

The Economics of Population Growth

The elephant in the room for Australia's Federal Parliament has finally been called out. Australia's rapid population growth is arguably as important an issue as balancing the budget and the environment. Yet almost no one has dared to mention it since Kevin Rudd talked of a "big Australia" in 2009. This failure to talk about it doesn't mean that politicians don't have a view. The major parties, by their actions have tacitly continued to implement a big Australia policy. Even the minor parties have said little and it has been left to non-politicians like Dick Smith to raise the issue.

Dick Smith's involvement is indicative of the low quality of economic understanding when it comes to the implications of population growth. He's half right and half wrong in his major claims that population growth makes housing more unaffordable (right) and will increase unemployment (wrong). This article brings basic economic principles and observations to the debate. It discusses both the obvious and the unseen implications of population growth, with the aim of allowing all Australians and particularly our leaders to consider whether a bigger Australia is better.

Australia's Population Growth is Abnormal

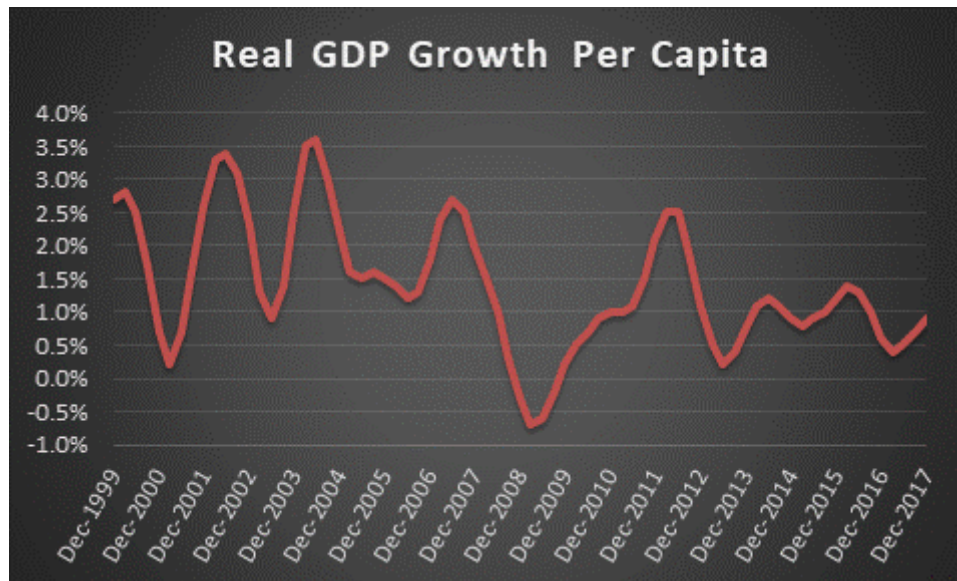
Over the last decade Australia has averaged annual population growth of 1.7% compared to 0.8% in the US and 0.1% in Europe. Of the world's wealthy nations only Singapore and Israel had similarly high levels, although Singapore has pulled back substantially with only 0.1% growth in 2017. Over the decade, 41% of Australia's population increase has come from natural growth (births minus deaths) and 59% has come from net migration.

However, this split of population growth between natural growth and migration is deceptive. [Since 1976](#) Australia has had a fertility rate (average births per woman) of less than the replacement rate of 2.1. Whilst much of the natural growth is due to increased lifespans, migration plays a major part. Australia's migrants are predominantly aged under 40, making most of them in, or soon to be in, their most fertile years. Once in Australia their future children count as natural population growth. Whilst there are many good arguments for focussing Australia's migration intake on highly skilled younger people we need to acknowledge that this group will have a secondary boost on our population by having children after they arrive.

Population Growth and Economic Growth

At the most basic level, population growth increases the total size of the economy including the demand for labour. There are more people purchasing goods and services so the economy grows to meet that demand. Politicians are positively disposed to population growth as it allows them to boast about economic growth and job growth. Big businesses love population growth as they are able to grow their customer base without having to aggressively compete. Unions may also benefit from population growth as it increases the total size of labour force and their pool of potential members.

