

#5  
Lessons from the Anglosphere



# Australian Fiscal Reforms

Since 1985

Robert Carling

November 2017



True North in  
Canadian public policy





True North in  
Canadian public policy



## Board of Directors

---

### CHAIR

#### **Rob Wildeboer**

Executive Chairman, Martinrea International Inc.,  
Vaughan

### VICE CHAIR

#### **Pierre Casgrain**

Director and Corporate Secretary,  
Casgrain & Company Limited, Montreal

### MANAGING DIRECTOR

#### **Brian Lee Crowley**

Ottawa

### SECRETARY

#### **Vaughn MacLellan**

DLA Piper (Canada) LLP, Toronto

### TREASURER

#### **Martin MacKinnon**

CFO, Black Bull Resources Inc., Halifax

### DIRECTORS

#### **Blaine Favel**

Executive Chairman, One Earth Oil and Gas, Calgary

#### **Laura Jones**

Executive Vice-President of the Canadian Federation  
of Independent Business, Vancouver

#### **Jayson Myers**

Chief Executive Officer,  
Jayson Myers Public Affairs Inc., Aberfoyle

#### **Dan Nowlan**

Vice Chair, Investment Banking, National Bank  
Financial, Toronto

#### **Vijay Sappani**

Co-Founder and Chief Strategy Officer,  
TerrAscend, Mississauga

## Advisory Council

---

#### **John Beck**

President and CEO, Aecon Enterprises Inc., Toronto

#### **Erin Chutter**

Executive Chair, Global Energy Metals Corporation  
Vancouver

#### **Navjeet (Bob) Dhillon**

President and CEO, Mainstreet Equity Corp., Calgary

#### **Jim Dinning**

Former Treasurer of Alberta, Calgary

#### **David Emerson**

Corporate Director, Vancouver

#### **Richard Fadden**

Former National Security Advisor to the Prime Minister,  
Ottawa

#### **Brian Flemming**

International lawyer, writer, and policy advisor, Halifax

#### **Robert Fulford**

Former Editor of *Saturday Night* magazine,  
columnist with the *National Post*, Ottawa

#### **Wayne Gudbranson**

CEO, Branham Group Inc., Ottawa

#### **Stanley Hartt**

Counsel, Norton Rose Fulbright LLP, Toronto

#### **Calvin Helin**

Aboriginal author and entrepreneur, Vancouver

#### **Peter John Nicholson**

Inaugural President, Council of Canadian Academies,  
Annapolis Royal

#### **Hon. Jim Peterson**

Former federal cabinet minister,  
Counsel at Fasken Martineau, Toronto

#### **Barry Sookman**

Senior Partner, McCarthy Tétrault, Toronto

#### **Jacquelyn Thayer Scott**

Past President and Professor, Cape Breton University,  
Sydney

## Research Advisory Board

---

#### **Janet Ajzenstat,**

Professor Emeritus of Politics, McMaster University

#### **Brian Ferguson,**

Professor, Health Care Economics, University of Guelph

#### **Jack Granatstein,**

Historian and former head of the  
Canadian War Museum

#### **Patrick James,**

Dornsife Dean's Professor,  
University of Southern California

#### **Rainer Knopff,**

Professor Emeritus of Politics, University of Calgary

#### **Larry Martin,**

Principal, Dr. Larry Martin and Associates and Partner,  
Agri-Food Management Excellence, Inc.

#### **Christopher Sands,**

Senior Research Professor, Johns Hopkins University

#### **William Watson,**

Associate Professor of Economics, McGill University



## Table of Contents

---

<b>Foreword</b>	<b>2</b>
<b>Introduction</b>	<b>4</b>
<b>Why Fiscal Reform?</b>	<b>5</b>
<b>Overview of Fiscal Reforms</b>	<b>6</b>
Institutional and fiscal governance reforms	6
Management of the fiscal balance and public debt	7
Expenditure policy	10
Tax policy	13
Efficiency in resource allocation	16
Fiscal federalism	17
Conclusions and key lessons	18
<b>About the Author</b>	<b>20</b>
<b>References and Major Data Sources</b>	<b>21</b>
<b>Endnotes</b>	<b>22</b>

*The author of this document has worked independently and is solely responsible for the views presented here. The opinions are not necessarily those of the Macdonald-Laurier Institute, its Directors or Supporters.*

# Foreword

---

—Peter Costello, Treasurer of the Commonwealth of Australia, 1996-2007

Most policy-makers would agree that in times of recession it is natural and beneficial for a Government to run a Budget deficit. After all, in a recession people are thrown out of work and tax collections decline. People out of work draw down on the social safety net, and expenditures increase. As an economy grows out of recession this process should reverse – these natural stabilizers should unwind and improve the Government’s financial position, bringing the Budget back to balance.

But what do you do if an economy, years out of recession, is growing strongly and the Budget continues to haemorrhage? If a Government is running deficits in years of plenty, imagine how those deficits will magnify if the economy goes into downturn. If a Government is borrowing in good times,

then it will be borrowing much more in lean times. A country that is perpetually borrowing – throughout the economic cycle – is asking for trouble. And it will come, eventually.

“No area of spending was quarantined from spending reduction. We tried to share the burden equitably.”

This was the challenge I faced when I became Australian Treasurer in early 1996.

We had been through a recession in 1991. The Budget went into deep deficit. As economic growth took off, the Government promised it would bring the Budget back into balance. After several years of strong growth, the Government forecasted a Budget surplus in 1995 and all the following years of projections. But it was a very liberal and creative accounting regime. When I took office there was no surplus, we

were facing our seventh consecutive Budget deficit, at around 2 percent of GDP. Without corrective action these deficits would have continued into the 2000s.

In my first Budget Speech I put it like this:

Our predecessors had Australia on a path of deficit and debt to the next century. Make no mistake, this path would only make future choices harder, future possibilities bleaker and rob Australians of the future opportunities they deserve. Our Government could not stand back and ignore the problem. Although we did not create it. We will take responsibility to fix it.

We set out a two-year plan to balance the Budget and to do it principally on the expenditure side. Over two years we cut expenditure by 1.7 percent of GDP, and revenue increased 0.4 percent of GDP. Cutting expenditure was not popular. But we called on the public to come on the journey with us and promised it would, in due course, produce results.

