

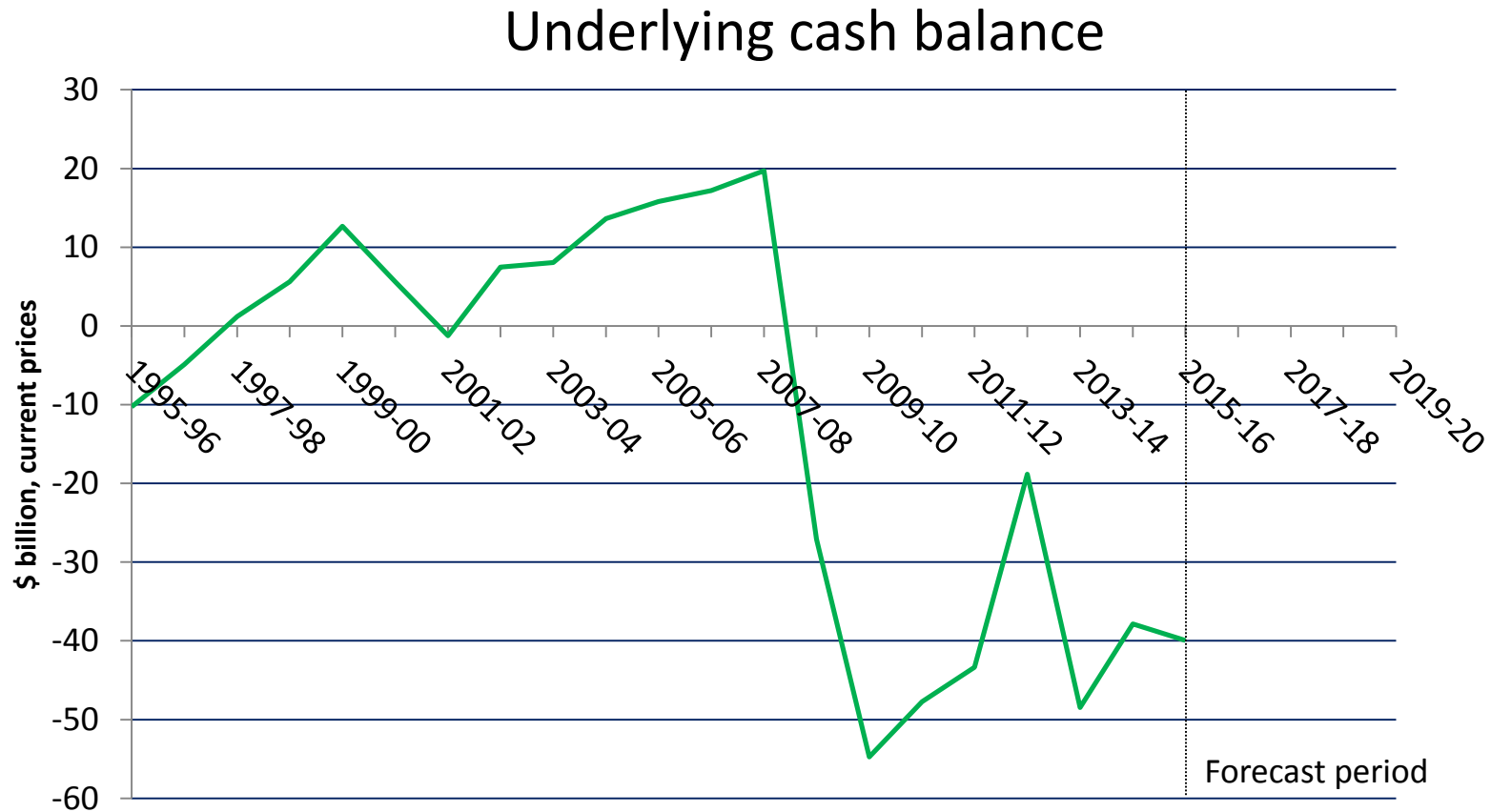
Aid Budget 2016-17

The macroeconomic context

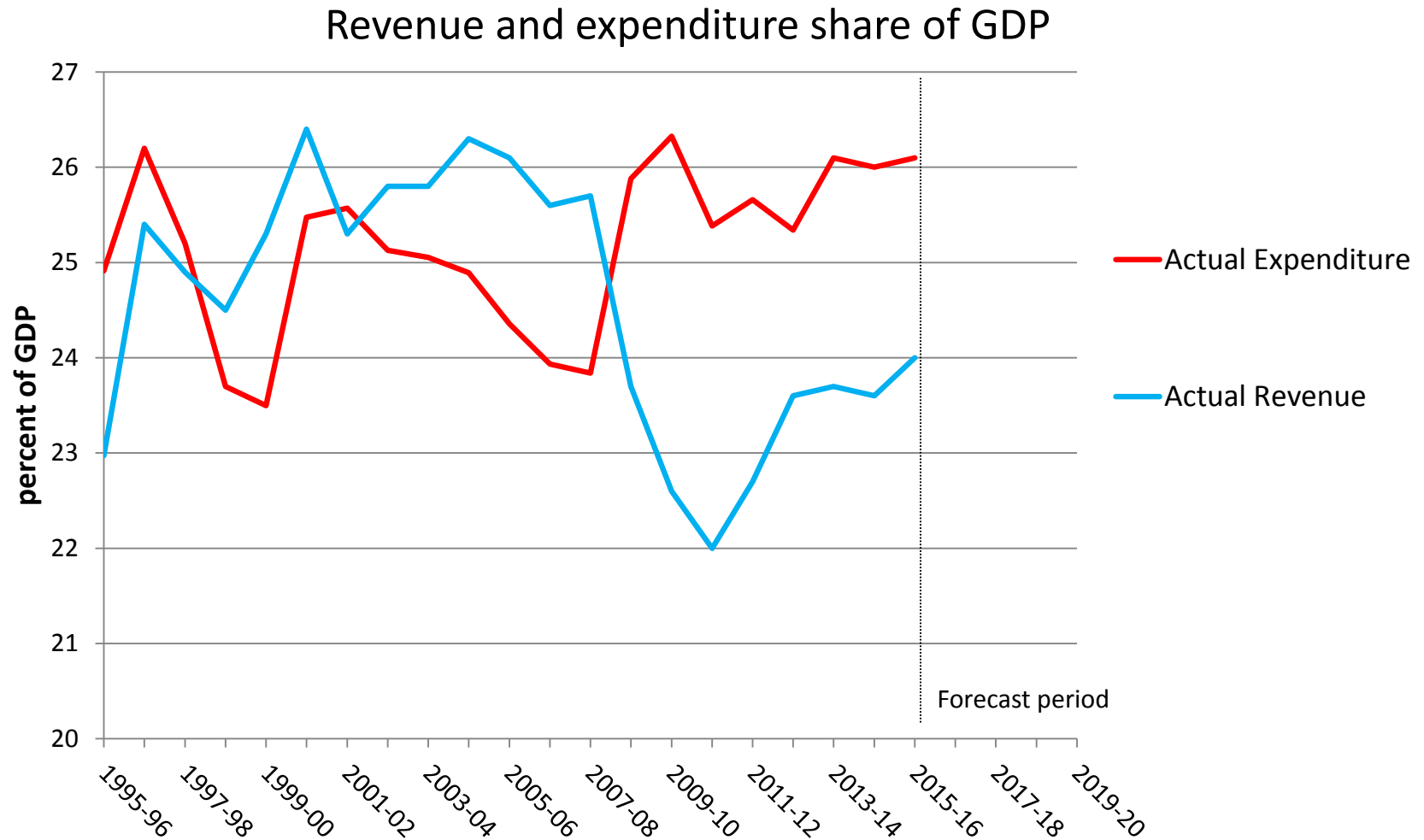
Anthony Swan

