey of NSW teachers found more than half reported more individual feedback to students than usual, and more than 70 per cent believed there was more collaboration between teachers, see R. Wilson et al (forthcoming).

### Cautiously trial blended learning approaches

Teachers and students have enhanced their digital technology skills during remote schooling, and we should build on those skills. The evidence shows that digital learning can work well when it complements – rather than replaces – face-to-face instruction.<sup>404</sup>

However, it is too early to rapidly expand the use of digital tools in the next six months, because there is still little information on which digital approaches are best.

Over the next two years, Australian governments should fund trials and collect information on what approaches are being used in schools, and which are proving most valuable.

### 8.4 We should be more prepared for remote learning in future

Australian governments did a lot to support remote schooling. They developed online platforms with digital tools and sample lesson plans, expanded access to digital devices and the internet, and provided supplementary hard-copy materials for students who could not connect to online platforms.

But the COVID-19 crisis caught schools and policy makers off guard. We must be better prepared next time. Remote schooling may be needed again if there are local outbreaks of infection or a second wave (Chapter 2).

Australia can learn from high-performing countries who were well prepared for remote schooling. Singapore had a fully online curriculum ready to go, and Hong Kong had digital resources aligned to the curriculum that could be easily shared.<sup>405</sup>

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404. Evidence for Learning (2020).

405. See NCEE (2020).

More fundamentally, several top-performing jurisdictions had ways of monitoring the quality of the digital tools and resources provided – drawing on their expert teachers to provide quality assurance. In Singapore, for example, many of the digital resources included in the centralised online platform are created by a team of expert teachers already working full-time at the Ministry of Education. Australia does not have such a layer of expert teachers to help provide quality assurance on teaching materials and approaches.<sup>406</sup>

### 8.5 Bailouts for private schools should be avoided unless their financial viability is threatened

Independent and Catholic schools may ask governments for extra financial support in coming months and years, as the effects of the virus and rising unemployment mean fewer families can afford their fees.

This is an especially thorny public policy issue. On the one hand, non-government schools cater for about 40 per cent of students in some states and territories.<sup>407</sup> If their financial viability is threatened, this is a major problem, because public schools may not be able to cope with the large influx of students. On the other hand, there are likely to be other high priorities for education funds at the same time.

The ‘right’ policy decision here is largely a values-based judgment on the extent to which we value school choice over other education priorities. It will also depend on the extent to which there is a genuine risk to school supply.

Governments should determine whether a school’s financial viability is genuinely threatened before stepping in to bail it out. Many

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406. For discussion of our recommended reforms to create expert teachers see Goss and Sonnemann (2020).

407. In major cities, non-government schools cater for more than 50 per cent of secondary students in some jurisdictions: PC (2020).

non-government schools, especially those serving advantaged students, provide 'gold-plated' facilities and activities, such as smaller class sizes, rowing camps, or indoor swimming complexes. In hard economic times, where parents cannot afford the fees to cover such activities or facilities, schools should first be forced to make tough decisions on whether their cost-structures are right in the circumstances.

In cases where non-government schools can demonstrate they have reviewed their cost structures and found that their financial viability is genuinely threatened, we recommend any extra funding be provided from the Federal Government's \$1.2 billion Choice and Affordability Fund for Catholic and independent schools.<sup>408</sup>

In May this year the Federal Government offered struggling non-government schools early access to future funding.<sup>409</sup> Given this extra windfall for non-government schools would be on top of already generous funding in the Choice and Affordability Fund, we do not recommend that that policy be repeated.

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408. Goss (2019).

409. Tehan (2020b).



## 9 Strengthening institutional oversight

The coronavirus crisis upended Australia's political institutions. Some changes, such as the suspension of federal and many state parliaments, were temporary. Others, including the new National Cabinet, are here to stay. Given the significant policy challenges ahead, robust institutions and strong oversight are more important than ever.

Oversight of government spending and health decisions should be restored as a matter of priority. Extraordinary measures may have been warranted early in the crisis but the special powers granted, and the volume of public money being spent, warrant much stronger oversight in the recovery period.

