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Economic statement: experts respond

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Abstract
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A slowing economy and drop in government revenue has led to an increased budget deficit, new taxes and some cuts to existing programs.

Delivering the Rudd government's long awaited economic statement, Treasurer Chris Bowen said the government wanted to avoid "harsh and swinging cuts that would make our economy
smaller and lead to higher unemployment”.

The government warned that the 2013-14 budget deficit is expected to be A$30.1 billion, falling to $24 billion in 2014/15. However, $17 billion in savings, when combined with additional revenue raising measures, would return the federal budget to a $4 billion surplus by 2016/17.

Savings and revenue raising measures announced - some of which had already been reported - include changes to fringe benefit tax arrangements for cars, a levy on banks and increased taxes on cigarettes.

The statement also outlined the costs associated with some programs announced since Kevin Rudd replaced Julia Gillard as prime minister.

The controversial plan to send asylum seekers arriving by boat to Papua New Guinea is slated to cost $1.1 billion over the forward estimates.

The Conversation spoke to economic and political experts about the impact of the pre-election economic statement.

John Wanna, Sir John Bunting Chair of Public Administration at Australian National University

Not sure what all the fuss was about or whether it was worth all the hoopla. The Economic Statement released by treasurer Chris Bowen and finance minister Penny Wong is not so much an economic statement as more a list of policy reminders and bribes, with any bad news (cuts, tightening, lapsed funding of programs) shoved out to the years 2015-17 – that is beyond the end of even the next parliament.

The new taxes or increased charges are largely ad hoc, random and nuisance in character producing very little for whatever political pain is inflicted by the electorate (smoking, company cars, bank deposits tax, unpaid tax swoop, mopping up small superannuation balances, and raising the hoary old efficiency dividend yet again to 2¼ for three out-years. Is this really the best that the government can do?

The document states that fiscal consolidation has slackened pace (p. 2) but does not explain why it has slackened – less than expected revenues are one factor but so too is excessive spending when the government does not yet have the money to spend. The statement admits that we have had seven large deficits straight – since 2008 through to 2015 – that’s a total of $245 billion in cumulative deficits over that period despite the government insisting we would be back in surplus as of last June (an annual average deficit since 2008 of $35 billion).

All major savings measures (cuts, offsets, etc) are shown in the fiscal years 2015-16 and 2016-17 – can we really believe that the government will stand by these austerity measures so far out? Hardly.

The statement reminds us of the need for some important changes as we transition from a mining boom economy to a broader based economy. These include improved productivity, improved competitiveness, innovation, research and development, regulatory imposts, along with hints at greater flexibility in labour markets and industrial relations. But was such a hyped-up statement needed to remind us of these fundamentals which been the subject of debate since the 1980s?

If the government’s Economic Statement was meant to give the Pre-Election Economic and Fiscal Outlook a more rose-tinted slant, then it has probably failed. Maybe the exercise was
one of getting the bad news out before the campaign begins so that the PEFO document produced by Treasury/Finance officials falls flat on its face and no-one pays any attention to it once the campaign is underway. It reminds me of an episode of The Hollowmen.

John Quiggin, Professor, School of Economics at University of Queensland

The government has taken a number of measures necessary to restore revenue to its long-term share of national income, around 25%. Both the increase in tobacco excise and the requirement for banks to pay for the government guarantee they enjoy are sound policy measures.

The changes to FBT arrangements point the way to further repairs of the revenue base. The existence of an entire industry devoted to salary packaging is clear evidence that fringe benefits are a major area of tax avoidance. The ultimate solution should be to make all convert all fringe benefits to taxable income, with the work-related component being claimed as an expense.

Phil Lewis, Professor of Economics at University of Canberra

The major thing people will focus on is: why have these estimates come out now? It's only two months after the budget and we have such a correction in these revenue figures that it's almost unbelievable. I think that's the first question to ask: if the budget estimates are so unreliable, how can we put any faith in these?

I think there is a fundamental structural problem, which is highlighted in the piece I wrote on the budget for The Conversation. I would like to point out the fact that given the erosion of the revenue base under Howard and Rudd, it is very difficult for us to finance continual government spending. So there either has to be a drastic reduction in spending, or they have to solve tax-based problems: which may mean increasing GST or increasing the coverage of the GST.

What we see here is a series of band-aid measures. I think the most obvious is the tax on tobacco. I think it’s right there will be some cut in smoking but to base it as a health initiative is somewhat disingenuous and is clearly just a grab for revenue due to an incompetency in raising revenue in the past.

Richard Denniss, Adjunct Professor, Crawford School at Australian National University

The economy is clearly growing a bit slower than anticipated, and in turn revenue is coming in a lot slower than expected. The obvious consequence of that is budget deficit is bigger than was forecast. The challenge for the government now is to manage good economics and good politics because good economics would suggest that we let the budget sink into a big deficit, we don’t now panic and cut government spending. Because if we reduce government spending at a time when the private sector is reducing spending then we’re just going to make things worse not better.

However with an election as close as it is, the government is clearly under pressure to look fiscally responsible even though what passes as fiscal responsibility is quite economically irresponsible.

Yesterday, the government announced it wouldn’t touch superannuation tax concessions for five years. Yesterday’s announcement shows how quickly things can change. The Gillard government got itself in all sorts of trouble by promising to get the budget into surplus by a
particular time. Today's announcement makes it clear how dangerous it is for a government to make promises about what it will or won't do over a five year period, or over a particular period of time in which the will or won't be able to achieve a particular budget outcome. The economics is quite clear on this, the economy has a much bigger effect on the budget than the budget has on the economy.

Zareh Ghazarian, Lecturer, School of Political and Social Inquiry at Monash University

The economic update presented by the government today brings a few surprises to the electorate. A critical issue is the timing of the update. With intense speculation about when the prime minister will call an election, coupled with the sense that the race between the major parties is now neck and neck, the update arrives at a critical period in the political cycle.

The update needs to achieve a couple of goals. First, it needs to outline the Australian government's budgetary framework. It gives a sense of the state of the economy and the economic parameters in which any future government will be able to operate.

The second goal is for the update to provide a spring-board for the government to launch into the formal election campaign. It is an opportunity for the government to articulate its economic plans and demonstrate how the Labor tradition will influence its future decisions. It will be championed by the government as an alternative to the Coalition's approach which it has warned would replicate European austerity measures.

In a political sense, there are some areas of concern for the government in the update.

The bigger budget deficit of $30 billion will be seized by the opposition and used as “proof” that Labor can not manage the economy. The new charges on bank deposits, tobacco excise and fringe benefits tax will also be vigorously attacked by industry groups.

The update now clears the path for the PM to name an election date, and provides a clearer idea of what Labor would do if it was to win the contest.

Arusha Cooray, Senior Lecturer, Economics at University of Wollongong

Australia has weathered the financial crisis relatively well despite a A$30 million budget deficit as announced by Chris Bowen. Although unemployment is expected to rise before it falls, it is still low compared to that of other OECD nations. Additionally, inflation is low.

Chris Bowen’s statement of plans to bring the budget to a surplus by 2017 is welcome news. However, taxes would have to be increased and expenditures cut in order to do so. Bowen has declared that the government would impose a levy on banks not depositors, but banks will pass this onto depositors which will discourage savings. Savings in turn finance investment, so therefore a fall in savings could reduce investment. Plans to cap deductions for education is good. However, there would have to be cuts in other sectors to offset this.

If cuts are made to welfare and infrastructure, this could slow down growth. In order to achieve the objective of returning the budget to surplus, Australia could attempt to take greater advantage of the opportunities provided by its trading partners, the emerging economies.