Apart from defence, which was already badly run down, no area of spending was quarantined from spending reduction. We tried to share the burden equitably. We asked all sectors to make their contribution.

One of the key things that helped was a clear explanation of the nature of the problem. People will not support difficult and tough measures just for the sake of it. They might support them if they think they are necessary. But you will have to convince them that they are necessary, and convince them

that they will solve a real problem. A doctor has to diagnose a patient before the patient can understand what the treatment is all about and co-operate with it. And of course, the treatment has to be the right one to cure the illness.

Our point was that if the Government was rapidly running up debt in the good times it would find itself awfully exposed in the bad times. Younger Australians saddled with debts run up by their parents were going to inherit less opportunity. Their taxes would be higher – not to buy services for themselves and their own generation – but to pay the bills their parents had never bothered to fund. It would be a very bad form of inter-generational transfer for those who took the services in our generation to bequeath the taxes to pay for them to the next.

And so we set out our goal – to balance the Budget on average over the course of the economic cycle. This meant that when the economy was growing strongly the Budget would be in surplus and we would pay down debt. If we could get the Budget in balance and debt under control, the Government wouldn't need as much tax – it could cut taxes. If taxes were reduced the economy would grow stronger and the virtuous cycle continue.

We set ourselves the task of balancing the Budget in our first term of government. In our second term we set ourselves the task of reforming and lowering tax. We introduced a GST, and abolished seven pre-existing indirect taxes. We cut Income Tax, Company tax, and Capital Gains tax. By our fourth term we had repaid the Commonwealth Government's debt in net terms. We established a Sovereign Wealth Fund – the Future Fund – to invest future Government surpluses.

From 2006, the Government debt to GDP ratio was better than zero. In fact, we had a negative debt to GDP ratio because of the assets we held in the Government owned Future Fund.

During this period of Budget repair, Australia's sovereign credit rating was upgraded twice to its current AAA-level.

Over the twelve Budgets I delivered, there were ten surpluses. And then, in 2007, our Government was voted out of office. We had been in office nearly twelve years. The public thought it was time for a change. Maybe they thought balanced budgets and tax cuts would continue to deliver themselves.

In 2008, the international financial system experienced great strain. Many countries went into recession. Australia did not. No major Australian bank failed. In fact, no major Australian bank experienced even a quarterly loss, let alone an annual loss. The Government unleashed a lot of fiscal stimulus. With such a strong Balance Sheet it had the means to do so.

As a result of that stimulus, the 2009 the Australian Budget went back into deficit. Although Governments of both political persuasion have promised to rectify the situation, it has remained there ever since. We have had ten Budget deficits since the massive fiscal stimulus that nicely match the ten previous surpluses. All the debt that was paid off when I was Treasurer has been borrowed back again.

People often ask whether it was worth paying off the debt given that subsequent Governments have gone out and borrowed it all back.

The only answer I can give is to say: just imagine where we would be if we hadn't paid off that

“If the Government was rapidly running up debt in the good times it would find itself awfully exposed in the bad times.”

debt. Sure, subsequent Governments have piled on debt, but if we hadn't got the Commonwealth debt free, they would have piled debt on pre-existing debt rather than debt against a strong asset position.

Even today Australian Government net debt is much lower than comparable companies. Our fiscal journey over the last ten years has been bad. But our starting point was extremely strong. It was the starting point that gave us the ability to weather the 2008 storm.

We still have a lot of other things to show from the strong fiscal management of previous years. We have a system of transparency in financial reporting that is second to none. This is prescribed by law under the Charter of Budget Honesty. As I have said, our Balance Sheet is comparatively strong because we went debt-free from 2006. Although memories dim, the public remembers the days of balanced Budgets not as a horror time, but as a period of great success. Most Australian politicians still pay lip-service to the policy of balancing the Budget over the course of the economic cycle. And we have a Future Fund.

No Government can expect to bind its successors. The argument for strong fiscal policy has to be mounted again in each election and in each generation. But successful prior experience should encourage those now engaged in that argument, that the public will support a well-designed program and it can be successful.

## Introduction

---

Australia has been described in recent decades as a “miracle” economy because of the longevity and strength of its growth, the absence of recessions, and the degree of improvement on the country's prior economic performance (Economist 2000).

Miracles come from supernatural forces, and there has been no miracle in Australia, though certainly for much of the past 30 years Australia has out-performed other advanced economies thanks to a combination of its economic policies and favourable external shocks. The starting point is somewhat arbitrary, but there was a decisive break in economic policies in the mid-1980s that began the reform path, even though the actual improvement in economic performance did not become apparent until some way into the 1990s.

This charting of a new path on economic and fiscal policy was by no means inevitable. It reflected choices by Australian policy-makers to liberalize the country's economy and strengthen its public finances. A new multi-partisan consensus was formed that favoured markets and disciplined spending. Australia has reaped the benefits ever since.

There is, however, evidence of growing complacency and reform fatigue in Australia, including backsliding on fiscal policy. Abandoning the policy course that has served the country so well for the past 30 years would be foolhardy.

The purpose of this essay, then, is to describe the economic and political circumstances that led to this new policy course, to detail and analyze the composition of Australia's fiscal reforms, and to highlight the economic and social outcomes associated with them. The goal is not only to remind Australia's policy-makers of the success of its economic and fiscal reforms, but also to share this experience with an American audience as policy-makers in the US grapple with how best to deal with Washington's growing budgetary crisis.

# Why Fiscal Reform?

---

The long history of Australia's under-performance up to the 1980s was reflected in sluggish economic growth, weak productivity growth, slippage in living standards relative to other advanced countries, relatively high inflation, union-led strife in the workplace, high tariff barriers and other forms of protection, low domestic saving, excessive fiscal deficits, and an inefficient tax system. Why these problems were not addressed earlier is an issue for the political scientists. Suffice it to say that a new Labor (centre-left) government elected in 1983 and re-elected in 1984 resolved to tackle the malaise and had the broad support of the Liberal-National (centre-right) parliamentary opposition, which in turn continued the reform approach when it came to government in 1996.

Economic performance improved noticeably after a severe recession in the early 1990s: low inflation became entrenched, there was a period of strong productivity growth, unemployment returned to levels not seen since the early 1970s, there were fiscal surpluses, and the general government net debt was eliminated. There has been no recession (on the admittedly deficient mechanical definition of two consecutive quarters' decline in real GDP) since 1991 – setting a new record for advanced economies – although on other definitions there was a mild recession coinciding with the global Great Recession of 2008–2009. Australia has progressed up the international economic league tables.

