



# **Balancing budgets: tough choices we need**

**John Daley, CEO, Grattan Institute  
2014 Economic and Social Outlook Conference  
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## Overview

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### **Australian government budgets are in trouble**

- For 7 years a structural deficit was masked by mining boom and GFC
- The Commonwealth has *both* a revenue and a spending problem
- Revenues are returning to long-run averages with bracket creep
- Health and infrastructure increased their share of government spending

### **Bracket creep is ‘solving’ the short-term structural problem**

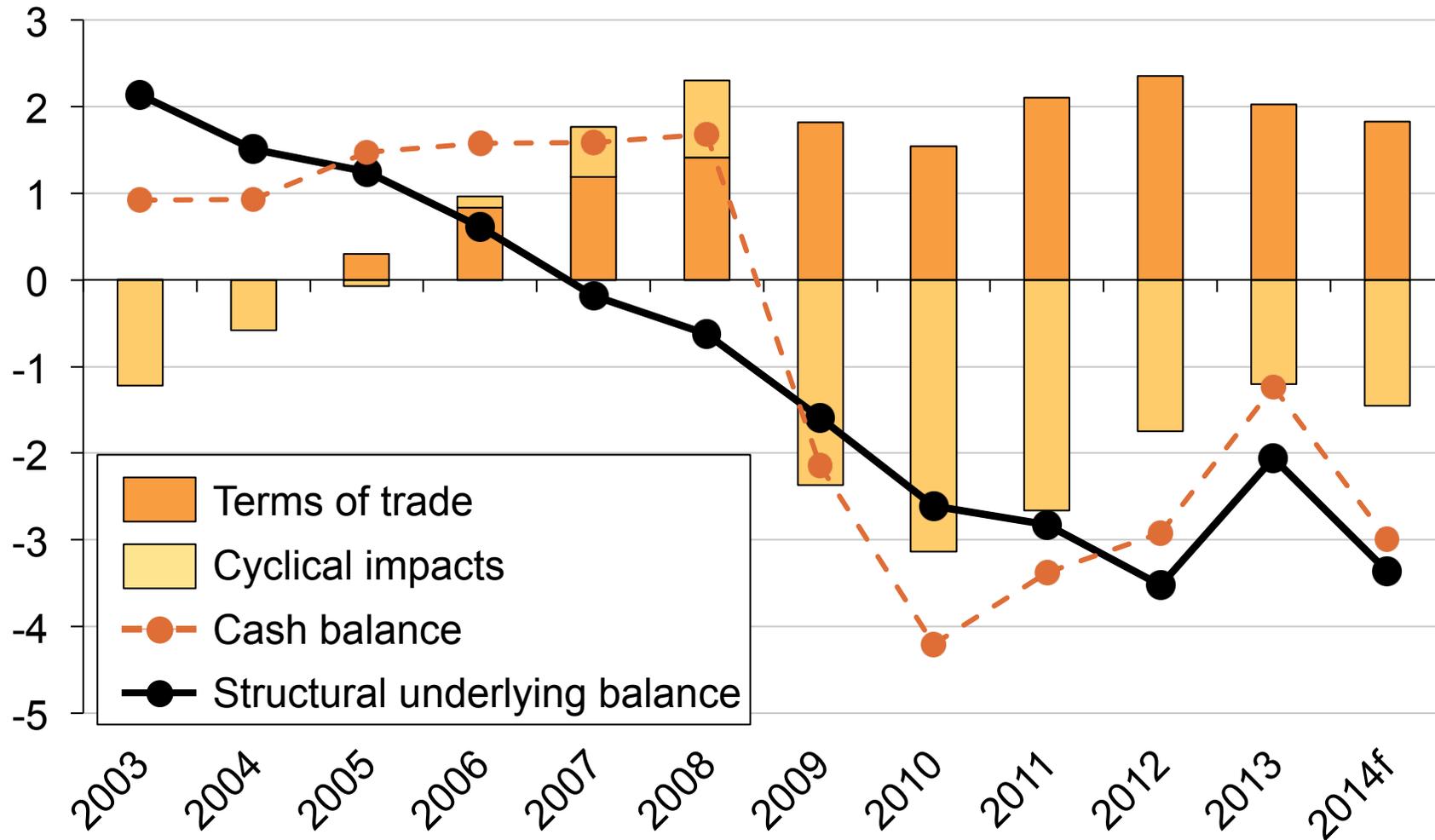
- Highly publicised budget cuts affect a wide variety of groups
- However, most of the structural improvement is a result of bracket creep
- Bracket creep hits middle income earners most, and is unlikely to be politically sustainable

### **Longer term structural budget problems require tougher choices**

- Longer term budget settings are not sustainable given signature policies, rising health costs and other pressures
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- Some structural improvements are in place, but more will be needed

# The Commonwealth's structural deficits was masked by mining boom and GFC

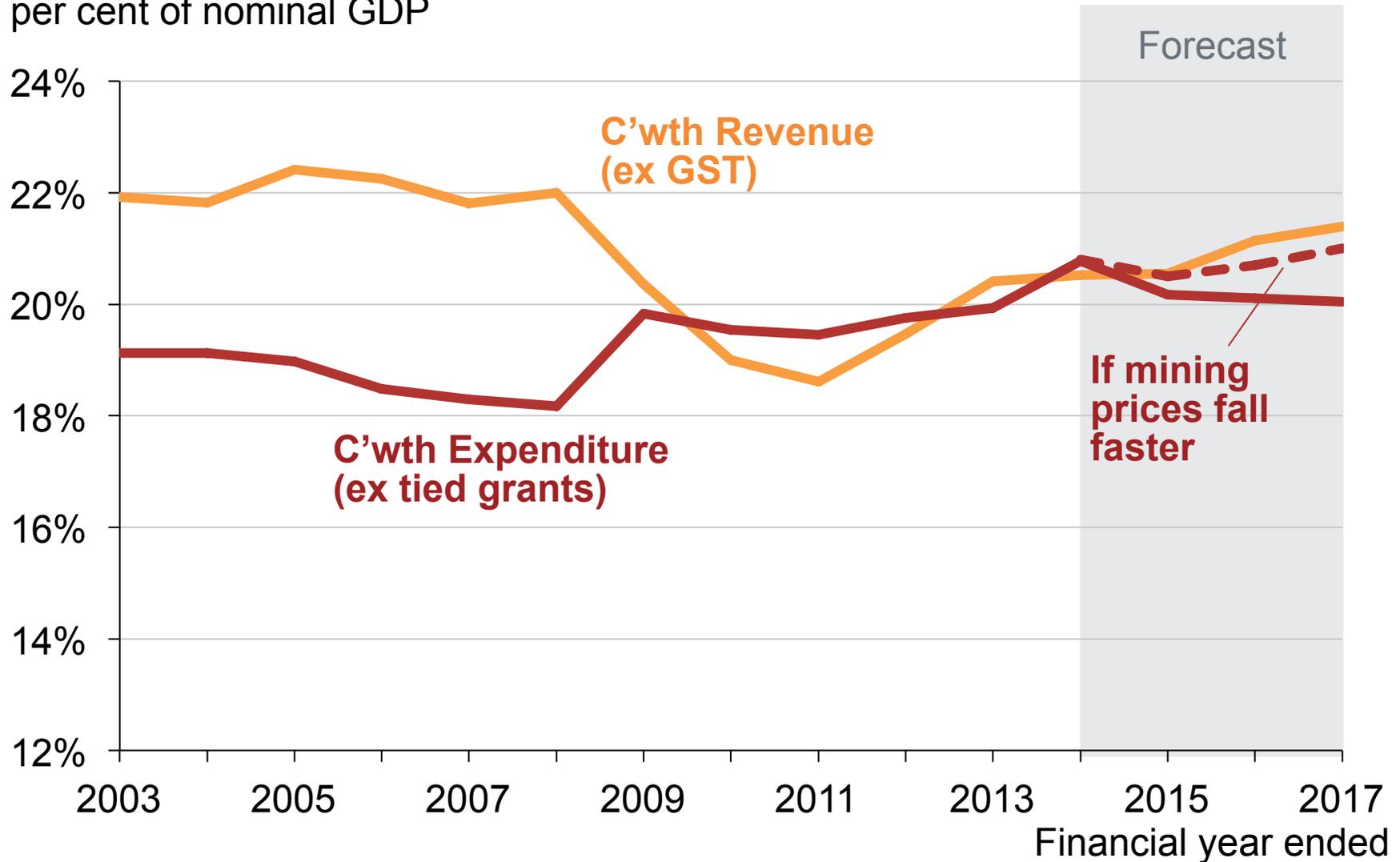
## Commonwealth budget balance per cent of nominal GDP