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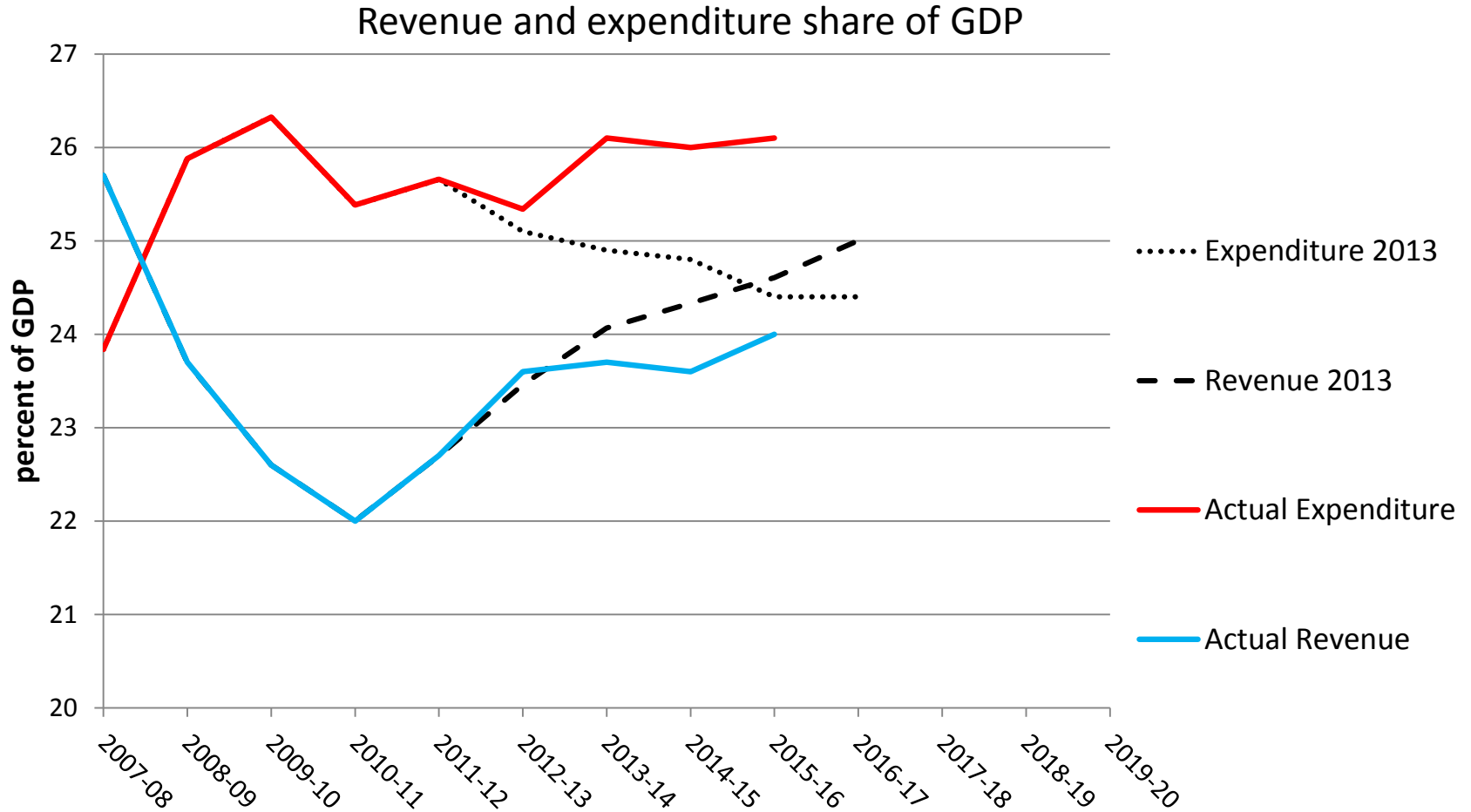
Despite the “budget emergency” the budget deficit problem is still with us. Why is this?