However, these successes are, of course, not only attributable to Australia's own reform efforts. As a major exporter of minerals, Australia has benefited enormously from China's industrial revolution. After a long period in the doldrums, Australia's terms of trade index doubled from the early 2000s to a peak in 2011. This, combined with earlier policy reforms, helped generate the largest improvement in living standards (over a relatively short period) since the gold rush boom of the colonial 1850s.

More recently though, prosperity has bred complacency and reform fatigue, and the forces of populism evident in other countries are evident in public policy initiatives in Australia. Fiscal performance has deteriorated markedly since 2007. It remains to be seen whether Australia learns from other countries' failures and returns to the reform path, or itself becomes a case study of failure to adjust.

The earlier reforms did not consist of a single roadmap but evolved over time. At different times they included liberalization of the exchange rate and capital flows, domestic financial deregulation, changes in the conduct of monetary policy, deregulation of the labour market including workplace relations, industry policy including protection, competition policy for goods and services markets, retirement incomes policy, education and training, and fiscal policy including fiscal federalism and privatization of state-owned enterprises. This paper is confined to an examination of the fiscal reforms, while recognizing the importance of other reforms.

Australia is constituted as a federation with a central government and six sovereign states. The central government is the dominant fiscal power – particularly in taxation – and makes large transfers to the states (vertical fiscal imbalance being very high). In the interest of consistency with other papers in the Anglosphere project, the focus here is on central government fiscal policy. This is not to deny that states have also undertaken fiscal reforms of their own.

“Abandoning the policy course that has served the country so well for the past 30 years would be foolhardy.”

# Overview of Fiscal Reforms

---

The fiscal reforms undertaken since the mid-1980s fall into six thematic categories:

1. **Institutional:** use fiscal rules and targets, lengthen the time horizon for fiscal policy, legislate the framework for fiscal policy, change accounting and financial management practices, establish a sovereign wealth fund, and establish a Parliamentary Budget Office.
2. **Management of the fiscal balance and public debt:** bring the budget into balance, use deficits and surpluses in economic management, reduce general government net debt.
3. **Expenditure management:** control the government spending growth rate and share of GDP, and take specific measures towards this objective.
4. **Taxation:** use tax policy changes in short-term economic and fiscal management, implement longer-term reforms, and develop policies on the overall tax burden and size of government
5. **Efficiency of resource allocation:** privatize and corporatize state-owned enterprises.
6. **Fiscal federalism:** reform general grants and those tied to the states, have the states participate in national tax reform.

The following sections expand on each of these categories.

The objectives of fiscal reform have evolved from an initial emphasis on reducing the fiscal deficit to helping to bolster national saving, reducing the external current account deficit, and bringing inflation under control. Later there came a stronger emphasis on privatization and corporatization, both to raise revenue and improve the efficiency of resource allocation in the economy. Deficit and debt reduction became prominent again after the early 1990s recession and a change in government in 1996.

In the 2000s the emphasis turned to management of the revenue windfall and fiscal surpluses resulting from the China-driven resources boom. In 2008 the emphasis shifted abruptly to fiscal stimulus as a means to soften the blow of the global Great Recession, and new social spending programs were added by the centre-left Labor government. These developments, together with the fading resources boom, produced a structural fiscal deficit and the emphasis has once again (but so far largely unsuccessfully) turned to reducing the deficit and public debt.

Throughout the last 30 years the imperative of tax reform has come to the fore on several occasions, prompted by considerations of economic efficiency, equity, international benchmarking, long-term revenue performance and deficiencies in fiscal federalism.

## Institutional and fiscal governance reforms

There has been little interest in “large C” constitutional changes in support of fiscal reform (such as a balanced budget amendment), as governments and their advisers shun the rigidities that constitutional constraints would impose on them. In any case, as a practical matter, it has proven very difficult to amend the Australian Constitution. There have, however, been other changes to the legal and institutional basis of fiscal policy.

1. **The use of fiscal rules and targets.** At various times – usually when fiscal consolidation was needed – governments have adopted quantitative fiscal rules and targets to signal their commitment to fiscal adjustment in a medium-term framework and to steer the type of adjustment in their preferred direction. These rules and targets have been self-imposed by executive government, have not been legislated, and are not subject to any enforcement mechanism other than public opinion.



For example, in the 1980s there was a “trilogy” of quantitative constraints on the deficit and both tax revenue and expenditure as proportions of GDP. However, there has since been a lack of consistency in the nature of these rules and targets. The most enduring and bipartisan has been the commitment to balance the budget on average over the business cycle, which more recently has evolved into achieving a surplus (unquantified) on average over the cycle. There was a legislated debt ceiling for a time, but it was abolished in 2013.

2. **The Charter of Budget Honesty.** The Charter was legislated in 1997 to provide a framework for fiscal transparency and discipline, and this legislation has bipartisan support and remains in force. However, it contains no fiscal rules or targets. Rather, it sets out broad principles for the conduct of fiscal policy and requirements for fiscal reporting.
3. **A longer-term horizon for fiscal policy.** Four-year budget forward estimates were adopted in the 1980s to demonstrate the medium-term consequences of current expenditure and revenue policies. The above-mentioned Charter of Budget Honesty introduced a requirement for “inter-generational reports” at five-year intervals. These reports take a 40-year forward view of the budget based on existing policies, attract as much public attention as annual budgets, and have influenced policies, such as those shaping the impact of population aging on government expenditure.
4. **Accounting and financial management changes.** Australia was one of the first countries to adopt accrual accounting in the public sector (in the late 1990s). This focused greater attention on the public sector balance sheet and limited opportunities for the government to distort annual budget results by arbitrarily shifting cash flows across years. However, while accrual-based results are published, the government continues to emphasise the cash budget result in its reporting.
5. **Establishment of the Future Fund.** This fund, although in essence the same as a sovereign wealth fund, was set up in 2005 to match the liabilities of the unfunded pension plan for civil servants. Injections to the fund came from privatization proceeds and, to a lesser extent, budget surpluses. Creation of the fund may have made budget surpluses politically easier to sustain. There have been no new injections since 2007, but through investment returns the fund has grown to around AU\$130 billion, which still falls short of fully funding pension liabilities. While it was desirable to reduce the unfunded pension liability, in broader terms there are arguments against sovereign wealth funds – for example, the available funds would be better used to finance productivity-enhancing tax cuts or infrastructure projects.
6. **Establishment of a Parliamentary Budget Office (PBO).** This office was created in 2012 to add a more independent voice to fiscal policy processes. In its own words, the PBO’s purpose is to “inform the Parliament by providing independent and non-partisan analysis of the budget cycle, fiscal policy and the financial implications of proposals” (Australia undated). Unlike its UK counterpart, however, the PBO plays no direct role in the preparation of the budget, such as in determining the macroeconomic assumptions underlying budget estimates.