Note: Cash balance is equal to receipts minus payments, minus Future Fund income, (under 0.25 per cent of GDP)  
Source: *Budget Pressures 2014*

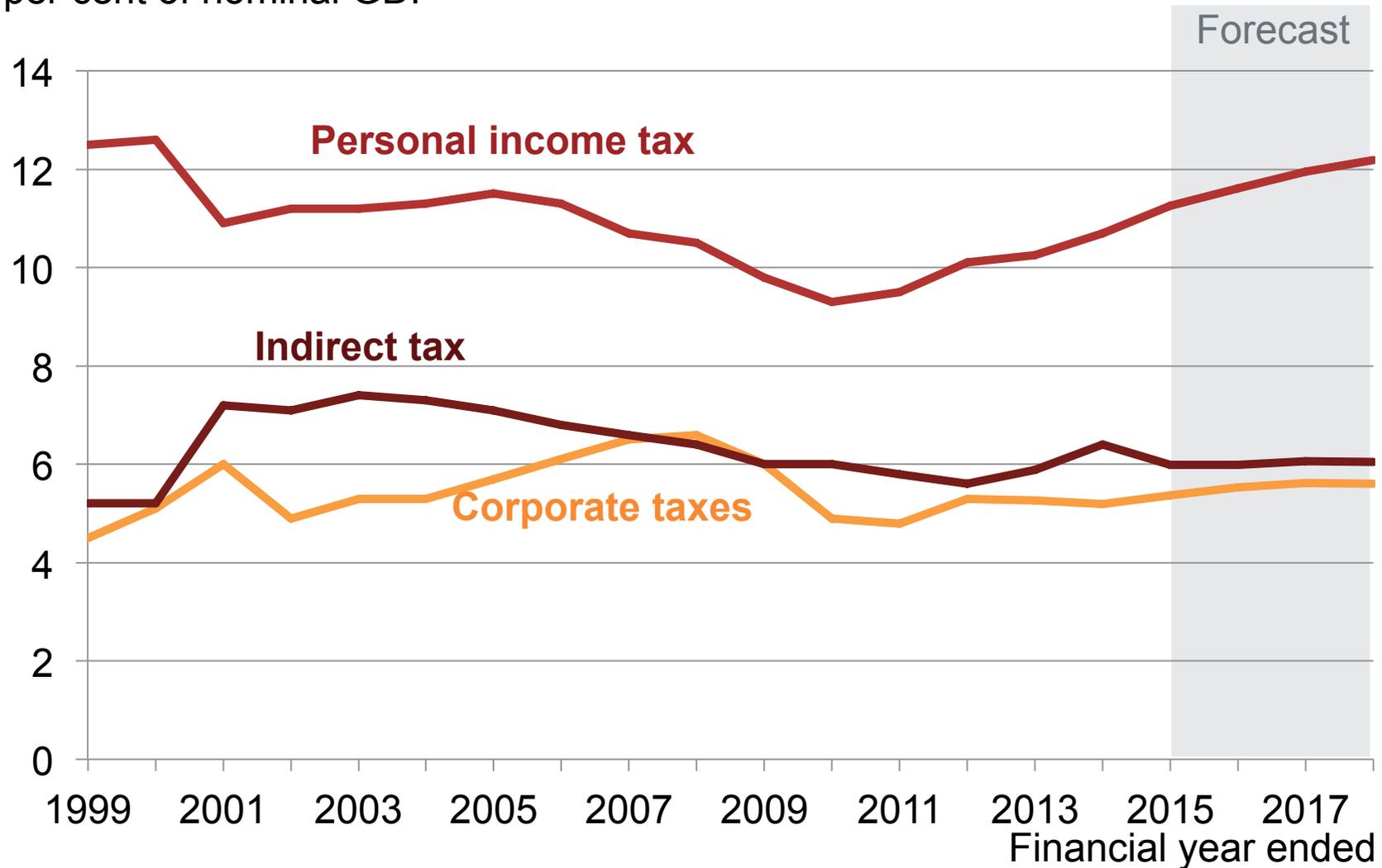
# Both revenue and expenditure are worse than longer-run levels

