THE AUSTRALIAN

Asset lottery makes it a merrier Christmas for some

Illustration: Eric Lobbecke

HENRY ERGAS THE AUSTRALIAN 12:00AM December 19, 2016

Little wonder Donald Trump swept the rural states: this year's Christmas Price Index, which calculates the cost of buying the full basket of goods and services specified in *The Twelve Days of Christmas*, shows America's milking maids are doing it tough, as are the country's suppliers of swans, geese and partridges in pear trees.

And the pain extends to Ladies Dancing and Lords Leaping, who, unlike their Australian counterparts, got a pay cut this Christmas.

But their plight didn't stop the US Federal Reserve from raising interest rates, as overall inflation picked up during 2016 to more than twice its 2015 level.

The Fed's move accelerated a bond market sell-off, but it would be premature to say the era of historically low real interest rates is over. Trapped in anaemic growth and low inflation, rates remain negative in Europe and Japan, while China's monetary policy secures the same effect by other means. And even before central banks were driven to those extremes, real rates had been falling for years, with the Asian financial crisis nearly halving global rates in real terms and each subsequent shock reducing them further.

Whether slashing interest rates has done much to stimulate economic growth is controversial. What every Australian knows, however, is that ultra-low rates have lifted asset prices into the stratosphere. In 1980, household wealth in Australia was four times household disposable income; thanks mainly to soaring house prices, that ratio has nearly doubled, with a 2.2 per cent increase in the September quarter taking households' net worth to record levels.

That may ensure Christmas is all the merrier. But one doesn't need to be Scrooge to be wary of the risks. Asset prices are inherently volatile, and they overshoot on the way down as well as on the way up. Yes, easy money can fuel the warm glow of prosperity by doping property values and sharemarkets; that, however, makes economies more fragile, not less.

Yet it isn't merely the economic consequences of asset price inflation that are worrying. From Max Weber to Talcott Parsons, the great social theorists of the 20th century regarded the declining significance of wealth compared to labour income as a crucial source of progress.

In societies in which living standards depended primarily on earnings from employment, rather than on financial wealth, education and hard work would be the key to affluence, motivating achievement and the willingness to make sacrifices. In contrast, asset price inflation delivers gains like manna from heaven, undermining the social standing of effort.

And social cohesion suffers too. Typically, people's pay has some legitimacy to it, at least in terms of overall rankings: while there may be arguments about just how much more doctors should earn than dustmen, few would claim the relativity ought to be the other way around. Moreover, the labour market largely treats like alike, keeping disparities in living standards between the similarly placed within reasonable bounds and maintaining a rough justice.

But abrupt changes in financial wealth aren't like that. Wealth is not only more unequally distributed than labour income as between the rich and poor, so that asset price inflation disproportionately benefits the better off, it is also very unequally distributed within income deciles. As a result, when asset prices take off, quite similar households can experience vastly differing gains in wealth, depending as much on luck and location as on acumen and dedication.

Nor are those differences trivial. The sociologist Louis Chauvel found that even within income deciles, the doubling in household wealth that occurred in the first decade of the 2000s caused gains in the consumption levels individual French families could afford that varied from being negligible to nearly equalling their labour earnings.

The rise in asset prices therefore acted as a lottery, giving rise to differences in living standards that lack any clear social legitimacy.

Relations between generations have also been reshaped by the great asset price inflation. When *The Twelve Days of Christmas* was written, short life expectancy, low savings rates and slow economic growth meant inheritance accounted for 90 per cent of the wealth acquired by any cohort; by the 1990s, that share, although variously estimated, had fallen below 25 per cent, so that each generation made its own way in the world.

Now, with rising asset prices boosting wealth while labour incomes stagnate, the leg-up inheritance provides is back as a major social differentiator, potentially transforming the birthright lottery into an even more enduring shaper of life chances.

That corroding the sense of fairness would incite demands for redistribution is understandable. But the politics of envy only tackles symptoms, typically in ways that are as inefficient as they are ineffective.

After all, the mess we're in is due to the slowing in the engine of growth, which has both stalled increases in wages and led to monetary policies that unmoor asset prices from reality. Shuffling the pie around, losing much of it in the process, would scarcely address those causes of our predicament.

Rather, the focus should be on rekindling productivity growth, which would replace artificial increases in financial wealth with sustainable improvements in real incomes.

There is, at last, some welcome news on that front, with Australia's latest national accounts suggesting that the decline in capital productivity that began in 2003-04 has halted, while aggregate productivity growth seems firmly back in positive territory.

Whether that trend continues is a choice, not a fate. Clearly, a huge amount remains to be done, from removing madcap energy policies to cutting too high tax rates.

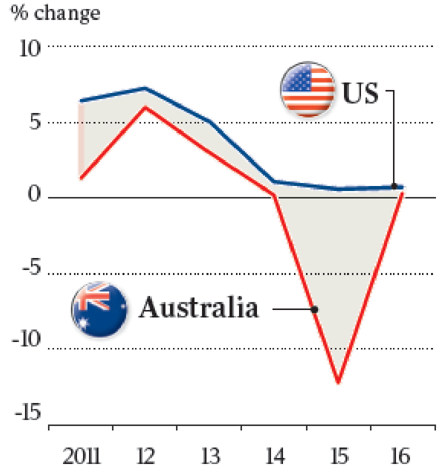
So let's sing, dance, leap, drum and pipe to reform. And hope Christmas brings all good girls and boys the rewards they deserve, and work so hard to achieve.

Annual 12c index

2016 prices	Cumulative price* US	Cumulative price* Australia
Partridge in a pear tree	$3363	$1240
Two Turtle Doves	$5506	$348
Three French Hens	$2423	$1400
Four Calling Birds (canaries)	$7207	$1140
Five Golden Rings	$8009	$13,661
Six Geese (laying)	$3364	$4515
Seven Swans	$105,112	$63,000
Eight Maids Milking	$387	$708
Nine Ladies Dancing	$40,325	$20,990
Ten Lords Leaping	$22,058	$17,492
Eleven Pipers Piping	$7230	$3247
Twelve drummers drumming	$3916	$1771
Total	$208,900	$129,112

US prices expressed in $A at 15-Dec-15 AUD/USD exchange rate

Christmas price 'inflation' index



*Total price multiplied by the number of times the gift is repeated in the song