Parliaments around the country should return as a matter of urgency – virtually if need be and with ‘catch-up’ sitting days – to debate these issues. Governments should be open and transparent about their decision-making through this period to enable public scrutiny. And the Federal Government should follow through on its election promise to establish a national integrity commission, to deal with any integrity concerns that arise through the recovery.

The National Cabinet was an important innovation during the pandemic, promoting national coordination and messaging on the health and economic responses. There are no shortage of important federal-state policy issues for it to grapple with in the recovery phase and beyond – including reforms to the health system, education and training, tax, and energy. The key question is whether national unity and streamlined decision-making can be maintained beyond the crisis.

### 9.1 National Cabinet leading the way and Parliament suspended

A National Cabinet was established on 13 March to lead and coordinate Australia's response to the coronavirus crisis.<sup>410</sup> Bringing together the Prime Minister and all state and territory premiers and chief ministers, it has met most weeks since. The National Cabinet has worked through problems (such as supplies of personal protective equipment and the number of intensive care beds) and provided direction (for example on social distancing requirements and support for households and businesses).

This new forum enabled rapid executive decision-making as the crisis unfolded, as well as information sharing between jurisdictions.<sup>411</sup> The states and territories have primary responsibility for public hospitals, public health, schools, and emergency management, including the imposition of lockdowns and social distancing restrictions. The Commonwealth has primary responsibility for income and business support programs. Coordination of these responsibilities has been crucial.

On 23 March, 10 days after the National Cabinet was established, Federal Parliament was suspended.<sup>412</sup> Most state and territory parliaments also adjourned.<sup>413</sup>

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410. Morrison (2020b).

411. Menzies (2020).

412. The original suspension would have resulted in the House of Representatives missing 21 sitting days and the Senate 23 days. Parliament temporarily resumed on 8 April to approve the Coronavirus Economic Response Package, and on 12-14 May for a ‘trial sitting’. It returned to normal operations in mid-June, so in the event about two sitting weeks were missed.

413. The NSW Parliament originally adjourned until 15 September, the Tasmanian Parliament until late August, and Parliaments in Victoria, Queensland, and the NT until a new date could be agreed. These parliaments have since sat on just a

While it might appear as if one forum temporarily replaced the others, they do not serve the same function. The National Cabinet allows for coordination, negotiation, and compromise, while Parliament is more about scrutiny, debate, and representation.<sup>414</sup>

Australian Parliaments have sat through previous crises – including wars, natural disasters, the Great Depression, and the Spanish Flu.<sup>415</sup> The rationale for suspension in this crisis seems to have been to protect the health of parliamentarians and their staff. A virtual parliament would resolve these issues,<sup>416</sup> but Australian governments did not take steps to establish one. Instead, Australia has had two crucial months without a functioning parliament and the democratic legitimacy and scrutiny it provides.<sup>417</sup>

## 9.2 Special powers and unprecedented spending

Authorities have been granted extraordinary powers to try to prevent the spread of coronavirus in Australia,<sup>418</sup> and ministers have more discretion than ever.<sup>419</sup> These powers, combined with the urgency of the response and only limited oversight, come with risks – for civil liberties, trust in institutions, vested interest influence, and inefficient use of taxpayer funds.

Governments have introduced penalties designed to discourage activities that might spread the virus, with on-the-spot fines of \$1,000+.

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handful of occasions. By contrast, the South Australian and Western Australian parliaments did not adjourn, and the ACT Legislative Assembly missed only two sitting days.

414. Menzies (2020).

415. Carr (2020).

416. Twomey (2020). The UK had one up and running in April: UK Parliament (2020).

417. S. Long (2020a).

418. Emergency powers mostly rest with the states, but the Commonwealth has some emergency powers under the Biosecurity Act, which have been used to ban cruise ships and overseas travel.

419. Tham (2020a).

In some states, people can be sent to jail for up to six months if they fail to comply with ministerial directions.<sup>420</sup> The new restrictions were introduced quickly, and are vague in some cases, leading to some instances of highly subjective policing.<sup>421</sup> The Australian Defence Force has been deployed to support policing efforts, on the streets and at our borders.<sup>422</sup> In normal times, the use of the military in these contexts would be unthinkable.