Commonwealth own purpose expenditures and revenues per cent of nominal GDP



# Commonwealth tax receipts are returning to historic levels

## Commonwealth taxes per cent of nominal GDP

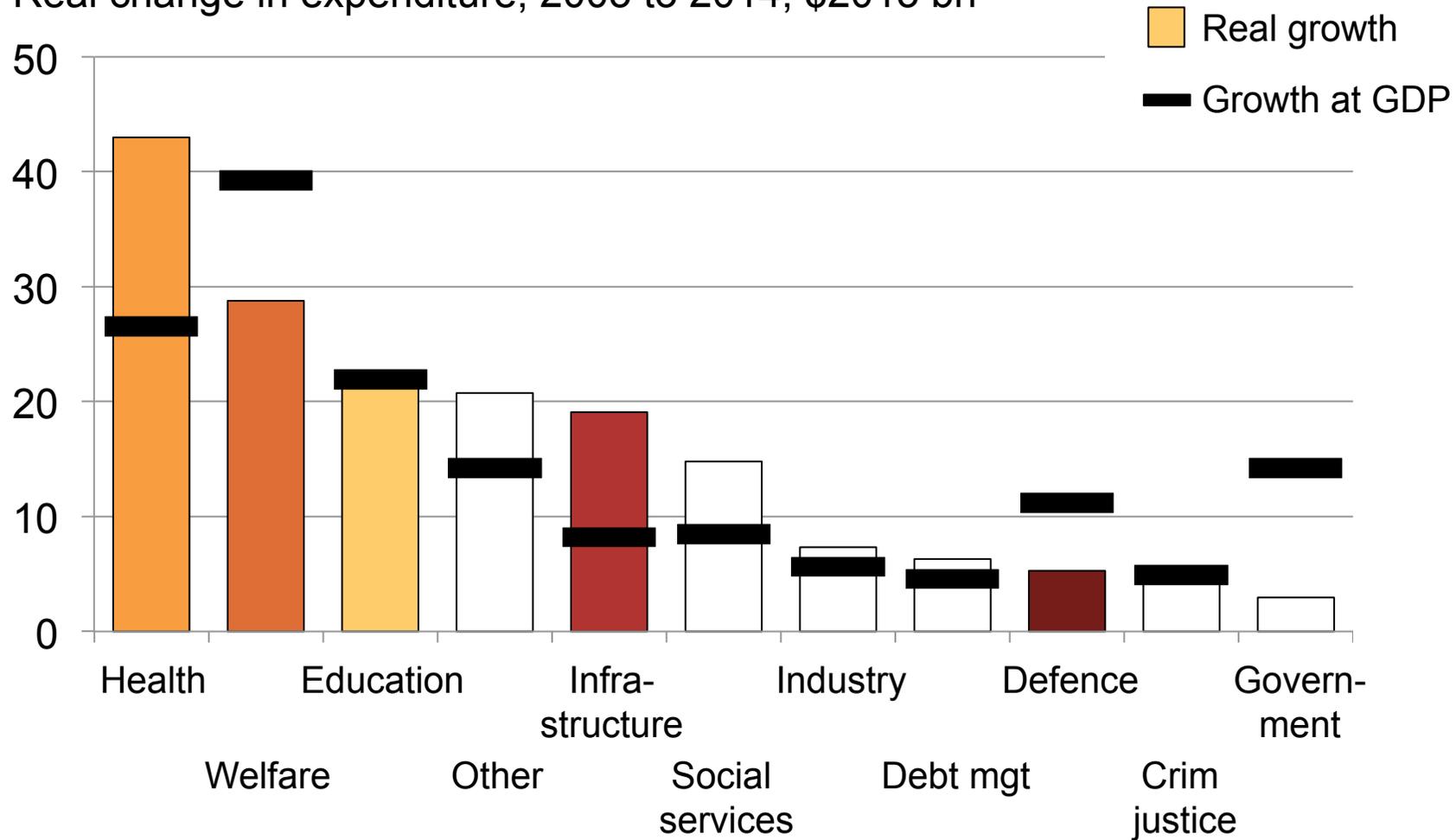


Source: Treasury, *Budget Paper 1*; Grattan Institute analysis

# Health and infrastructure increased their share of government spending

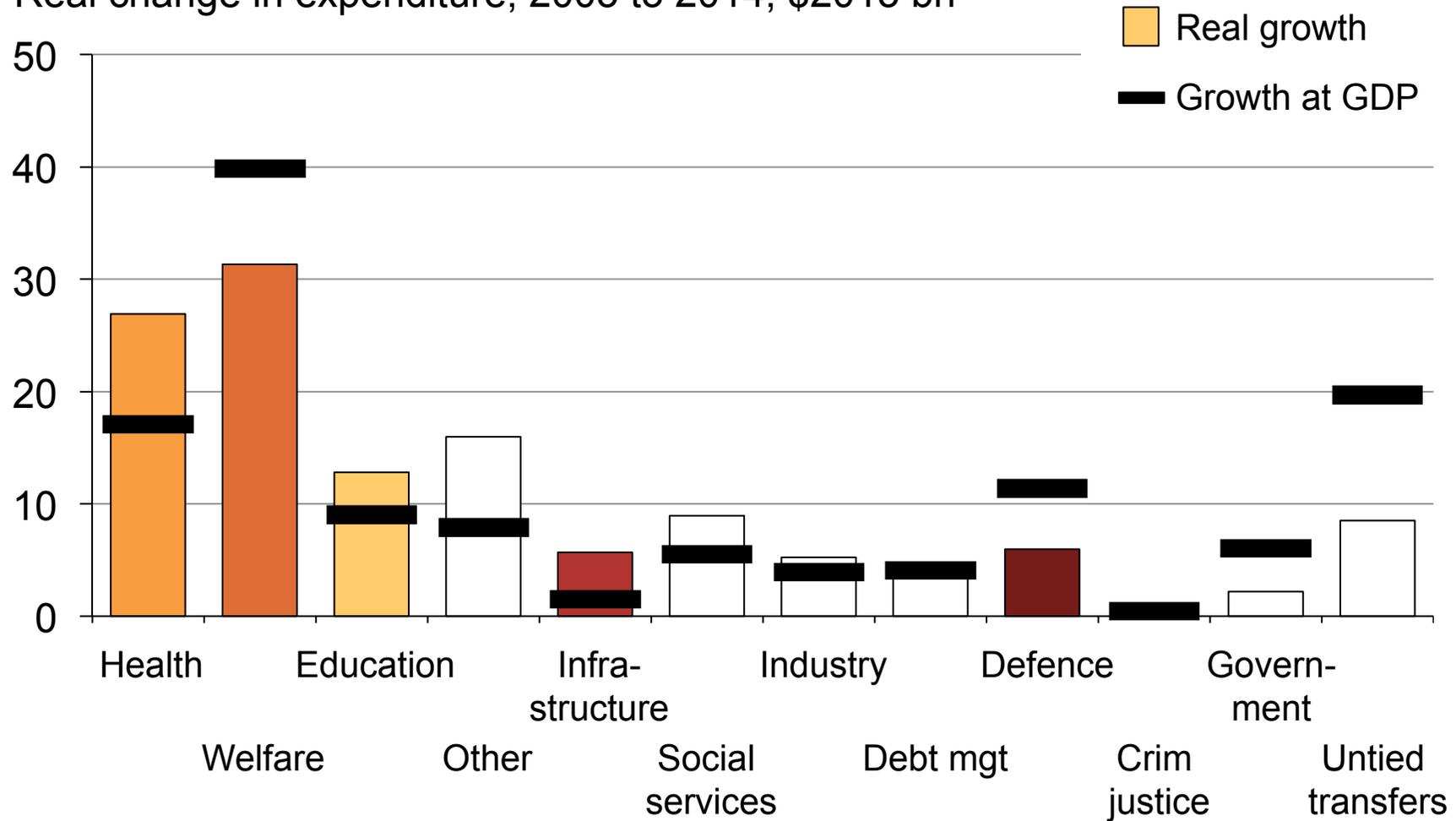
## Change in Australian governments' expenditure 2003-2014

Real change in expenditure, 2003 to 2014, \$2013 bn



# Health increased and welfare reduced their share of Commonwealth spending

**Change in Commonwealth recurrent expenditure**  
Real change in expenditure, 2003 to 2014, \$2013 bn

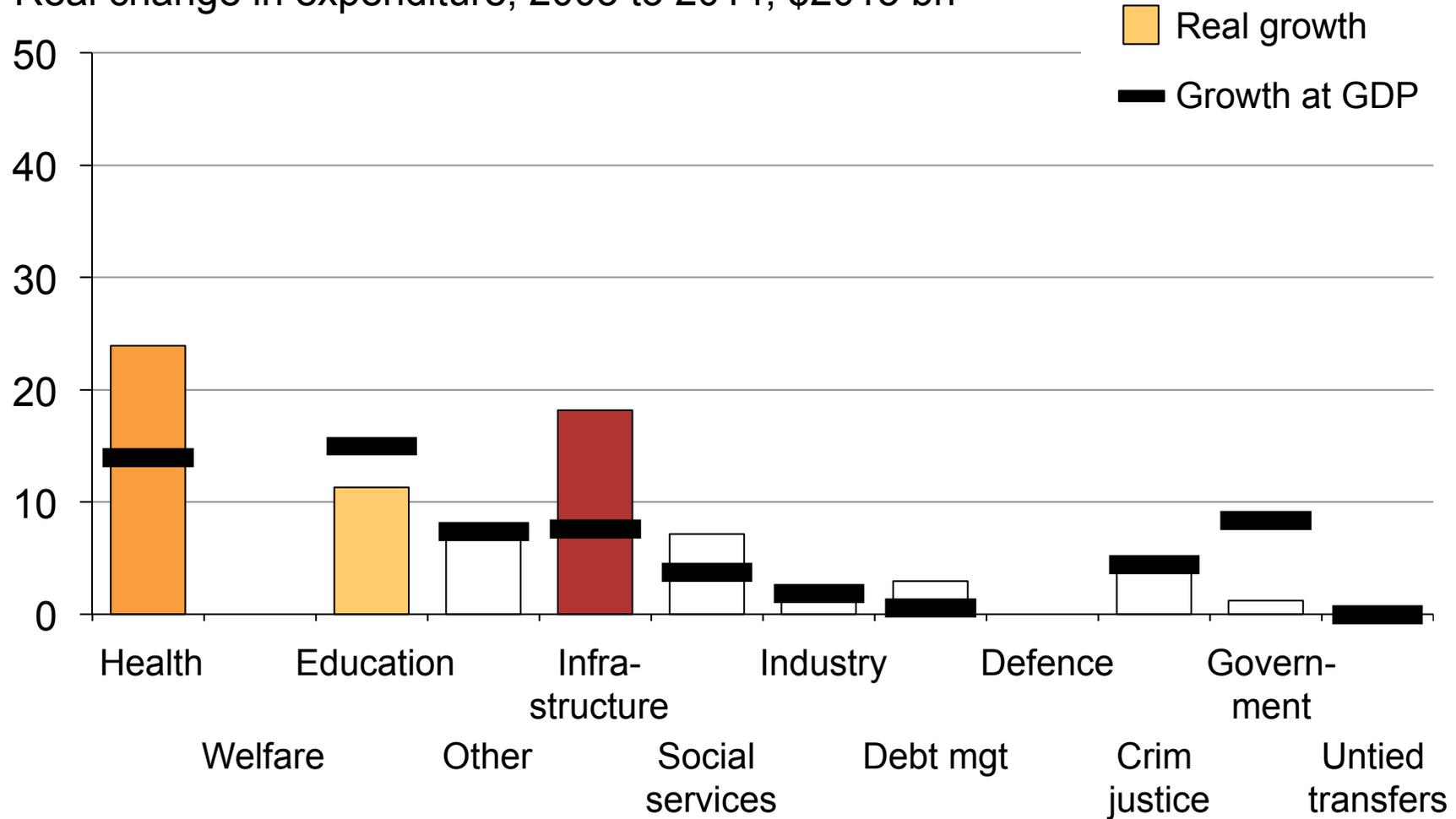


Note: Includes funds transferred to States. 'Other' comprises all expenditure not elsewhere included. 'Social services' comprises ageing and aged care services, disability services, and community services. 'Govt & econ' comprises government operations and economy and finance.  
Source: *Budget Pressures 2014, Supporting Materials*