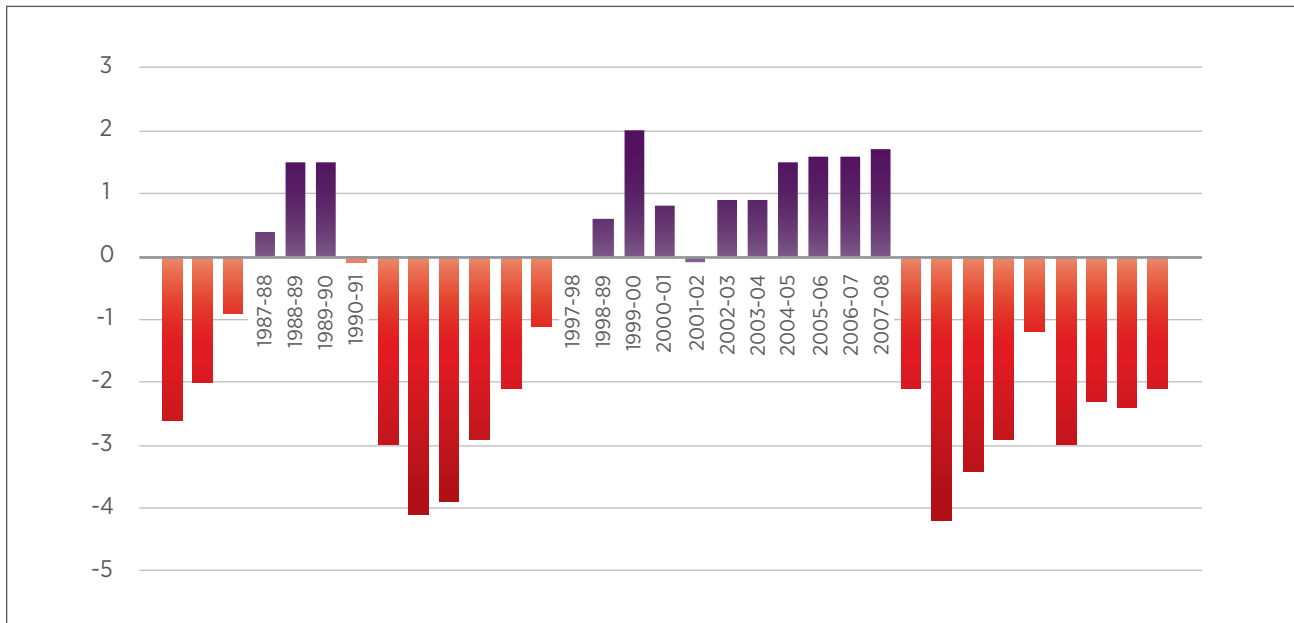
It is difficult to say what difference these changes to institutional and fiscal governance arrangements have made to actual fiscal outcomes. Certainly, it can be said that budget procedures, documentation, and transparency have improved greatly and are now among the best in the world. Governments with a weak fiscal record have nowhere to hide. While these improvements supported an improvement in fiscal performance up to 2007, they have not prevented a serious weakening since then. Strong fiscal institutions and governance arrangements are an essential foundation of good fiscal policy, but they cannot compensate for a lack of political resolve in addressing underlying fiscal problems.

## Management of the fiscal balance and public debt

Fiscal consolidation – achieving balanced or surplus budgets and keeping public debt low – has been a regular theme of fiscal policy. As noted above, the most consistent fiscal rule has been maintenance of a balanced or surplus budget on average over the business cycle. The record of achievement against that benchmark is mixed.

As Figure 1 illustrates, the deficit has been low by international standards, both on average and at its cyclical peaks, averaging 0.8 percent of GDP in the 30 years to 2016, 0.6 percent in 20 years, and 1.8 percent in the last 10 years. It could also be said there was an improving trend, with the 10-year average dropping from a deficit of 1.6 percent to 1986 to 1.2 percent in 1996 and a surplus of 0.7 percent in 2006. However, the trend has subsequently been reversed, with the 10-year average rising to a deficit of 1.8 percent of GDP in 2016.

**FIGURE 1: Federal budget balance, percent of GDP, 1985-2017**



Source:

The long-standing rule of balancing the budget, on average, over the business cycle has not been achieved. It is true that 11 consecutive years of balanced or surplus budgets up to 2008 gave the appearance that the rule was being achieved, but in fact that period featured continuous economic expansion and high commodity export prices rather than a business cycle. The expansion was interrupted by only minor slow-downs in growth and was fuelled by Australia’s largest ever resources boom, which supercharged tax revenue growth to 8 percent a year in the five years to 2007-08. Since the boom ended, revenue has been repeatedly written down and sizeable budget deficits have prevailed, more than offsetting the preceding run of surpluses. Over a long period including both boom and bust, the budget has been in deficit on average (for example, an average of 1 percent of GDP in the period 2002 to 2017).

The negative side of this mixed record stems from the fiscal consequences of a severe recession in the early 1990s and the global financial crisis of 2008-09. In each case, the operation of automatic fiscal stabilizers inflated the deficit and was reinforced by discretionary fiscal stimulus. The stimulus was particularly aggressive in response to the global crisis of 2008-09, with Australia registering an above-average dose of stimulus among G20 countries. Both episodes represented a departure from previous official statements that fiscal policy should maintain a medium- and long-term focus and not be side-tracked by short-term macro-economic stabilization considerations. In each case the budget swung from surplus to deficit by around 6 percentage points of GDP in two or three years to a peak deficit of around 4 percent of GDP (see Figure 1). Following the typical asymmetric pattern of discretionary fiscal stimulus, part of what was intended to be temporary became structural and the unwinding of the inflated deficit was slow until concerted consolidation efforts began.