Mass surveillance capability has been rolled out via the COVIDSafe app to help track and trace the virus. While the app itself looks to be well-designed to protect the privacy of Australians, concerns remain about what happens to the data and capability after the crisis.<sup>423</sup>

There has been a substantial shift in decision-making in recent months, from federal and state parliaments to individual ministers.<sup>424</sup> The federal Finance Minister has been granted extraordinary discretionary spending authority – with the normal discretionary fund of \$1.2 billion per annum for unforeseen expenses increased to \$40 billion on the eve of the parliamentary shutdown.<sup>425</sup> This authority gives the Government enormous flexibility in spending, without any regular reporting requirements. The Treasurer has also been granted extraordinary discretion in the design of the \$70 billion JobKeeper scheme.<sup>426</sup> And state ministers have special powers to fast-track planning and development approvals without the usual checks.<sup>427</sup>

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420. Boseley and Landis-Hanley (2020); and NSW Government (2020b).

421. COVID Policing Australia Coalition (2020); and Reinecke and B. Lowe (2020).

422. Sharland (2020).

423. Duckett and Mackey (2020); and Reinecke and B. Lowe (2020).

424. Tham (2020a). Federal and state Cabinets have also been sidelined, e.g. Towell (2020).

425. Coorey (2020).

426. Tham (2020a).

427. e.g. Clayton Utz (2020).

The coronavirus response has prompted unprecedented government spending (Section 3.2) with limited oversight. The Federal Government's biggest economic response package, JobKeeper, was approved during a special one-day sitting of Parliament with little time for debate. There's no doubt the package was urgently needed, but in the rush, significant flaws in the design were not fixed (see Section 4.3.1), and there have been reports of rorting.<sup>428</sup> A proliferation of new programs and grant schemes have been rushed through state parliaments too. Many of these present risks for effective competition (see Section 4.6) and vested interest influence.

Federal and state governments are also relying heavily on delegated legislation in the COVID-19 response.<sup>429</sup> Normally, new regulations and grant programs are debated by parliament and amended if necessary, before being voted on. But delegated legislation allows the government to change laws without parliament having a direct say, as long as those laws link back to a main piece of enabling legislation.<sup>430</sup> Even before the crisis there were concerns about overuse of delegated legislation, with almost \$5 billion spent by the Federal Government in 2019 under these special conditions.<sup>431</sup> Since February this year, more than 180 new federal regulations have been enacted via delegated legislation as part of the COVID-19 response.<sup>432</sup>

### 9.3 Limited oversight

Sitting parliaments would normally help to work through these issues. In their absence, the main avenues of scrutiny have been media conferences and parliamentary committees.

Parliamentary committees can provide some oversight by questioning decision makers. A Senate Select Committee on COVID-19 was established on 8 April to 'inquire into the Australian Government's response to the COVID-19 pandemic'.<sup>433</sup>

The committee has a big job ahead of it – even with broad powers and plenty of time.<sup>434</sup> It intends to scrutinise decisions of ministers and public servants, as well as hearing from the community via regular public hearings.<sup>435</sup> But the real power and 'bite' of parliamentary committees depends on a sitting parliament.<sup>436</sup> The committee's scope is also limited to federal government decisions, so scrutiny of National Cabinet decisions may be tricky. Most states have established equivalent committees, but Western Australia and Tasmania have not.

There is much greater secrecy around National Cabinet than around its predecessor COAG (the Council of Australian Governments). COAG decisions were made public within a week, whereas National Cabinet decisions are released when the participants choose.<sup>437</sup> National Cabinet meetings to date have typically been followed by a media conference, but there is no formal obligation to have a conference, and it is not clear whether these conferences cover all decisions made. National Cabinet has not released communiqués, as COAG previously did, and National Cabinet papers appear to be exempt from Freedom of Information laws.<sup>438</sup>

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428. Hitch (2020).

429. Parliament of Australia (2020); and Moulds (2020).

430. Parliament of Australia (2018).

431. Middleton (2020).

432. As at 16 June: Parliament of Australia (2020).

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433. Senate (2020).