# Health and infrastructure drove increases in State spending

## Change in State recurrent expenditure

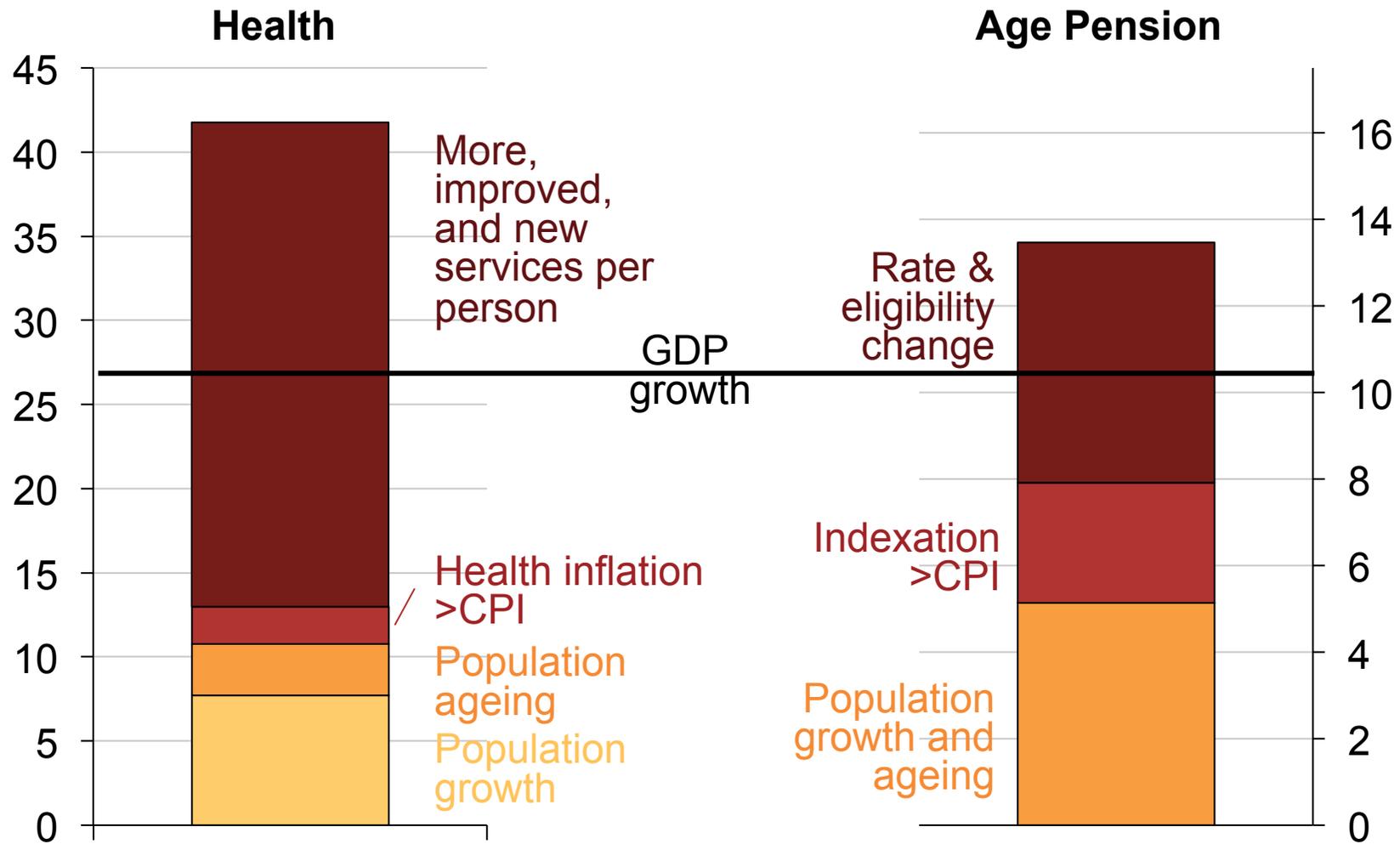
Real change in expenditure, 2003 to 2014, \$2013 bn



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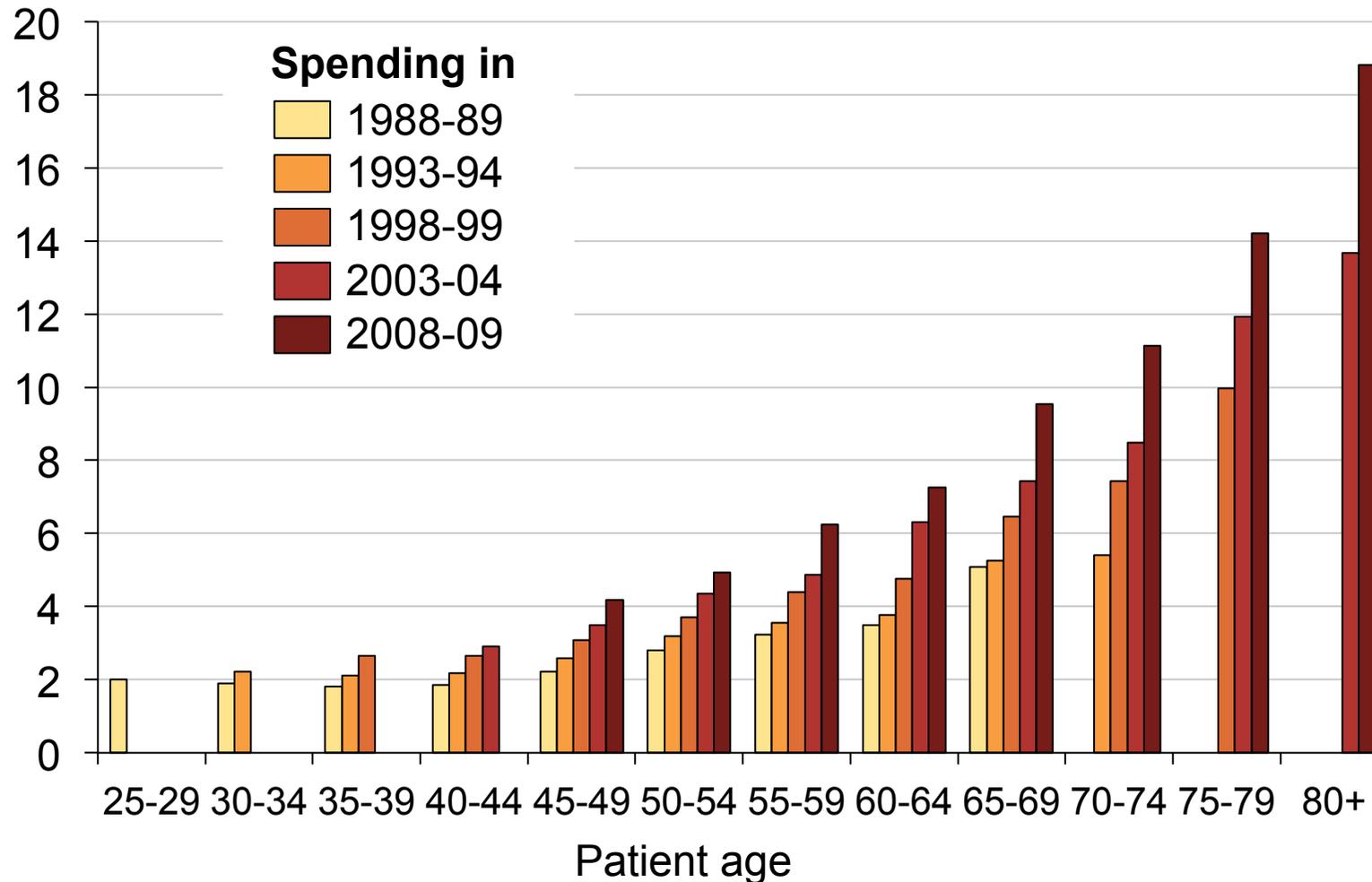
# Health and Age Pensions spending were due to policy choices, not population ageing