While it is generally accepted that automatic fiscal stabilizers should be allowed to work, the wisdom of discretionary fiscal stimulus – particularly the large dose applied in 2008-09 – remains hotly debated. The Australian economy held up relatively well during the global crisis, but other favourable influences at the time may account for that outcome. Proponents say the stimulus was justified by the scale of the threat from the global crisis and that fiscal multipliers were large enough for the stimulus to provide significant support to economic activity and employment. Others argue that any stimulus was largely offset by other variables such as interest and exchange rate effects, the multiplier being close to zero, and that the stimulus comprised wasteful measures and put the budget onto an unsustainable path to higher public debt in the context of Australia’s high household debt and foreign debt.

The positive side of Australia’s fiscal record can be seen in past episodes of successful fiscal consolidation, or what is now called “austerity.” In the late 1980s and again in the late 1990s, the deficit was reduced by around three percentage points of GDP through discretionary policy action, particularly on the spending side of the budget. Further discussion of how this was done follows in the next section, but it is worth noting here that contrary to the fears often expressed by opponents of consolidation, it did not drive the Australian economy into recession or even produce a growth slow-down of any significant size. A recession did follow the 1980s episode, but that is attributable to a severe tightening of monetary policy.

Those earlier episodes of successful consolidation have not been repeated after the latest large increase in deficit spending following the global crisis of 2008-09. The deficit has come down, but remains elevated seven years after its peak and, under current policies, is projected to continue for several more years. By the same point in previous cycles, the budget was balanced or in surplus thanks to policies of consolidation. This time, a small surplus is projected for 2020-21, but there are serious doubts as to whether this will actually be achieved, and if it is, whether it can be sustained for long. The challenge may have been greater this time due to weaker economic growth, slumping commodity export prices and a slow automatic recovery in budget revenue, but consolidation efforts also have been weaker. Particularly telling has been the failure to make a dent in elevated levels of federal spending sufficient to close the budget deficit. Stimulus-level spending was partly unwound, but this emphasis quickly gave way to renewed spending of a more permanent kind.

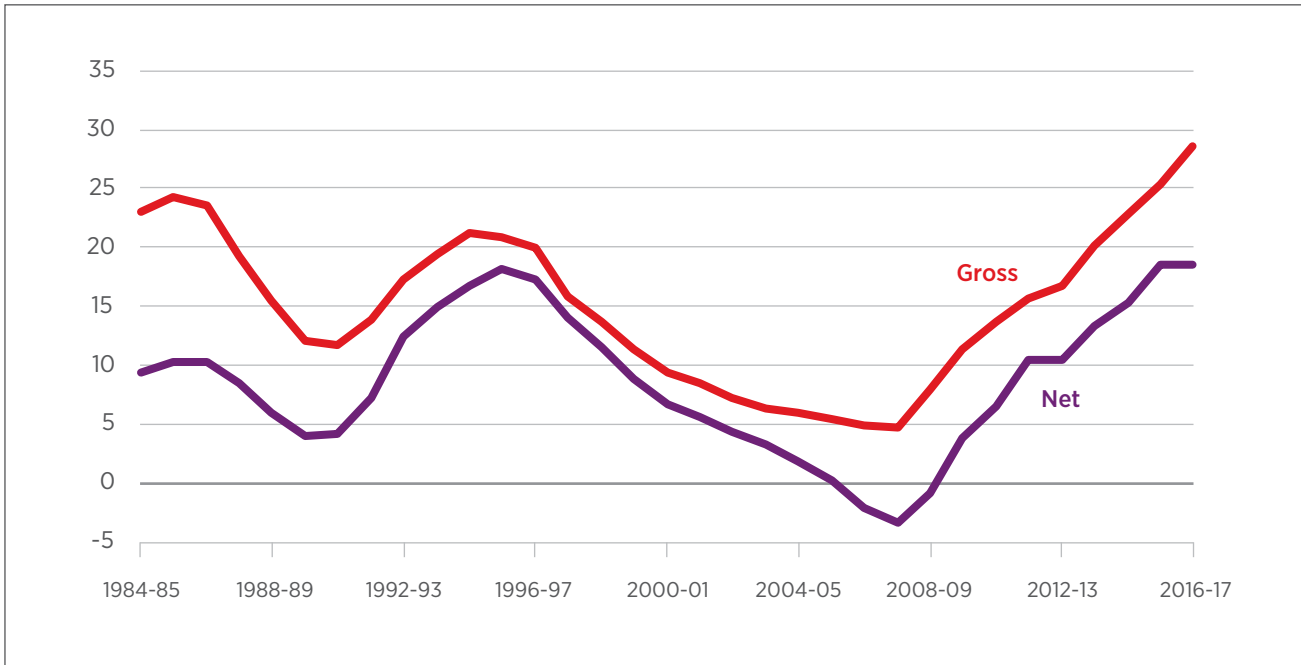
The long-term challenges are clearly set out in the government’s latest Intergenerational Report (2015), which maps fiscal projections over a 40-year horizon. The report shows the budget position improving under then legislated policies until around 2023, then deteriorating continuously so that by 2055, the deficit would be 6 percent of GDP and net debt 60 percent of GDP.

In contrast, and despite the deficits of recent years, federal debt is currently low by international standards with general government gross debt at around 29 percent of GDP and net debt at around 19 percent (see Figure 2). However, if the current level of debt appears manageable, this reflects a favourable starting point rather than the trend of recent years, which has been emphatically unfavourable. The relatively low level of debt reflects the history of low deficits discussed above and the retention of privatization proceeds as financial assets. Cyclically, debt has fluctuated and reached a peak of 18 percent of GDP (net debt) in the 1990s before fiscal consolidation reversed the increase, but it now again stands near 18 percent. Further increases appear certain, with a peak of 20 percent of GDP currently projected by the government for 2019, which the recent track record suggests is more likely than not to be exceeded. It is not so much the current level of debt that is worrying, but its upward

“The positive side of Australia’s fiscal record can be seen in past episodes of successful fiscal consolidation.”

trajectory under current policies. While Australia remains among a handful of governments with a triple-A credit rating, one rating agency has now qualified this with a negative outlook pending the government’s future actions to curb the deficit and growth in debt.