434. It is due to report on or before 30 June 2022.

435. Karp (2020d).

436. Joo Cheong Tham, Constitutional Government webinar, 7 May 2020.

437. Schultz (2020).

438. Ibid.

## 9.4 Trust in government

Australians' trust in their governments and political leaders has been falling for more than a decade.<sup>439</sup> Yet during this pandemic Australians have placed extraordinary faith in government decisions – accepting new rules and severe restrictions on their freedoms and livelihoods to reduce the spread of the virus.<sup>440</sup>

Australians generally support the national response.<sup>441</sup> Australia has fared very well compared to other countries, and the vast majority of Australians recognise that.<sup>442</sup> The approval ratings of all federal and state leaders grew during the crisis and remain high (Figure 9.1).<sup>443</sup> Crises can forge a sense of the common good and give leaders an opportunity to shine – but the 2019-20 bushfire crisis showed that this is by no means a given.

Maintaining trust will be important in the post-pandemic rebuild. The recovery stage will test Australians' trust, particularly as major support programs such as JobKeeper are unwound. Long-term reforms to boost productivity will be required in the coming years – and trust could be a major determinant of their success or failure. People are less willing to accept 'difficult but necessary' reforms when they do not trust their government, and fear it will not cushion the losers.<sup>444</sup>

Federal and state leaders have an opportunity to build and maintain trust through this crisis through open communication and evidence of progress. But it won't be easy.

439. Griffiths and D. Wood (2020); and D. Wood et al (2018a).

440. Innis and Young (2020).

441. Melbourne Institute (2020b); and Kassam (2020).

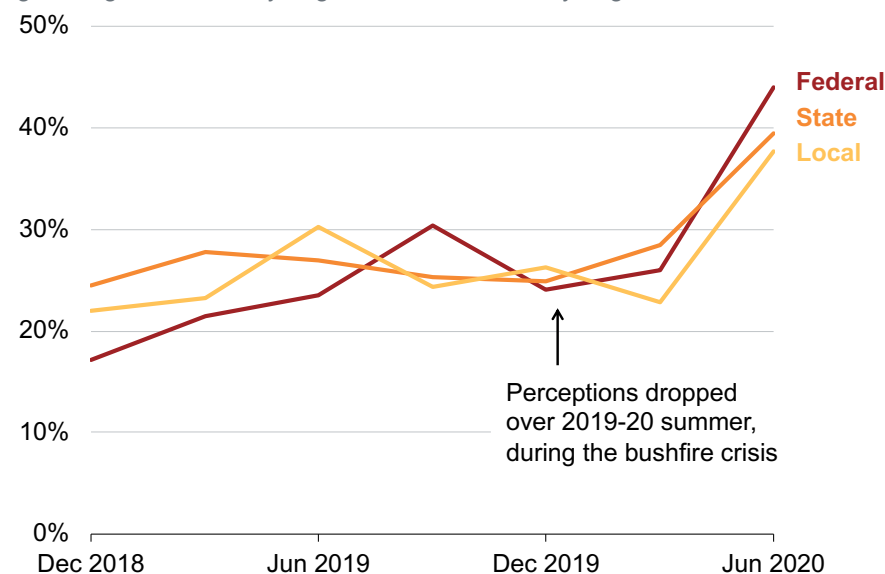
442. 93 per cent of Australians surveyed say Australia has handled the COVID-19 coronavirus outbreak 'very well' or 'fairly well' so far: Lowy Institute poll, May 2020, Kassam (2020).

443. S. Wilson et al (2020).

444. Griffiths and D. Wood (2020).

**Figure 9.1: Australians' perceptions of federal and state leadership have improved during the crisis**

Percentage of Australians who think that governments show 'leadership for the greater good' to a 'fairly large extent' or 'extremely large extent'



Sources: S. Wilson et al (2020) and ALI (2020).

## 9.5 What we need to do

In times of crisis, transparency and accountability are more important than ever.<sup>445</sup> A short period of reduced oversight may have helped enable a more rapid executive response, but the longer it continues, the greater the risks. The special powers granted, and the volume of public money being spent, warrant much stronger oversight.

Interest groups are already knocking on government doors – many with valid concerns – and this is only likely to escalate in the next phase of recovery as current support measures are wound back. Governments should be open and transparent about these important discussions, allowing for public scrutiny and debate.