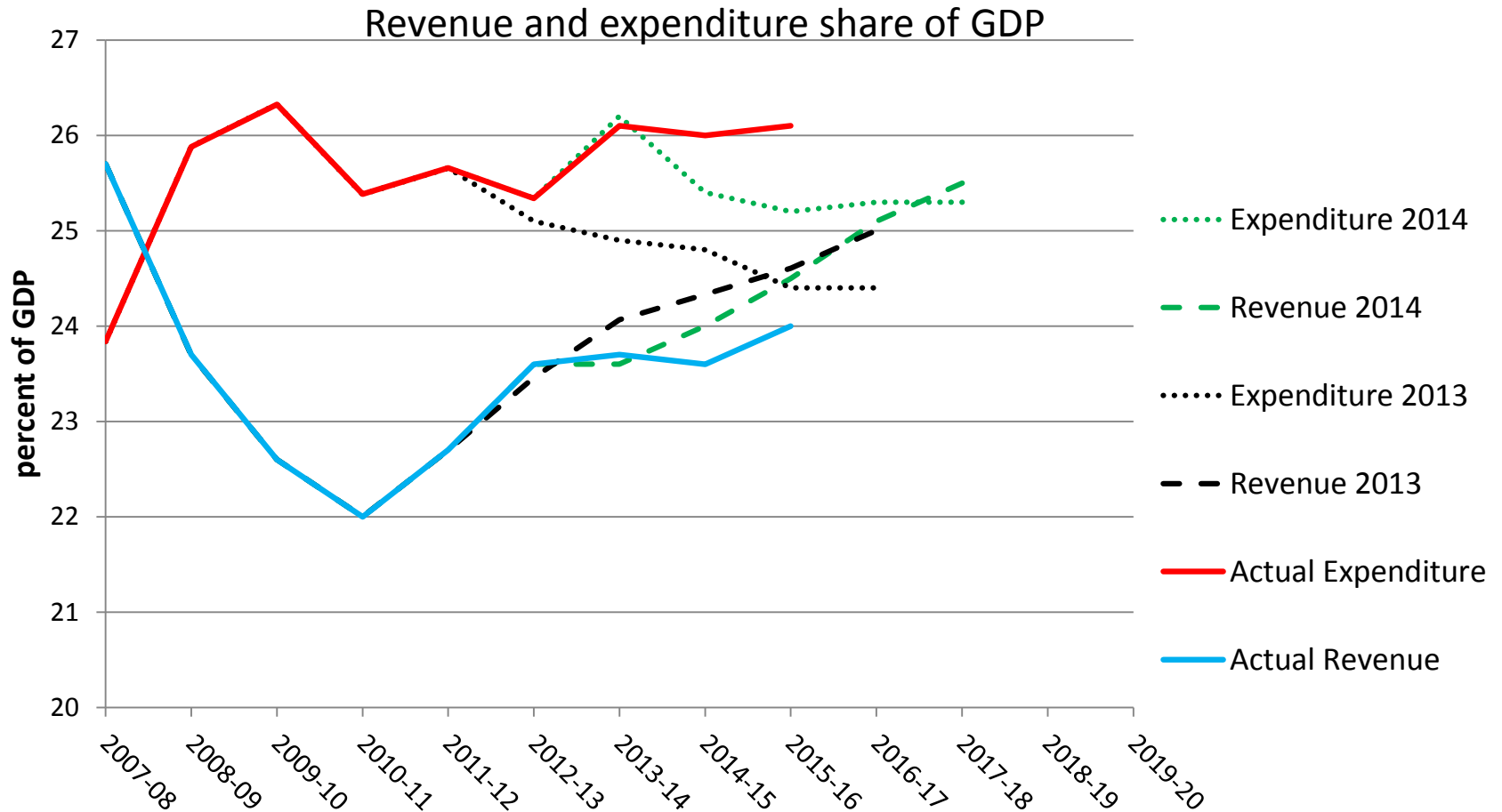
It reflects a persistent gap between expenditure and revenue. But what efforts have been made to close the gap?