Real increase in expenditure 2003-2013  
\$2012 bn



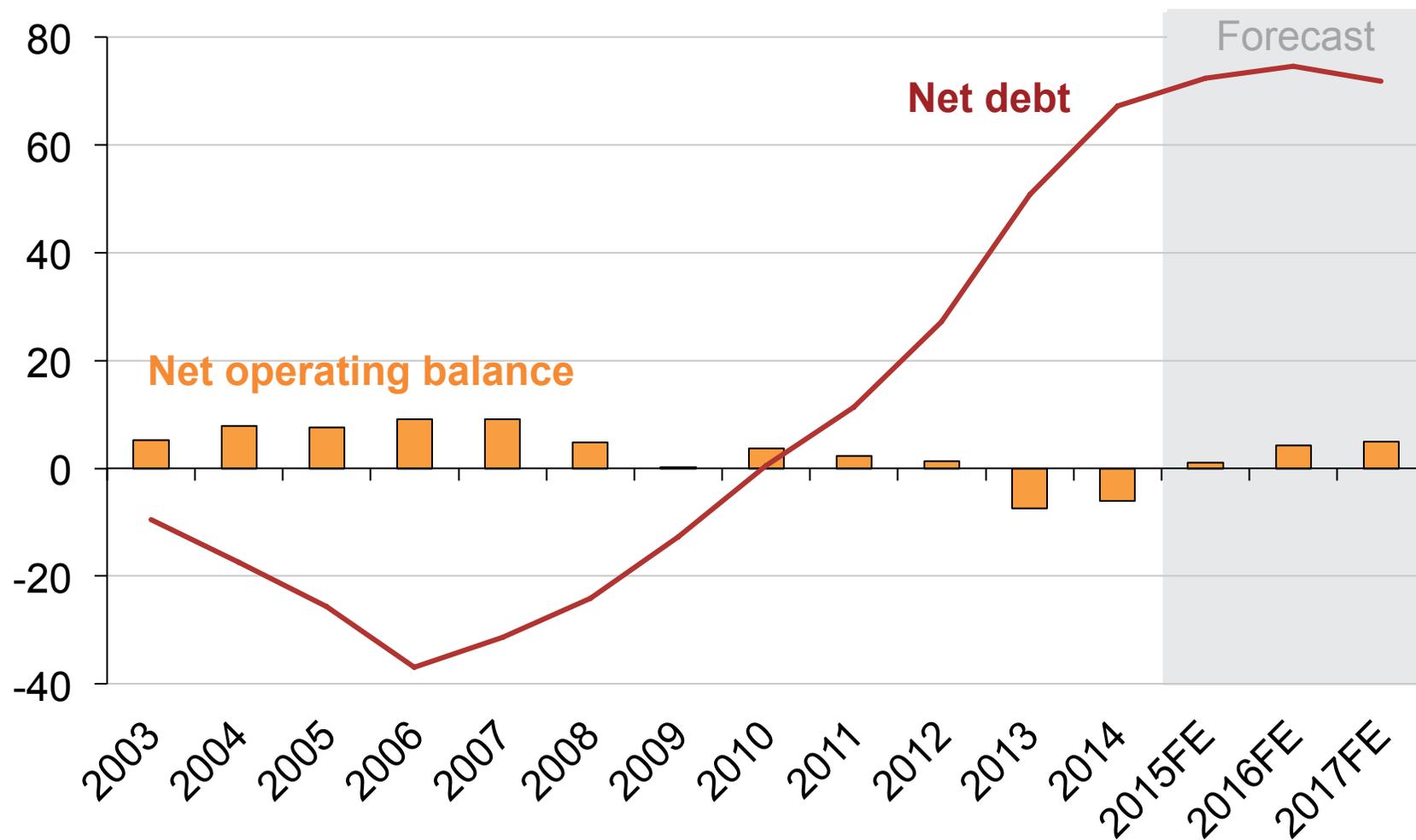
# Spending on health has risen for all ages, but is much greater for older age groups

**Government spending on health per person**  
All governments, \$2012 '000 per year per person



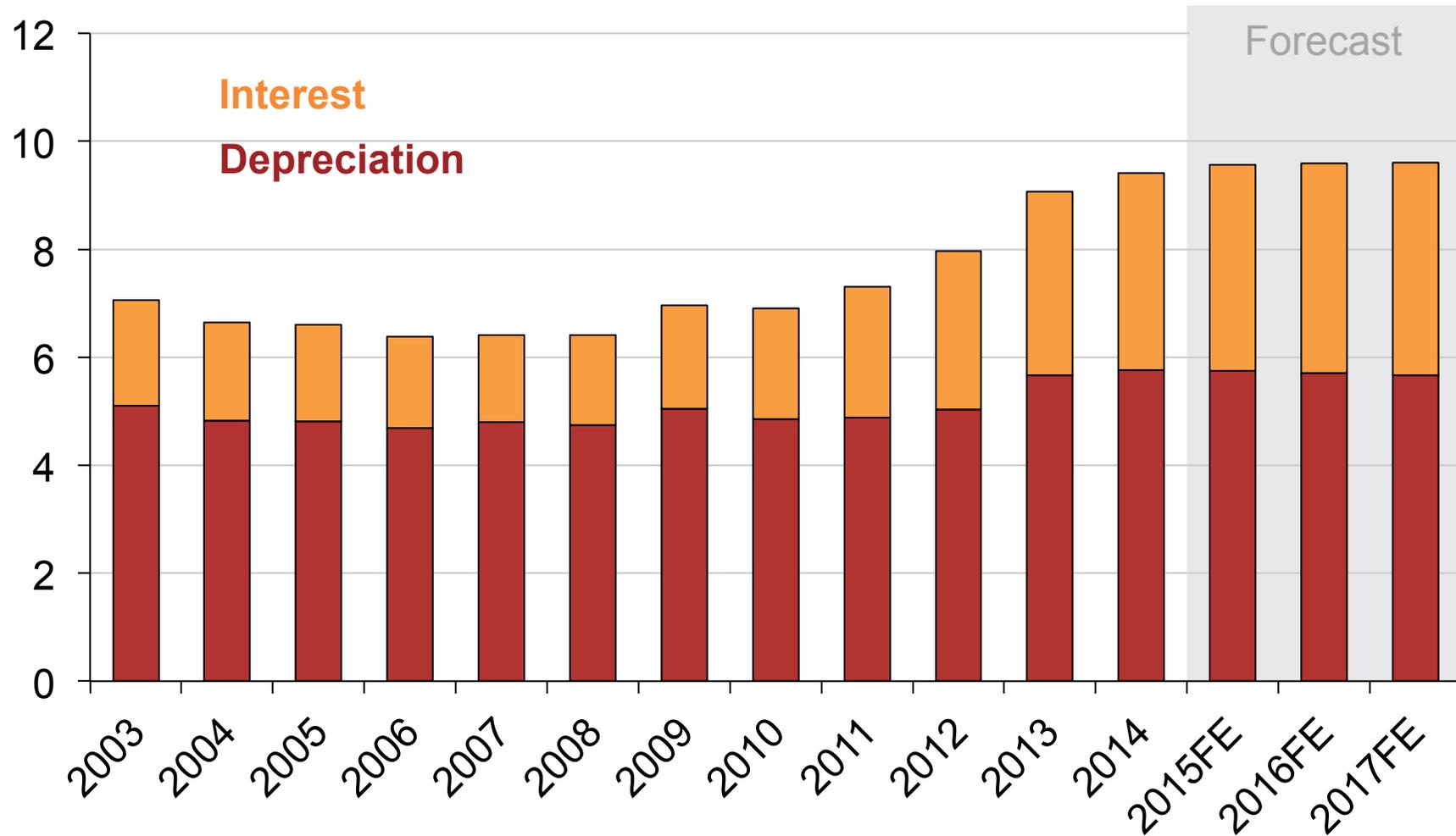
# Capex has driven increase in State debt