Cooperation between state and federal governments has been a big success of the response to date. Governments should build on this capability and goodwill by committing to a joint reform effort on funding and responsibilities after the crisis.

### 9.5.1 Strengthen oversight

The checks and balances of parliamentary democracy have never been more necessary. The ‘complex moral calculus’ of this crisis calls for accountability through parliamentary and public debate.<sup>446</sup> Parliaments around the country should resume – virtually, if need be<sup>447</sup> – and make plans for ‘catch-up’ sitting periods. Parliaments should reduce ministerial discretion by amending COVID-19 legislation to include clear rules where practicable.<sup>448</sup>

Scrutiny of National Cabinet decisions is essential. For the time being, this task will probably fall to state and federal parliaments and

parliamentary committees. But now that the National Cabinet is a permanent institution, replacing COAG,<sup>449</sup> it should develop rules to provide some transparency – including publishing agendas and decisions within a reasonable time-frame after meetings.

The Senate Select Committee on COVID-19 should ensure that each new regulation in response to COVID-19 is ‘necessary and proportionate to the health risk posed and does not unduly impinge on personal rights and liberties’.<sup>450</sup> The committee should call on other parliamentary committees and independent reviews to support its inquiry. The Australian National Audit Office should get more resources to enable an independent audit in 2021 of the COVID-19 response.

Similar parliamentary inquiries are needed at state level too – Western Australia and Tasmania should establish their own inquiries, and state committees should work together, and with the federal committee, to examine National Cabinet decisions as needed. State audit offices should also review the various state-based grant schemes in the wake of the crisis.

The Australian Public Service is playing a critical role in designing policy responses and delivering services at a greater scale than ever. The Federal Government should ensure the APS is properly resourced and able to hire through this period. In particular, agencies that deal directly with the public, such as Services Australia and the Australian Tax Office, have had a significant increase in work and will need extra resources.

### 9.5.2 Ensure integrity

State integrity commissions should keep a close eye on the COVID-19 response and recovery. The NSW Independent Commission Against

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445. Lillywhite (2020); and Tham (2020b).

446. Tham (2020b).

447. Twomey (2020).

448. Tham (2020a).

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449. Morrison (2020c).

450. Moulds (2020).

Corruption (ICAC) has published guidelines for agencies on corruption risks in periods of disruption and economic downturn – some arising from new working arrangements and others associated with emergency procurement and rushing out new services.<sup>451</sup> Victoria's Independent Broad-based Anti-corruption Commission (IBAC) is overseeing the policing of COVID-19 restrictions.<sup>452</sup> Other state commissions continue to manage complaints and provide a gateway for whistle-blowers.

But at the federal level, despite commitments in 2018 from both sides of politics, there is still no integrity commission. Federal Parliament should establish a national integrity commission within the next year. A cross-party Senate committee should be established immediately to put forward a proposed model.<sup>453</sup> A national integrity commission should be up and running to deal with any integrity concerns that arise through the recovery, to provide a safe gateway for whistle-blowers,<sup>454</sup> and as a commitment to maintaining the trust of the Australian people.

The creation of the Government's National COVID-19 Coordination Commission – a select group of business leaders advising the Prime Minister on 'all non-health aspects of the pandemic response'<sup>455</sup> – raises several red flags. Australians have been told very little about it, and it does not appear to be underpinned by legislation.<sup>456</sup> Concerns have been raised about conflicts of interest,<sup>457</sup> and the commission

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451. NSW ICAC (2020).

452. Vic IBAC (2020).

453. Hamilton and Kells (2020).

454. A. Brown (2020).

455. PMC (2020).

456. S. Long (2020a).

457. Murphy (2020). Some members of the commission have interests in the energy and resources sectors, and leaked documents suggested the commission planned to call for government support for the gas industry (S. Long (2020b)). Around the same time, the federal Energy Minister was spruiking a 'gas-led recovery' (O'Malley and Foley (2020)), and the Department of Industry published a Technology Investment Roadmap discussion paper detailing a future role for gas (Department of Industry (2020)).

has failed to answer Senate committee questions about its formation, role, and management of conflicts.<sup>458</sup> The Government should clarify the commission's role, and the commission should publicly disclose any conflicts of interest, as well as publishing regular updates on its deliberations.