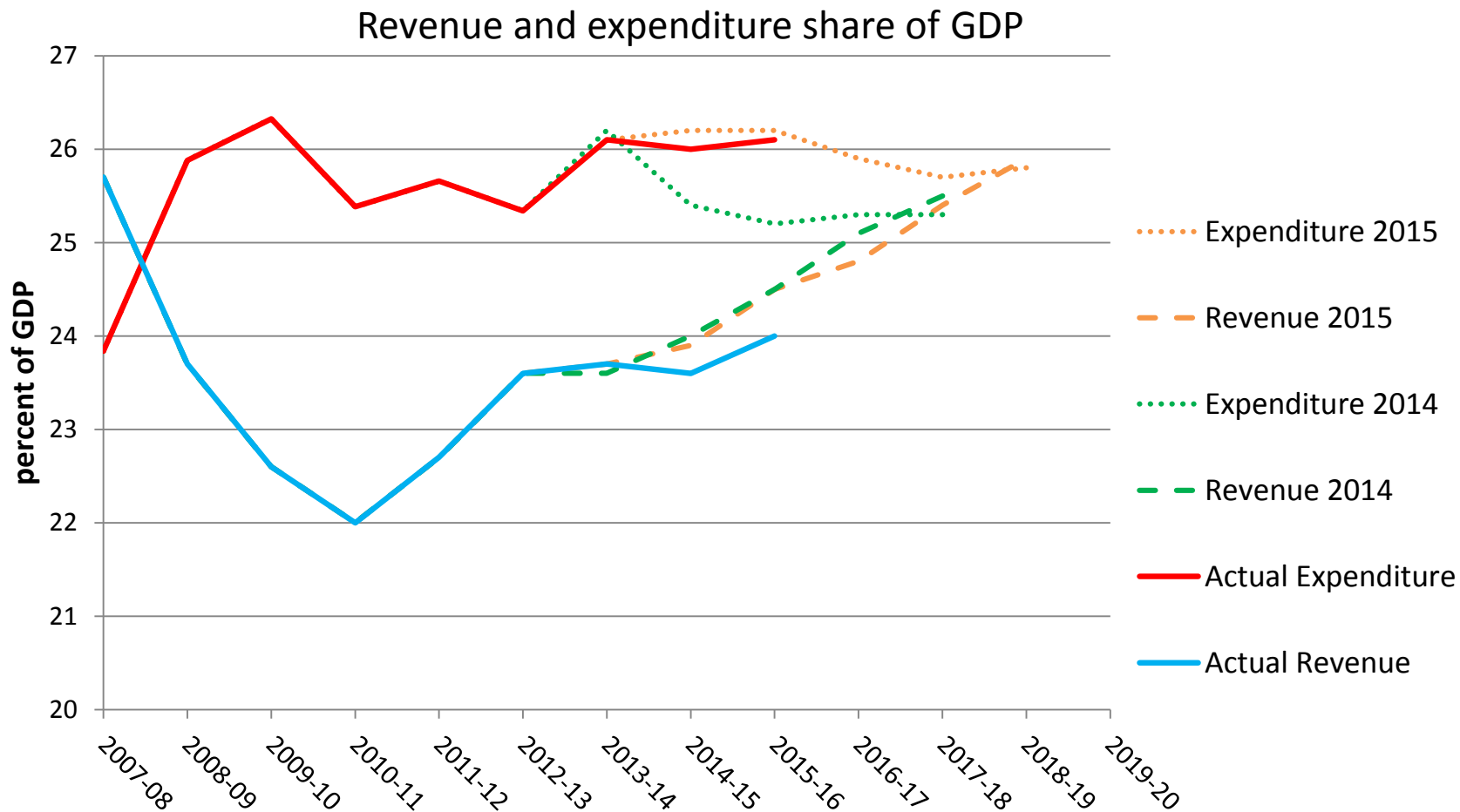
The last Labor government budget projected strong revenue raising effort and large cuts to spending. Both failed.