**FIGURE 2: Federal debt, percent of GDP, 1985-2017**



Source:

Policy constraints on the growth of debt have been relaxed recently, as the federal government has taken a more expansive approach to infrastructure spending in the belief that at least some debt incurred for such investments is sustainable whereas debt incurred to finance recurrent deficits generally is not. Although direct capital spending by the federal government is quite limited (mainly defence equipment), the government makes grants to the states and injects debt and equity funding into its own business enterprises for capital purposes. Taking all these forms of capital commitments together, they are projected to increase by around AU\$11 billion a year on average in the four years ending in 2019-20 compared with the preceding four years.

This policy shift in favour of capital expenditure is open to criticism on several grounds. It downplays the fact that much of the existing federal debt reflects past recurrent deficits and that the recurrent budget remains in deficit today. This deficit needs to be corrected before consideration is given to increasing debt for capital expenditures. Even then, the quality of proposed infrastructure spending and its contribution to future economic growth needs to be carefully examined. In practice, some infrastructure spending is undertaken for political reasons and would fail a rigorous cost/benefit analysis.

### Expenditure policy

Australia has big government, even if it is not as big as in some other developed countries where government spending exceeds 40 or even 50 percent of GDP. In Australia, the proportion stands at around 37 percent for all levels of government combined, of which some three-quarters is financed by the federal government either directly or indirectly via transfers to lower tiers of government. The welfare state is as extensive as in other developed countries and social benefits are as generous, but the cost is more contained because benefits are more tightly targeted by means testing and other eli-

gibility criteria. Moreover, private savings make a major contribution to retirement incomes through a system of compulsory, tax-favoured private retirement accounts. These features have kept the public sector below 40 percent of GDP.

The familiar forces behind the long-term growth in the size of government in many countries are also evident in Australia. Expenditure policy reflects the tension between these forces and the pressure to limit the tax burden and budget deficits. Pressures to increase spending through new programs and the widening of existing programs are always present, while the countervailing forces tend to come into play only when the budget deficit becomes problematic. To the extent that growth in government spending has been held in check, it is more because of resistance to excessive deficits and tax increases than any widely held belief in the benefit of smaller government.

Three key episodes can be identified since the 1980s when concerns about a deterioration in the fiscal position have focused attention on excesses in federal spending. First, in 1985 federal spending reached the peacetime record level of 27.6 percent of GDP amid concerns about the fiscal deficit, the external current account deficit, and exchange rate weakness. Second, in the mid-1990s a newly elected government, having campaigned on the need to reduce a persistent deficit and reverse the rise in public debt, resolved to attack the problem mainly through spending curbs. Third, since the large fiscal stimulus of 2008-09 and subsequent persistent weakness in tax revenue, successive governments have aimed to slow the growth in spending in order to curb persistent deficits. The first two episodes were examples of successful fiscal consolidation through spending cuts, but the third has been largely unsuccessful.

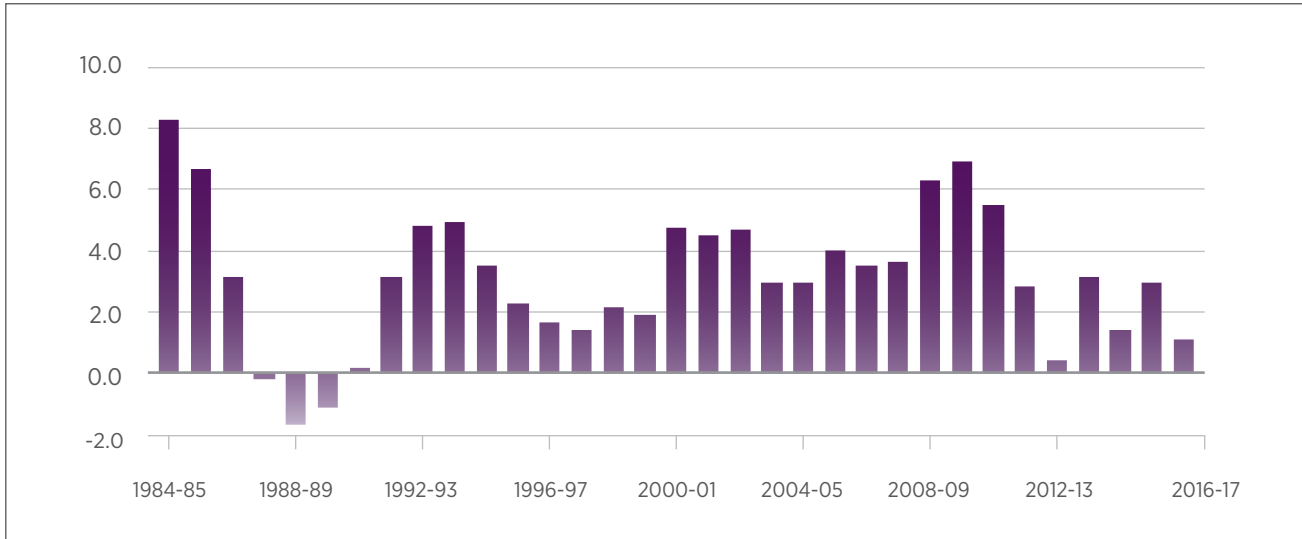
When the need for cuts has overcome the urge to spend more, the particular measures have covered a wide range and it is difficult to generalize. However, the following list provides some examples:

- Tightening of eligibility criteria for social benefits – for example, a tighter means test and increases in the minimum retirement age for the public pension.
- Pauses in indexation of social benefits such as family allowances.
- Periodic intensified culling of ineligible recipients from the ranks of social security beneficiaries.
- Cuts in defence spending, which was 2.2 percent of GDP in the early 1990s but fell as low as 1.7 percent in recent years.
- Cuts in foreign aid, which was as high as 0.5 percent of GDP in the mid-1980s but is now less than half that level.
- Reductions in discretionary grants to the states.
- Efficiency dividends. These are annual clips from the budgets of most departments, and are meant to replicate the pressure for productivity gains in the private sector.
- Reductions in the size of the civil service, though not in pay or benefits.
- Increased or new charges, such as the introduction of university fees in the 1980s accompanied by an innovative income-contingent government loan scheme (HECS), which enables students to defer payment (via the tax system) until their annual earnings reach a certain level.

