Senate Standing Committee on Economics

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates, 2 June – 4 June 2009

Question: **bet 83**

Topic: **CPRS Modelling**

Hansard Page: **E97-98**

Senator Boswell asked:

Senator BOSWELL—This is my last question. You did not model the fact that Australia or the world was in a recession. You put in an assumption that there would be no unemployment in two of your three models. You then assumed that the rest of the world was going to follow. There are three major assumptions that you have made and I do not believe that is an accurate way to model. That is almost asking a question to get the result that you wanted. We know in politics that if you want an answer you ask a question in a certain way. I suspect you have fallen for that. You have been asked to ask questions in a certain way so you will get an answer. Thank you very much.

Ms Quinn—I will just respond. There was some incorrectness in your statement. One of the models that we used suggested that employment is in equilibrium in the short term. Two of the models assume that there was a change.

Senator BOSWELL—You are going to give me the information on how that modelling worked?

Ms Quinn—I am happy to take that on notice. We were asked about the implications of putting emission pricing in the Australian economy. We were not asked to look at the global financial crisis. We looked at the implications for the Australian economy of putting a price on emissions, and that is the analysis that we did. We were not instructed to produce particular results. We were asked to examine the implications of different emission targets over the medium to long term, and that is the analysis that we provided to the Australian people through the Australian government.

Answer:

The three computable general equilibrium (CGE) models used in the Government's *Australia's Low Pollution Future: The Economics of Climate Change Mitigation* (*ALPF*) report, make different assumptions about the short-run dynamics of the labour market.

- The Global Trade and Environment Model (GTEM) is at one end of the spectrum. It assumes that labour and capital are perfectly mobile across industries, at all times and at no cost.
- The G-Cubed model is at the other end of the spectrum. It assumes immobility of capital, slow adjustments to wages and liquidity constraints, and includes partial forward-looking behaviour.
- The Monash Multi-Regional Forecasting (MMRF) model assumes capital, labour and abatement technologies take time to adjust, capturing the short-term adjustment cost mechanisms in the economy. In particular, the MMRF model assumes that it takes between seven and ten years for the labour market to adjust following an economic policy change.

All three CGE models assume that in the long run, in the absence of any further change in policy, real wages will adjust such that aggregate employment levels return to their pre-policy levels.

All three CGE models have been developed over time by independent researchers and have been used extensively in peer-reviewed literature. The Government ALPF report drew on, and reported results from, a suite of economic models to encompass the wide variety of academic views about how the Australian economy responses to policy changes.