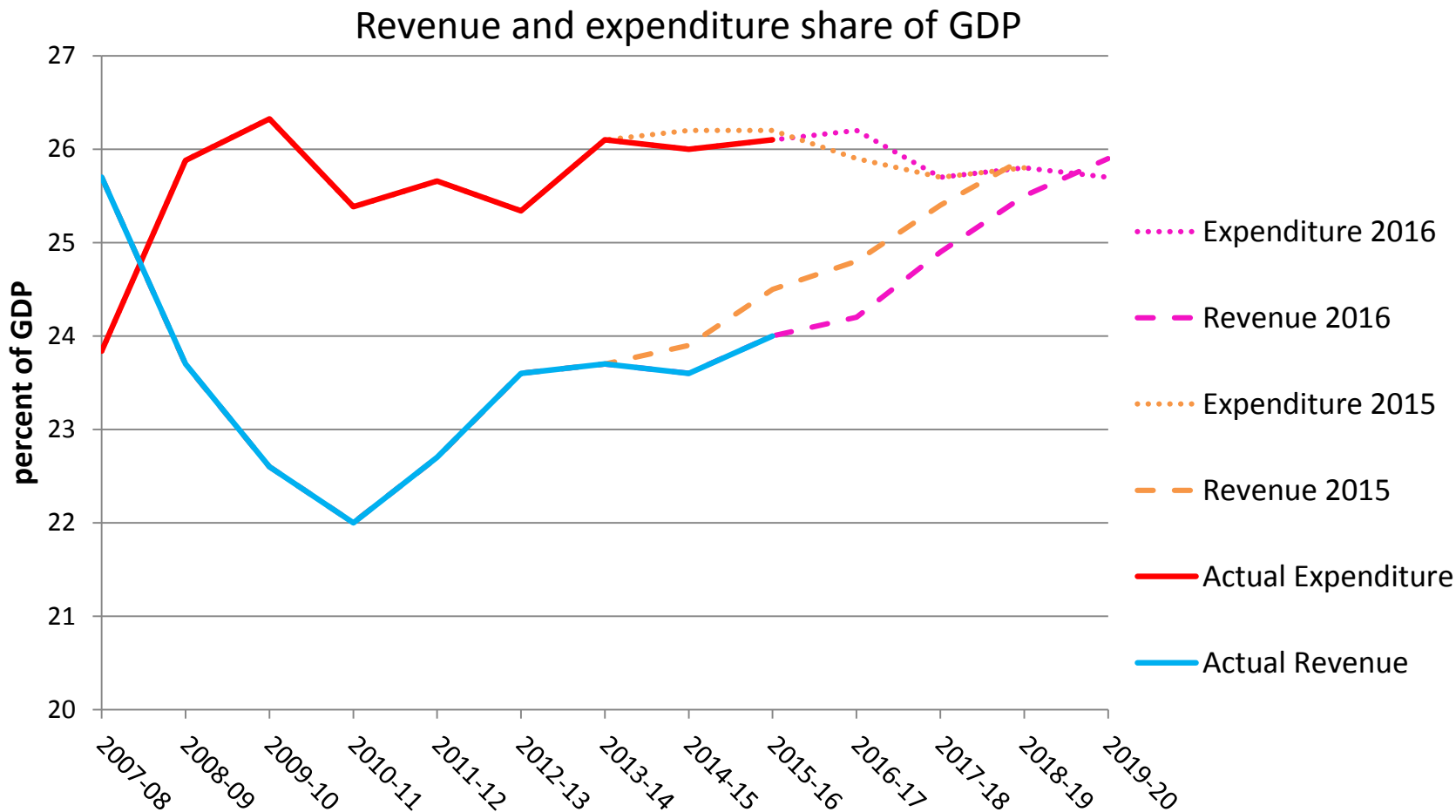
Under Abbott's 2014 budget, spending initially spiked but was later expected to fall. It didn't. Strong revenue raising measures were also expected but never eventuated.



