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Wayne's deficit chainsaw massacre



Illustration: Eric Lobbecke Source: The Australian

THIS is a tale of deficits, deaths and deceptions. The deficit is that for 2011-12, which we now know was nearly \$44 billion. The deception is the process by which the estimates of that deficit were massaged in the lead-up to the 2010 election. The death is that of budget honesty.

As with all good murders, the perpetrator has an alibi. According to Wayne Swan, the 2011-12 deficit is due to revenue shortfalls, not spending excesses. Unfortunately, that alibi doesn't stand up to scrutiny. But before we get there, some detective work is required.

The forensic evidence is summarised in the graph, which traces the road to the 2011-12 outcome. The bars show how estimates of that 2011-12 deficit changed as the end of the 2011-12 fiscal year came closer and closer. The estimates look like an upside-down version of Everest: they start high (large deficits), then decline (to ever-smaller deficits) and then rise again (back to almost smack bang where they started). So what happened?

What happened is that as the 2010 election approached, Wayne Swan shrank the projected 2011-12 deficit. Nor did he use half-measures: this was the Canberra Chainsaw Massacre, with the estimated deficit being sliced by 80 per cent. But not a single public service job was lost, nor a single centime of wasteful spending retrenched. And little wonder: for this murder was by assumption.

The assumption was that the government would show the expenditure restraint of St Antony while enjoying an increase in projected tax revenues worthy of the second coming.

In the 14 months from the 2009-10 budget to the July 2010 Economic Statement, the estimated taxes that would be collected in 2011-12 increased by nearly \$40bn. To make matters worse, Swan's estimate, which had been met by howls of derision, was largely confirmed in the supposedly neutral Pre-election Economic and Fiscal Outlook, issued by the departments of Treasury and Finance.

Which brings us to a first point. At exactly the same time Treasury was alleging the Coalition's costings were incorrect, it put out a projection of the 2011-12 deficit that has proved to be inaccurate to the tune of \$35bn.

While heaping scorn on the opposition, it managed to simultaneously underestimate the cost of Labor's election promises and overestimate the revenue needed to fund them. Talk about attention deficit disorder.

But there's a second point as well. And this one goes directly to Swan's "the dog ate my taxes" alibi. Contrary to all the hype, actual revenues in 2011-12 were not lower than those originally projected in the 2009-10 budget:

thanks, in part, to larger than expected company tax collections, they were some \$20bn higher. But spending also increased by around the same amount. It was this rise in outlays that mainly accounts for the large size of the 2011-12 black hole.

Nor was the spending blow-out due to factors beyond the government's control. Rather, fully two-thirds of it was the result of policy decisions - ie, decisions to increase spending on existing programs or launch new programs.

Let's put that spending in perspective. Swan committed the government to increase outlays by no more than 2 per cent a year in real terms until the budget returned to surplus. Had he stuck to that commitment since 2008-09, spending would be \$46bn lower than it is today, wiping out the shortfall.

No surprise then that the deficits this government has accumulated in five years are now barely 1 per cent less, in inflation adjusted terms, than the sum of all deficits incurred in the 37 years from 1970 to 2007. Moreover, that Olympic record was achieved despite an economy that, thanks to the resource boom, was expanding at or even above its trend rate of growth, while the period from the 1970s to the mid-90s was marked by prolonged bouts of stagnation.

As for fiscal consolidation, Swan claims Australia "leads the world" in the return to budgetary virtue. And so we should. But the reality is that data from the International Monetary Fund ranks Australia 19th among the advanced economies in the fiscal consolidation stakes, measured in terms of the speed at which structural deficits are being closed. The IMF estimates that to restore structural budget balance by 2020, Australia must close a gap between spending and taxing of some 4 per cent of GDP.

Swan claims that gap is being closed by "savings" measures, with the government asserting that since 2008-09, it has undertaken "savings" of some \$135bn. In fact, those claimed savings are at best the deferral or cancellation of even greater spending that had been programmed. Largely, however, they are not even that.

This can be seen by examining the 23 major "savings" initiatives that account for \$25bn of the claimed \$32.6bn total for 2012-13. Of that \$25bn, fully \$15bn are not reductions in outlays. Rather, they are tax slugs, involving tax penalties (as with private health insurance rebates) or reduced tax concessions (for example, for superannuation), misleadingly labelled as spending reductions.

And more tax hikes are in the air. For like the alcoholic who, having drunk his pay, cuts back on the groceries, Labor has shown no willingness or ability to tackle the root causes of our fiscal problems. Those problems cannot be addressed without real efficiency improvements in the core areas of government spending, including health, education and welfare.

That is the challenge for the opposition. For however abysmal Labor's record is, the opposition needs to show it will do better.

This is not to suggest an opposition can undertake the careful planning required to redress six years of maladministration. In our system of government, which does not provide the transparency needed for detailed budget analysis, such a requirement would be absurd.

And of course, Labor came nowhere near fully costing its policies in 2007, while the 2010 experience casts enormous doubt on the value of Treasury's costings of electoral commitments.

But what the opposition can and should do is outline a comprehensive fiscal strategy. And it must set that strategy within the confines of credible fiscal rules and of renewed mechanisms to ensure budget honesty. Until it does, Swan's way will prevail. And we now know where that leads.