This is not to suggest that every cut has been permanent. Sometimes they have been politically or otherwise unsustainable, such as the cut in defence spending, which is being restored to 2 percent of GDP.

“*The familiar forces behind the long-term growth in the size of government in many countries are also evident in Australia.*”

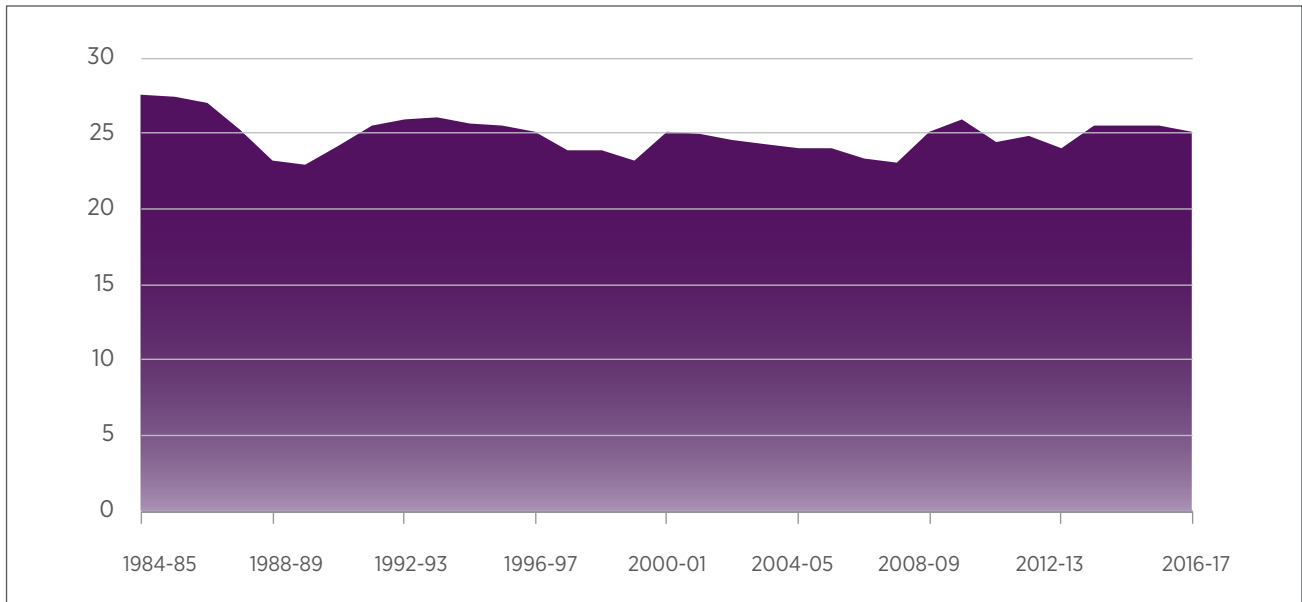
**FIGURE 3: Federal budget spending, 3-year moving average real % change**



Source:

As Figure 3 illustrates, the 1980s episode of spending restraint was the most successful, achieving an absolute reduction in federal spending in real terms, while the 1990s episode severely curbed the rate of growth in real spending for a few years. In each case there was a significant reduction in federal spending as a proportion of GDP (see Figure 4). As a result of this pattern of growth in government spending followed by periods of restraint, spending as a proportion of GDP in the early 2000s was lower than in the mid-1980s. Subsequently it has tended to increase again due to the long period of ample revenue growth generated by the resources boom, the fiscal stimulus of 2008-09, and more recently, the introduction of new social spending programs.

**FIGURE 4: Federal budget spending % of GDP, 1985-2017**



Source:

The most recent episode warrants closer attention as it represents a departure from the past pattern of fiscal weakening forcing strong spending restraint. On this occasion the forces for expenditure discipline have been much weaker. While some spending curbs have been put in place, at the same time

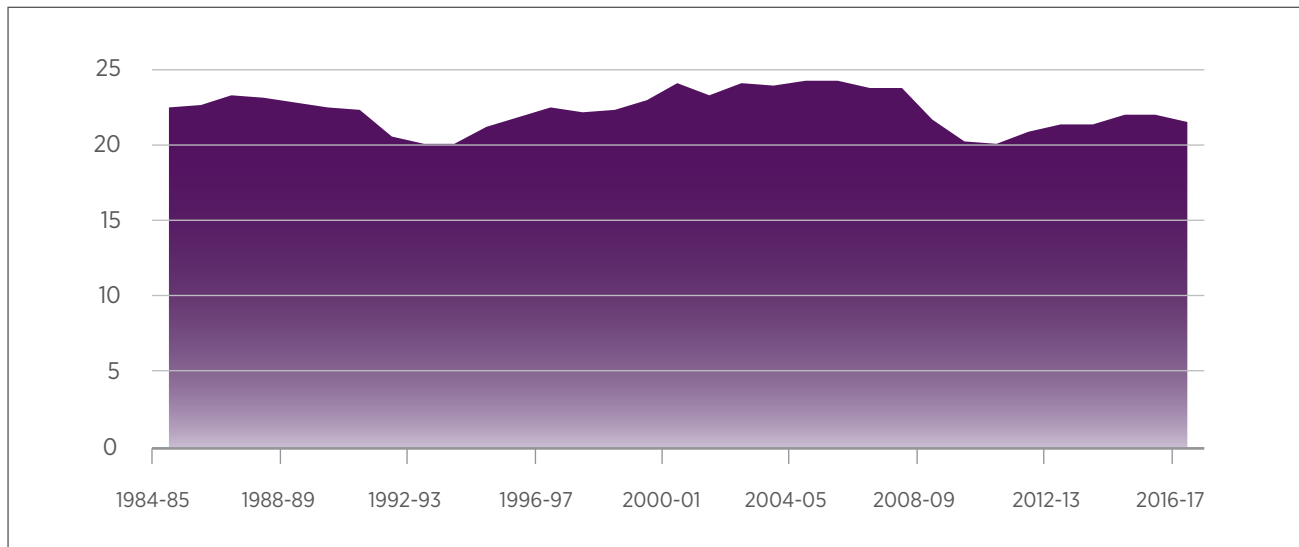
new programs in disability care, school education, and child care have been rolled out, while public expenditure on health continues to grow faster than other programs on average, and faster than GDP. The government's stated objective has been to reduce spending, but its position in Parliament has been weakened by recent election results that rendered it unable to secure parliamentary approval of many expenditure savings measures in the upper house (Senate). Even the measures it has put forward but failed to implement would not have been sufficient to close the budget gap. It has not prosecuted the case for spending restraint effectively in the face of well-organized and effective public campaigns to protect existing programs or promote new ones. The budget for 2017-18 suggests that the current government has largely surrendered to these forces and retreated from expenditure restraint, with expenditure in real terms rising by more than 2 percent a year and maintaining its proportion of GDP.