Under Abbott's 2015 budget, there was little effort to reduce spending. Increased revenue was expected to bring the budget towards balance but there is little evidence of this.

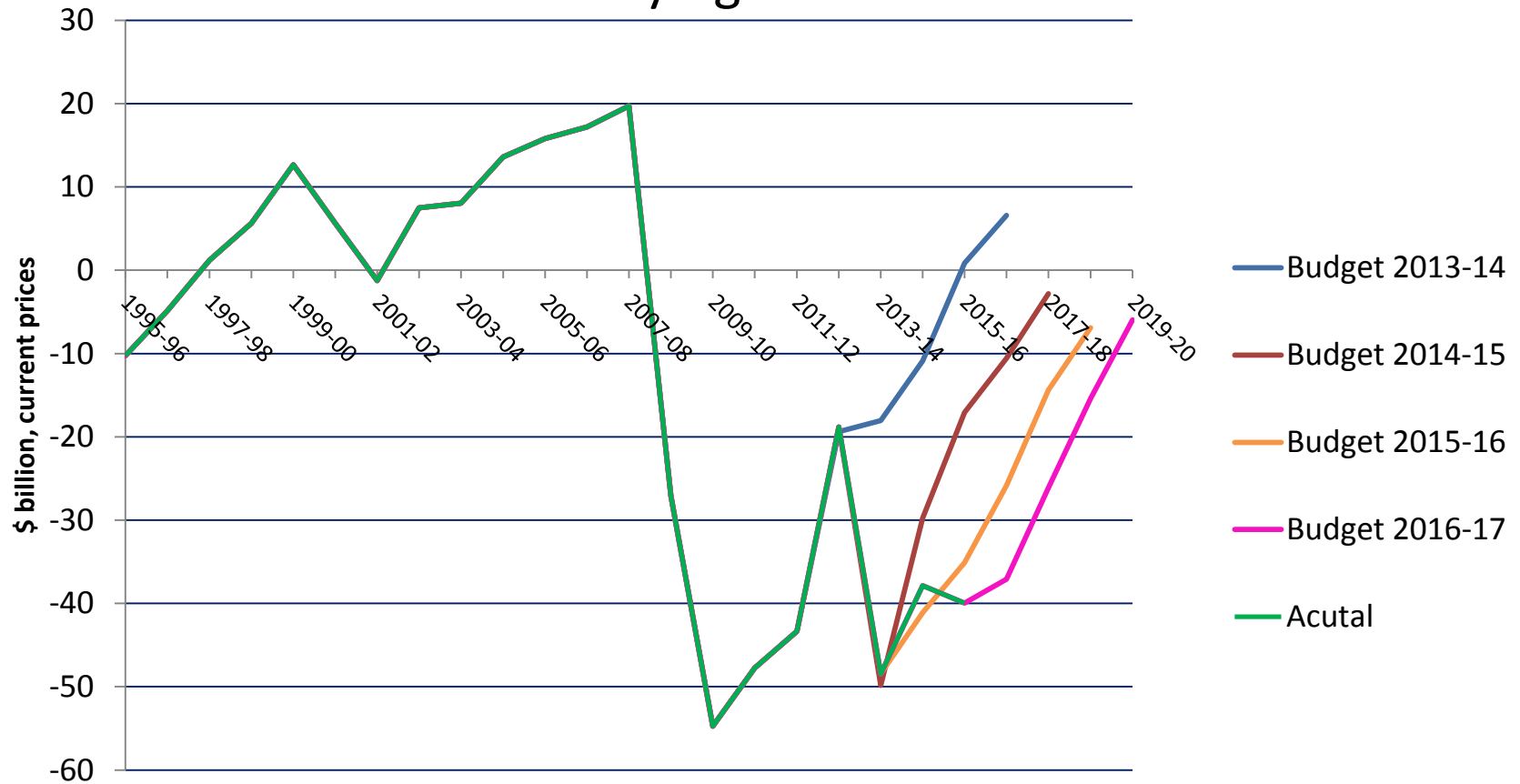


In this year's budget spending remains high and once again revenue raising effort is expected to bring us to budget balance.