With many different groups vying for government attention and support in the wake of the crisis, transparency around lobbying activity will be more important than ever. Access and influence are inextricably linked, so it's important the public can know who meets with senior policy makers.<sup>459</sup>

Federal and state ministers should publish their diaries regularly – as ministers in NSW, Queensland, and the ACT already do.<sup>460</sup> For example, all official meetings for one month could be published by the end of the following month, as already happens in Queensland. Publishing ministerial diaries would enable public scrutiny of who ministers are meeting (and not meeting) through this particularly crucial period – and may encourage policy makers to seek out a wider range of views.

Urgent times may call for urgent measures, but transparency in government decision-making is essential to counter the risks of undue influence and the potential for (knowingly or unknowingly) misusing public money and power in the rush.<sup>461</sup>

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458. Secombe (2020). Only one of the six members has voluntarily released a conflict-of-interest declaration: Knaus (2020).

459. D. Wood et al (2018b).

460. Ibid (pp. 57–58).

461. Lillywhite (2020).



### 9.5.3 Promote federal-state cooperation

The National Cabinet has been one of the great innovations of the coronavirus pandemic, replacing the fractious talkfest between the heads of Australian governments, known as COAG.<sup>462</sup>

Gone were the demeaning fights over money where the mendicant states sought more largesse from the Commonwealth. Ushered in was a new era of cooperation where federal, state, and territory leaders exercised their 'joint responsibility to act to protect the Australian community by ensuring that the health system can respond effectively to the outbreak of Novel Coronavirus', as the COVID-19 National Agreement phrases it.<sup>463</sup>

The Prime Minister announced in May that the National Cabinet would be made permanent, and 'COAG is no more'.<sup>464</sup> But can the new cooperative spirit survive?

The pandemic created a peculiar dynamic that allowed this cooperative regime to flourish. As the scale of the pandemic became apparent, tough decisions about lockdowns needed to be made. And with the states responsible for emergency management, schools, and public health, the big lockdown decisions actually rested with them.

But it will be harder to maintain national unity in the next phase of this crisis. Over time, motivations for cooperation will dissipate, and the balance of power will shift back to the Commonwealth.

Nonetheless we should hope that it does not revert to the old logjam. Significant cross-jurisdictional challenges remain on education and skills, health, tax, and energy and climate-change policy. Coordination on economic stimulus will also be pivotal in the next six months (Chapter 3).

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462. Duckett and Stobart (2020).

463. NPA (2020).

464. Morrison (2020c).

National Cabinet will meet more frequently than COAG did, and this may help the collaborative spirit endure.<sup>465</sup> And there is a shared interest in improving productivity – recent borrowing has put immense pressure on state and federal budgets alike.

Major structural and fiscal change will be needed, and that will have to be negotiated between the Commonwealth and the states. The National Cabinet should continue to draw on expert advice to inform decision-making, as it has done throughout the crisis.<sup>466</sup>

The Prime Minister says the National Cabinet will work closely with the Council on Federal Financial Relations (the meeting of federal and state treasurers). One of the council's first tasks is to 'consolidate and rationalise' funding agreements between the states and the Commonwealth.<sup>467</sup>

No doubt there are opportunities here, but some of the biggest economic gains to be made are in tax reform, including replacing stamp duties with a broad-based property tax, and broadening and raising the GST.<sup>468</sup> The council and National Cabinet should not shy away from these tough but necessary reforms.

Grattan Institute will explore some of the medium and longer-term opportunities in future work.

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465. National Cabinet will meet at least fortnightly for now, and monthly in a 'normal year'. COAG met 2-to-4 times a year. The Australian Local Government Association (which was part of COAG) will be invited to meet with the National Cabinet only once a year: Morrison (ibid).

466. Medical/health advice has been given primacy in National Cabinet meetings, supporting evidence-based decision-making (see Chapter 7).

467. Morrison (2020c).

468. Daley et al (2018b); and Daley et al (2019).

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