However, this is a very shallow line of thinking as ordinary Australians have been receiving little benefit from broadly measured economic growth. Ordinary people want their incomes to increase relative to their expenses and this requires real (after inflation) GDP per capita growth. As the graph below shows, real GDP per capita growth has averaged less than 1% over the last decade. This explains much of the disquiet amongst Australians with both major parties since the end of the Howard/Costello government. Australians became used to stronger growth in real incomes and are now unhappy that this has slowed.



Source: [ABS](#)

Population Growth and Employment

The lie that population growth takes jobs fools many as it contains a kernel of truth. On an overall basis, skills based migrants (but not family and humanitarian migrants) are likely to create slightly more jobs than they take through their upskilling of the workforce and broader contribution to the economy.

However, some migration does take jobs that would have otherwise gone to Australians. Several sectors such as restaurants, construction, mining and technology have found that it is easier and cheaper to hire a skilled worker from overseas than to train a local to do the job. For technology, it is arguable that a business would relocate some or all of its operations overseas if it cannot get the skilled workers they need in Australia. However, in restaurants, construction and mining jobs rarely can be outsourced overseas.

There are two issues behind the problem of businesses looking to import labour. First, in some cases businesses are neglecting their social responsibility to train the workers they need. There are substantial discounts to the minimum wage for many trainees, apprentices and employees aged under 21. There are government schemes encouraging traineeships and apprenticeships, as well as low cost training via TAFE. In some sectors, the availability of visas should be withdrawn altogether and businesses should source their employees solely from the domestic population.

Second, there is a willingness to work issue amongst a small portion of Australians. This is particularly apparent in unskilled jobs, which are often filled by backpackers and overseas students. The levels of unemployment and underemployment indicate that some Australians prefer to live on welfare (often topped up with cash in hand jobs) rather than take an unglamorous job. Welfare and tax reform aimed at eliminating the “welfare trap” and more stringent testing of attempts to find work are required. In extreme cases, unemployed people should be directed to attend a workplace with a vacancy rather than being given continued flexibility to search for their ideal job.

Population Growth and Housing Affordability

Whilst there are many factors that impact housing affordability, rapid population growth is arguably the largest contributor to Australian housing being amongst the most expensive in world. Housing (both purchasing and renting) functions like almost all other markets in that demand and supply determine the price. Rapid population growth is a

continual boost to the demand for housing. The supply of housing has struggled to keep pace with demand growth, as evidenced by rent and house prices rising much faster than inflation for several decades.

Reducing the migration intake is [just one of eight reforms](#) politicians should pursue to make housing more affordable. Of the eight reforms, it is amongst the least controversial and would have the most impact. If Australia was to dramatically slow its population growth (most easily achieved by reducing the migration intake) the stock of available housing could increase faster than demand for it. The basic laws of demand and supply would then see rents and house prices fall as the number of vacant properties increased. Slowing the rate of population growth would have a secondary impact on prices as the cost of building would fall as the stretched capacity in the construction industry returned to normal levels.

Quality of Life Impacts

Even if discussions of economic growth are shifted to a real GDP per capital basis that still ignores the quality of life impacts. Roads and public transport have become more congested, capacity at schools and hospitals is stretched and housing must densify to cope. As backyards become less common, the use of public spaces like beaches, parklands and sporting fields increases. Governments often respond to the increased usage by implementing user pays charges, (e.g. toll roads and parking meters) another impost on citizens who are already angry that the quality of services they receive for their taxes appears to have declined. For the average citizen, a bigger Australia is not a better Australia.

Population Growth is Expensive

Whilst the broad economic growth that comes with population growth is obvious, the financial cost of the growth is often forgotten. The infrastructure spending binges in Sydney and Melbourne will need to continue for decades if population growth doesn't slow. These projects create a temporary boost to the economy and employment but are a huge impost on government budgets. Rapid population growth makes these projects even more expensive as the construction industry is already stretched keeping up with the demand for additional housing.

The lack of available land means most new transport projects require tunnels. These are many times more expensive than previous projects, as tunnels are far more expensive to construct than above ground road and rail infrastructure. If Australia's population was stable only a small fraction of current infrastructure spending would be required to maintain the existing infrastructure base.

Will Cutting Migration Cause a Recession?

Proponents of high population growth often argue that if Australia stopped its rapid population growth a recession would ensue. Superficially this seems correct as construction and associated industries employ a material portion of the population. However, as discussed in the previous paragraphs rapid population growth is expensive for governments. A slower level of population growth would require less infrastructure spending. This would allow governments to cut taxes, increasing spending in other areas or a combination of both. If taxes were cut, residents would allocate their increased spending power to other areas of the economy offsetting the reduction in construction.