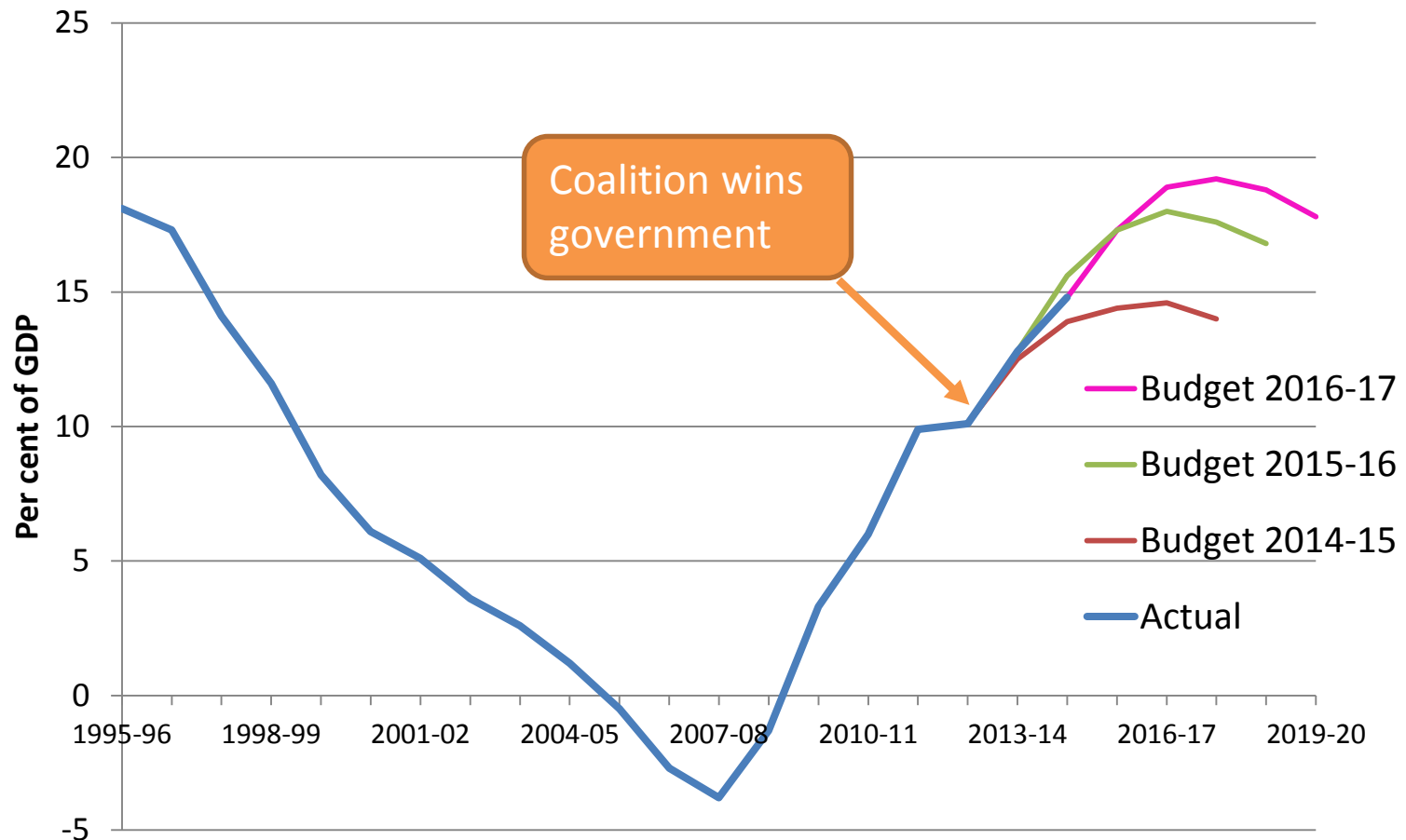
Are we to believe the latest budget projections?

Underlying cash balance



Continuing budget deficits mean that the government debt problem is exacerbated.

Government net debt share of GDP



The key to a growing real aid budget is a healthy government fiscal position. Why isn't this being achieved?

1. Few actual revenue raising measures being implemented
 - Thought bubbles on tax reform but not much more.
 - New tax initiatives are offset by tax cuts elsewhere (e.g. superannuation concessions, income tax cut to relatively wealthy, company tax cuts)
 - Over-reliance on relatively small tax changes (e.g. tobacco excise) rather than deep reform

The key to a growing real aid budget is a healthy government fiscal position. Why isn't this being achieved?