State net debt and operating balance  
\$2013 bn



# Recurrent State budgets are now paying for past capex

Depreciation and interest expense as a percentage of State revenue  
% of revenue



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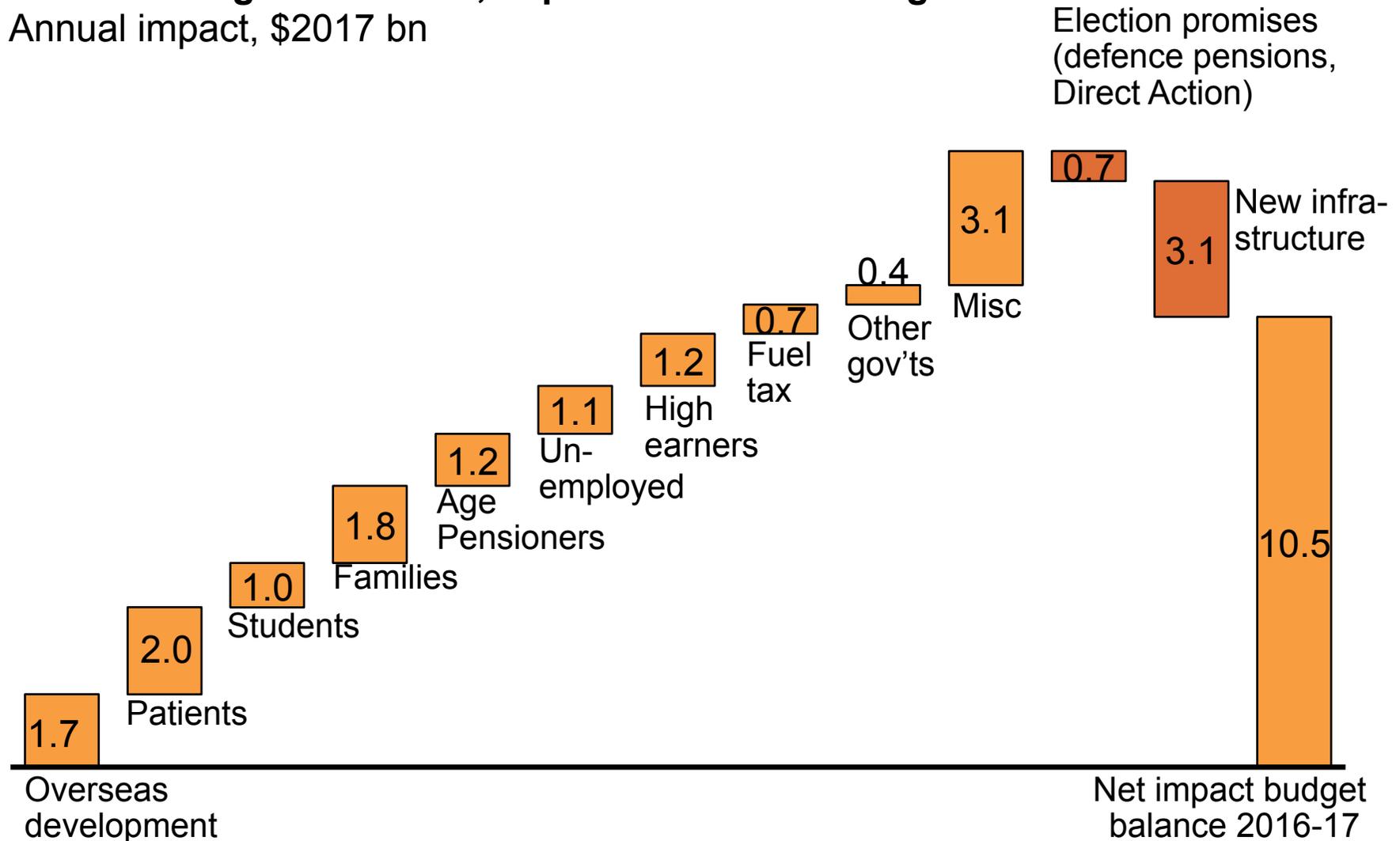
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# Budget cuts affect a wide variety of groups