What About an Ageing Population?

The Productivity Commission has substantially debunked the arguments that Australia needs migration to counter the ageing population. It [noted in its 2016 report](#) that migration "does not offer a long term panacea – immigrants age too". Australia must confront the costs of an ageing population eventually. What is often forgotten is that whilst the population is living longer, it is also healthier for much longer. Despite these substantial health and life expectancy improvements the pension eligibility age has [barely moved in 100 years](#). The obvious solutions are to continue to

increase the starting age for the pension, along with reform of the tax and welfare systems to encourage all adult Australians to work at least part time.

Are There Other Ways to Generate Growth?

As discussed earlier, population growth is a cheap way to generate headline economic growth, but it does little for real GDP per capita. To do this, all levels of government should embark on a wave of taxation and productivity reforms. Taxation reform would encourage underemployed Australians to increase their levels of work, saving and investment. Productivity reform would remove unnecessary regulation and government interference in the economy allowing businesses to produce better goods and services at a lower price.

The analysis of these reforms has already been done by the Henry Review, the Tax White Paper process and the Productivity Commission. It's a matter of having the political leadership and courage to implement them. Together these reforms will increase incomes and decrease the cost of living, delivering the disposable income growth Australians are demanding.

Who Should We Encourage to Migrate to Australia?

Given growth is expensive, Australia should focus a limited migration program on new residents who will be substantial taxpayers, more than covering the costs they create by their addition. This program would encourage high skill and high wealth migrants. High skill migrants that earn high wages pay material income tax and GST. They also assist Australian businesses to be internationally competitive thus increasing our exports. High wealth migrants should be encouraged to live and invest in our economy, with the additional jobs and taxes generated a net positive. High wealth migrants are likely to purchase very expensive properties, generating substantial property tax revenues with little impact on the pool of affordable housing.

The Refugee Question

The United Nations currently cites [65.6 million people as forcibly displaced](#) and 17.2 million people as UNHCR refugees. Australia's annual humanitarian intake is less than 0.1% of UNHCR refugees and 0.03% of forcibly displaced people. Even if all wealthy nations were as generous as Australia in accepting humanitarian migrants only a tiny portion of these groups would ever be resettled in wealthy nations.

Humanitarian migrants have historically made up 5-10% of Australia's net migration. These migrants predominantly come from [non-Western and non-English speaking backgrounds](#). Whilst not a significant part of total migration these migrants have significant difficulties adjusting to life in Australia, requiring disproportional ongoing government assistance. This assistance is in addition to the costs created by increasing the population.

The approach of Australia and other wealthy nations means that a tiny proportion of potential humanitarian migrants are able to resettle in comparative comfort whilst tens of millions remain impoverished. These migrants create substantial direct and indirect costs. It is arguable that a fairer outcome is to provide greater assistance to a much larger number of displaced people at their current location instead of allowing a much smaller number to migrate to wealthy countries. As an example, Australia spent [\\$9.6 billion in three years](#) on migration and border protection measures. This amount could have bought [32 million temporary family shelters](#) including sleeping mats, blankets, kitchen equipment and a stove.



Conclusion

Australia's rapid population growth has had substantial negative impacts on existing residents, yet Australia's politicians have chosen to not discuss the elephant in the room. This doesn't mean that they don't have a view, their continuation of abnormally high levels of migration shows they are strong supporters of a big Australia. Rapid population growth is expensive and has decreased the quality of life for Australians. Population growth has been poorly managed with vital transport and social infrastructure failing to keep up with the population that uses it.

Arguments that population growth is necessary to avoid a recession or to prevent ageing of the population are erroneous. Australia should implement tax, welfare and productivity reforms to lift incomes, decrease the cost of living and to underpin Australia's future economic prosperity. Migration levels should be dramatically reduced with the migrants selected being those who have the best prospects of contributing more than they cost. More than ever, Australians are looking for political leadership and courage with population growth an obvious area to begin.

Written by Jonathan Rochford for Narrow Road Capital on March 26, 2018. Comments and criticisms are welcomed and can be sent to info@narrowroadcapital.com

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