2. Low tax revenue due to slow wages growth

- Labour productivity not increasing fast enough
- A low inflationary (and now deflationary) environment means that tax payers are not being pushed into higher tax brackets and paying more tax.
 - Instead the government is reducing the tax benefit of bracket creep through tax cuts (albeit small)
- A lower than expected working age population (by 150,000 people by 2019) as a result of reduced net migration. This is a policy decision by government.

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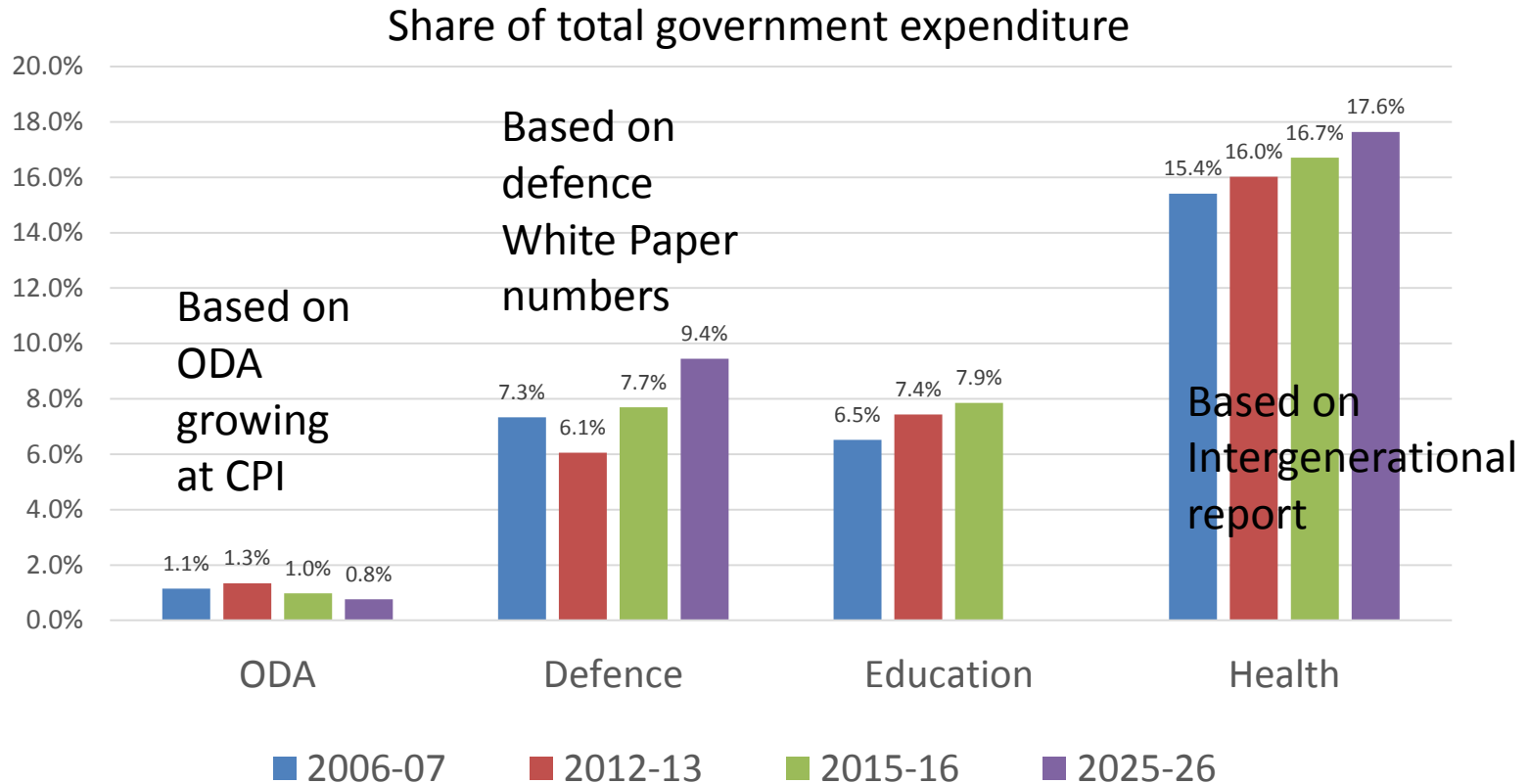
3. Lack of control on spending

- Cuts to spending offset by new spending initiatives
- Failure to negotiate changes in the Senate
- A high interest burden from increased government debt
- Poor revenue forecasting is likely to give rise to overspending

4. Continued expectation that the economy will pick up by itself.

- But current stagnant growth may be the new normal!

The squeeze on the aid budget is set to worsen as further spending pressures build, particularly in defence and health sectors



From an aid budget perspective it's important for the government to strengthen its fiscal position before this squeeze occurs.

Thank you