## 2014-15 Budget measures, impact on 2016-17 budget

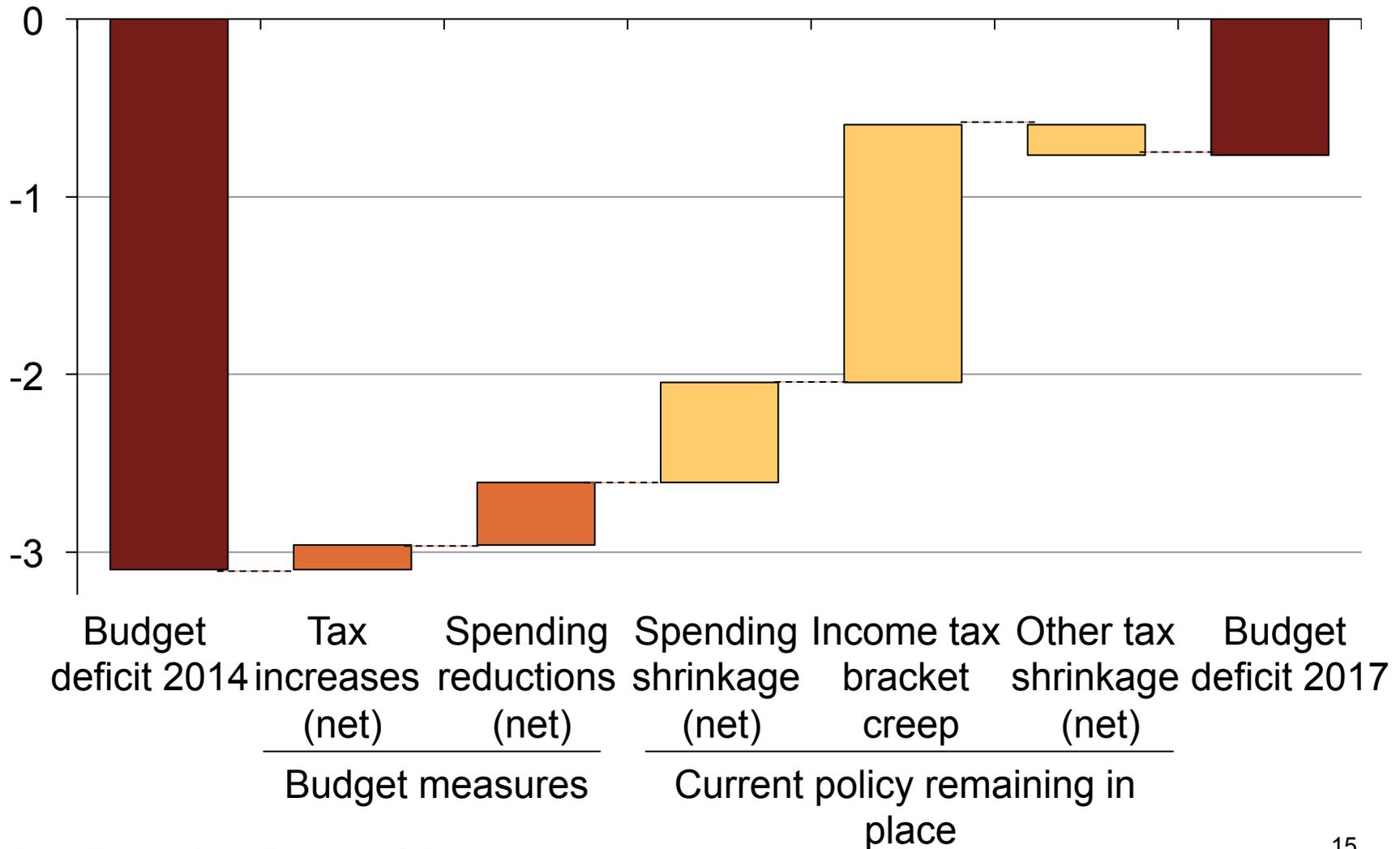
Annual impact, \$2017 bn



# Most of the structural improvement is the result of bracket creep

## Budget balance as a percentage of GDP

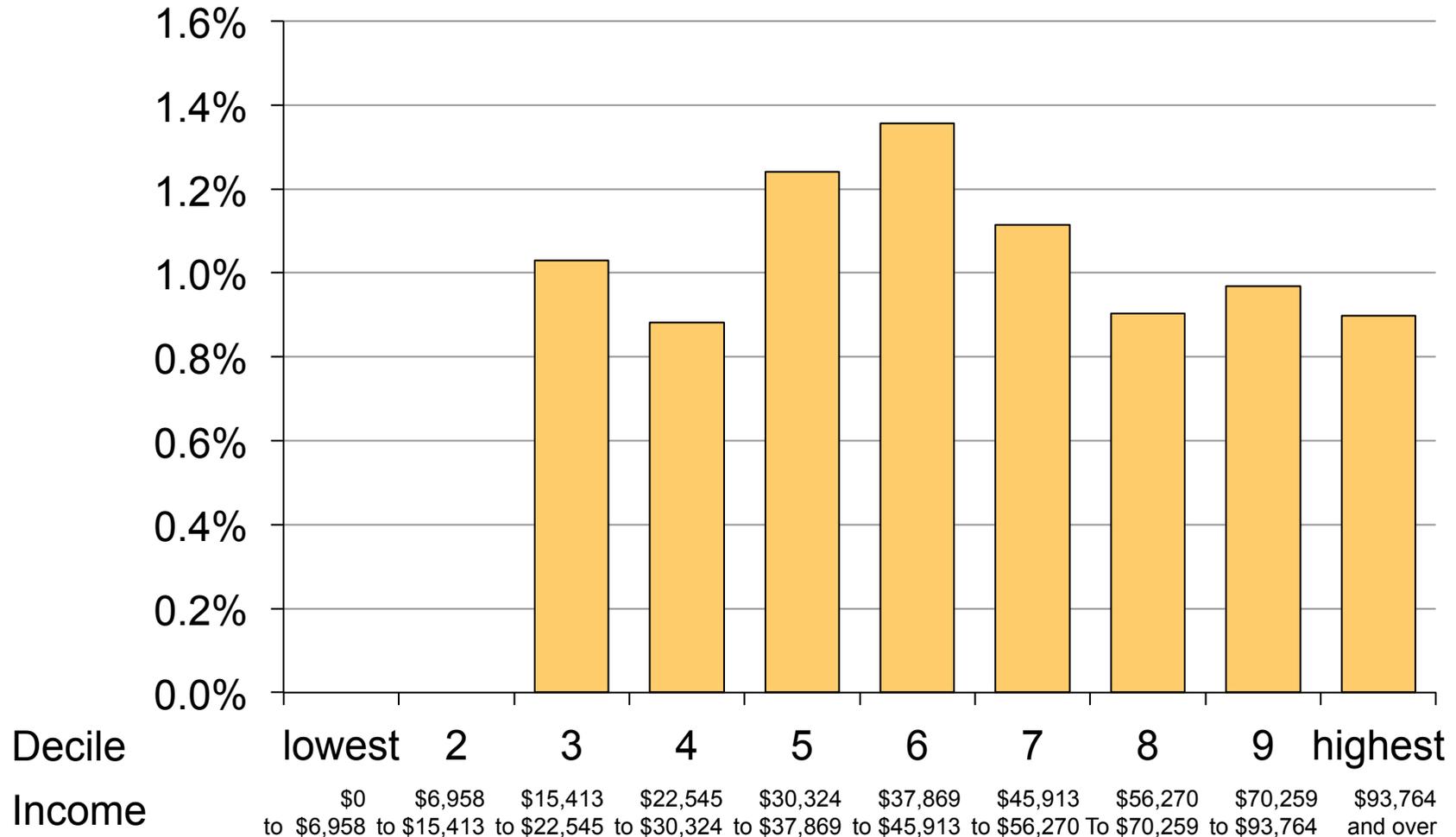
2016-17 budget compared to 2013-14 budget, % of GDP



# Bracket creep hits middle income earners most

## Impact of bracket creep, 2013-14 to 2016-17

Additional percentage of income paid in tax, by taxpayer income decile



Source: Treasury, *Budget Paper 1*, ATO, *Taxation* statistics 2010-11, Grattan analysis

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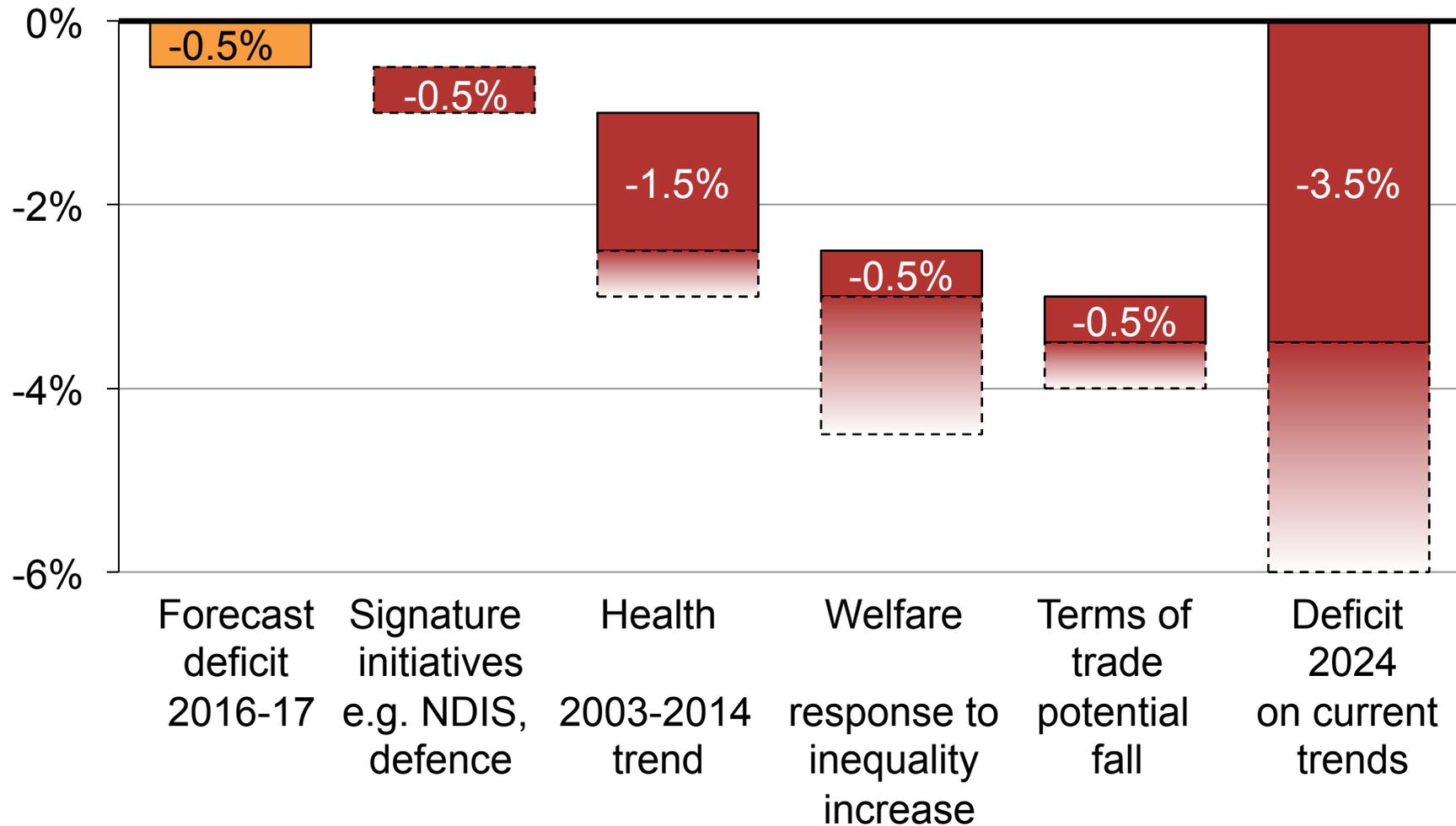
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# Longer term budget settings are not sustainable

