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COMMITTEE ON STATISTICS

Working Party on National Accounts

Real income and its allocation

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This document has been prepared by Michael Davies (Macroeconomics Statistics, ABS -Australia) and will be presented under item 9 of the draft agenda.

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Real Income and its Allocation

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2008 SNA treatment of retained earnings

• The 2008 SNA treats certain retained earnings of corporations as if distributed and remitted to investors while other retained earnings are held by the domestic corporation in the form of net saving.

• Where foreign investment is concerned, this treatment is only applied to the retained earnings of foreign direct investment enterprises and investment funds.

• This treatment is not applied to the retained earnings on all other foreign investment (i.e. portfolio investment).
Retained earnings and real incomes

• Real incomes show how the purchasing power of domestic income is affected by terms of trade changes, income flows to and from the ROW, and the consumption of capital.

• But these aggregates are affected by the inconsistent treatment of retained earnings.

• Income flows to and from the rest of the world exclude retained earnings on portfolio investment payable to and receivable from abroad. This income is retained by domestic corporations as net savings.
Australian real incomes

- Australia has a mining boom which has taken place over most of the last decade.
- Between 2002-03 and 2010-11, average annual GDP in volume terms growth was 1.3% while real net national disposable income (RNNDI) growth was 4.1%.
- However, portfolio investment and net savings of corporations also increased over this period.
- Real income gains may have been misstated due to the inconsistent treatment of retained earnings.
Australian real incomes, 1999-00 to 2010-11

Notes: Chain volume measures ($m) expressed in index form
Base year for indexes is 1985-86 = 100.
Reference year for chain volume measures is 2009-10 = 100.

Source: ABS Cat. No. 5204.0, Table 1
Alternative Australian real incomes, 1999-00 to 2010-11

• Tests the sensitivity of Australian real incomes to the inconsistent treatment of retained earnings.
• Produces alternative estimates by allocating net savings of domestic corporations to investing sector and doing the same for Australian foreign investment.
• Affects net income payable abroad as retained earnings on foreign portfolio investment are fully allocated.
• Most retained earnings flow to domestic investors as the treatment of retained earnings on foreign investment is more comprehensive than on domestic investment.
Real gross national income, 1999-00 to 2010-11

Notes: Chain volume measures ($m) expressed in index form
Base year for indexes is 1999-00 = 100.
Reference year for chain volume measures is 2009-10 = 100.

Source: ABS Cat. No. 5204.0, Table 1, Derived estimates
Real net national disposable national income, 1999-00 to 2010-11

Notes: Chain volume measures ($m) expressed in index form
Base year for indexes is 1999-00 = 100.
Reference year for chain volume measures is 2009-10 = 100.

Source: ABS Cat. No. 5204.0, Table 1, Derived estimates
## Composition of real income growth, 1999-00 to 2010-11

<table>
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<tr>
<th></th>
<th>Published</th>
<th>Alternative</th>
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<tr>
<td></td>
<td>1999-00 to 2002-03</td>
<td>2003-04 to 2006-07</td>
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<tr>
<td>GDP in volume terms growth</td>
<td>3.0% 3.5% 2.4%</td>
<td>3.0% 3.5% 2.4%</td>
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<td>RGDI effect</td>
<td>0.3% 1.6% 1.4%</td>
<td>0.3% 1.6% 1.4%</td>
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<tr>
<td>RGNI effect</td>
<td>0.0% -0.5% 0.2%</td>
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<tr>
<td>RGNDI effect</td>
<td>0.0% 0.0% 0.0%</td>
<td>0.0% 0.0% 0.0%</td>
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<tr>
<td>RNNDI effect</td>
<td>-0.2% -0.2% -0.3%</td>
<td>-0.2% -0.2% -0.3%</td>
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<td>RNNDI growth</td>
<td>3.1% 4.5% 3.7%</td>
<td>3.1% 4.5% 3.6%</td>
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Note: Average growth in chain volume measures ($m)
Source: ABS Cat. No. 5204.0, Table 1, Derived estimates
Import and gross national expenditure
IPD, 1999-00 to 2010-11

Note: Base year for indexes is 1999-00 = 100.
Source: ABS Cat. No. 5204.0, Table 4
Real gross domestic income, 1999-00 to 2010-11

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<td>2003-04</td>
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<td>2009-10</td>
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</table>

Notes: Chain volume measures ($m) expressed in index form
Base year for indexes is 1999-00 = 100.
Reference year for chain volume measures is 2009-10 = 100.

Source: ABS Cat. No. 5204.0, Table 1, Derived estimates
Findings and conclusion

• Although the 2008 SNA treatment of retained earnings is inconsistent, recent income has not been misstated for the following reasons:
  – The impact on income payable aboard is small as most income is retained domestically and the majority of real primary income payable abroad, mainly dividend and interest payments as well as retained earnings on foreign direct investment, is already recorded as net primary income payable abroad;
  – Most of the real income growth which has produced a divergence between GDP in volume terms and RNNDI is due to the strong contribution of terms of trade gains over recent years. Furthermore, Australian real incomes are largely insensitive to the choice of terms of trade deflator.
Questions?