## Potential annual deficit of Australian governments' budgets by 2024 (Percent of GDP)

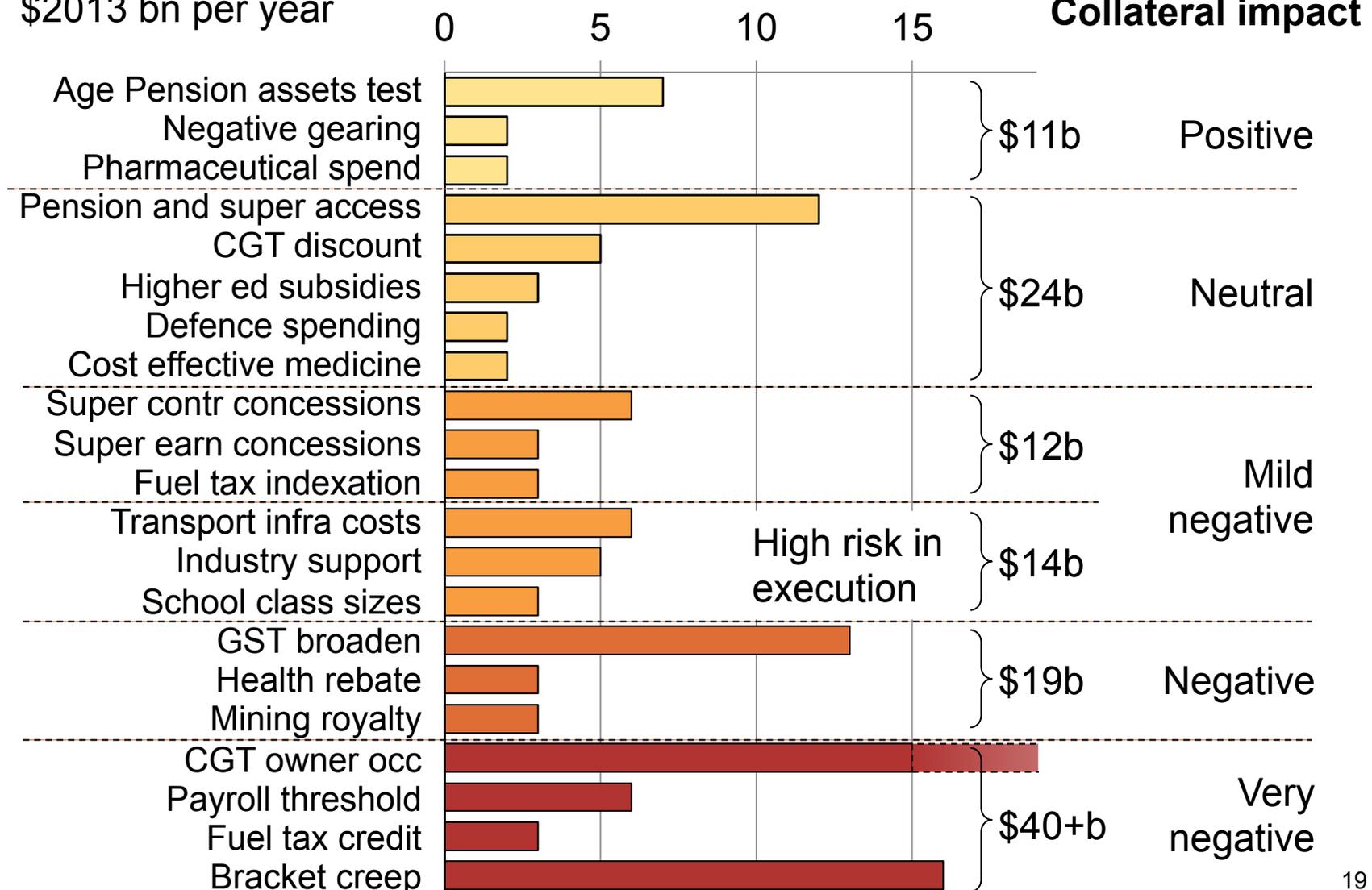


# Few options for budget repair are both large and socially responsible

## Budgetary impact of tough budget choices in ten years' time

\$2013 bn per year

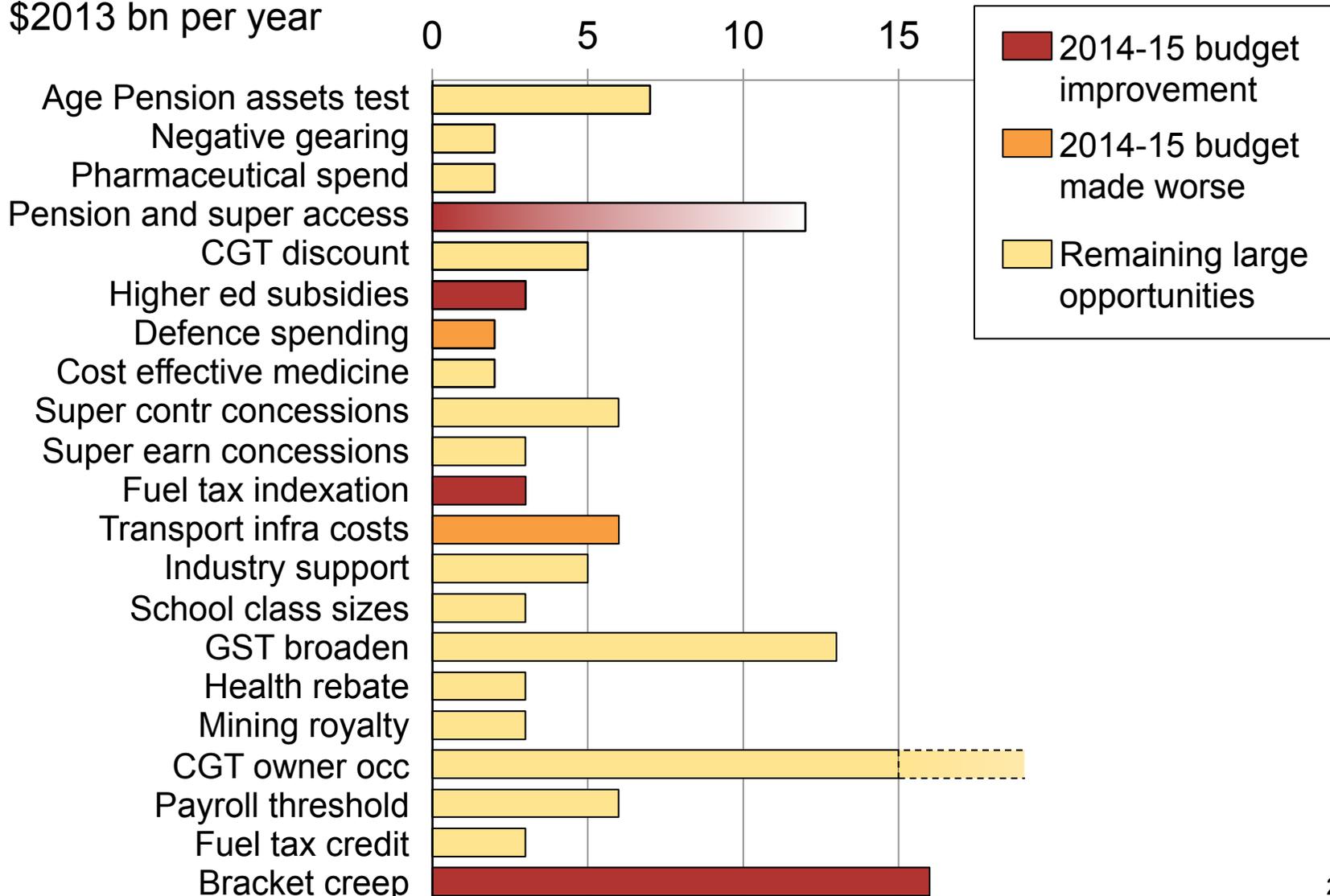
Collateral impact



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## Budgetary impact of tough budget choices in 10 years' time

\$2013 bn per year



Source: Grattan Institute, *Balancing Budgets*