Government expenditure outcomes have undoubtedly been influenced by the politics of inequality and populism that have been evident in other countries. Even though Australian inequality is unexceptional by international standards and has not significantly changed in recent times, the worldwide movement against inequality has reached Australia, and the perception that it is a major issue has spread without much attention being paid to what the statistics reveal. The largest potential expenditure savings tend to have a disproportionate impact on lower and middle income households and it is therefore difficult for governments to win wide support for them. Increasing taxes has proven politically easier, particularly if the impact is concentrated on big business, multinationals, and individuals with above average incomes.

## Tax policy

Federal tax revenue as a share of GDP has risen strongly over the long term (as has the public sector total, of which federal revenue comprises over 80 percent). There was a particularly rapid increase in the 1970s and early 1980s, which has not subsequently been reversed. Since the mid-1980s the share has fluctuated around an average of about 22 percent of GDP with no clear trend (see Figure 5). There is no official policy ceiling, but when the ratio has risen above the average, pressure for tax relief has intensified, as in the mid-1980s when it reached 23 percent and in the 2000s when it reached 24 percent. On both occasions there were extensive changes to tax policy, as discussed below.

**FIGURE 5: Federal tax revenue, % of GDP, 1985-2017**



Source:

Fluctuations in the tax-to-GDP ratio reflect the economic cycle, but tax policy changes are of more interest to us here. While there have been many policy changes, they have not normally been made for

counter-cyclical purposes; rather, revenue weakness in recessions and strength in booms has reflected the elasticity of revenue in relation to tax bases and the automatic growth of personal income tax revenue in response to inflation in a non-indexed, progressive tax rate scale (the “bracket creep” phenomenon). Policy changes have usually been motivated by one or more of the following objectives:

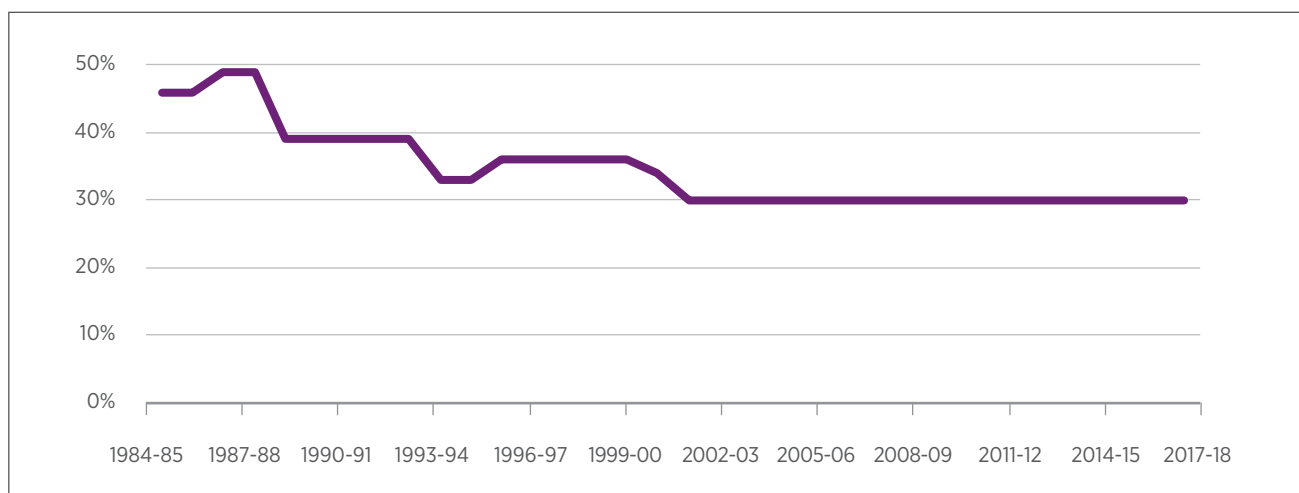
- Relieving built-up pressure of bracket creep, which automatically lifts average income tax rates;
- Reducing imbalances in the composition of tax revenue, particularly the excessive reliance on personal and corporate income tax that has long been a feature of the Australian tax system;
- Maintaining or improving the international competitiveness of Australian taxation, particularly corporate and personal income tax;
- Improving economic efficiency and horizontal equity by broadening tax bases and closing gaps and loopholes;
- Strengthening federalism by using federal policy levers to improve the states’ revenue bases; and
- Managing budget deficits and surpluses.

Such considerations have at times led governments to launch tax reform initiatives based on major reviews of the tax system, leading to bursts of policy changes. This happened in the 1985-89, 1999-2000 and 2003-07 periods.

In 1985, the focus was on reducing high marginal rates of personal and corporate income tax, updating personal tax thresholds, and paying for these changes in part through base-broadening, such as the introduction of a capital gains tax and a fringe benefits tax and reductions in business depreciation allowances. The top marginal personal rate was reduced in stages from 61 percent to 48.5 percent and the corporate rate from 46 percent to 39 percent (see Figures 6 and 7). To a significant degree, Australia was playing catch-up with an international trend towards lower marginal rates that had started several years earlier.

In 1999, personal income tax was again reduced (both by cutting marginal rates and updating thresholds), the corporate rate was cut in stages to 30 percent, and a value-added tax (Goods and Services Tax, or GST) was introduced at a rate of 10 percent to replace a narrowly-based wholesale sales tax and a number of inefficient state financial transactions taxes. Although broad-based by comparison with the sales tax it replaced, the GST itself provided substantial exemptions (such as for unprepared food, water, education, and health services) which took the effective coverage of household consumption expenditure to around 50 percent.

**FIGURE 6: Corporate income tax rate, 1985-2018**



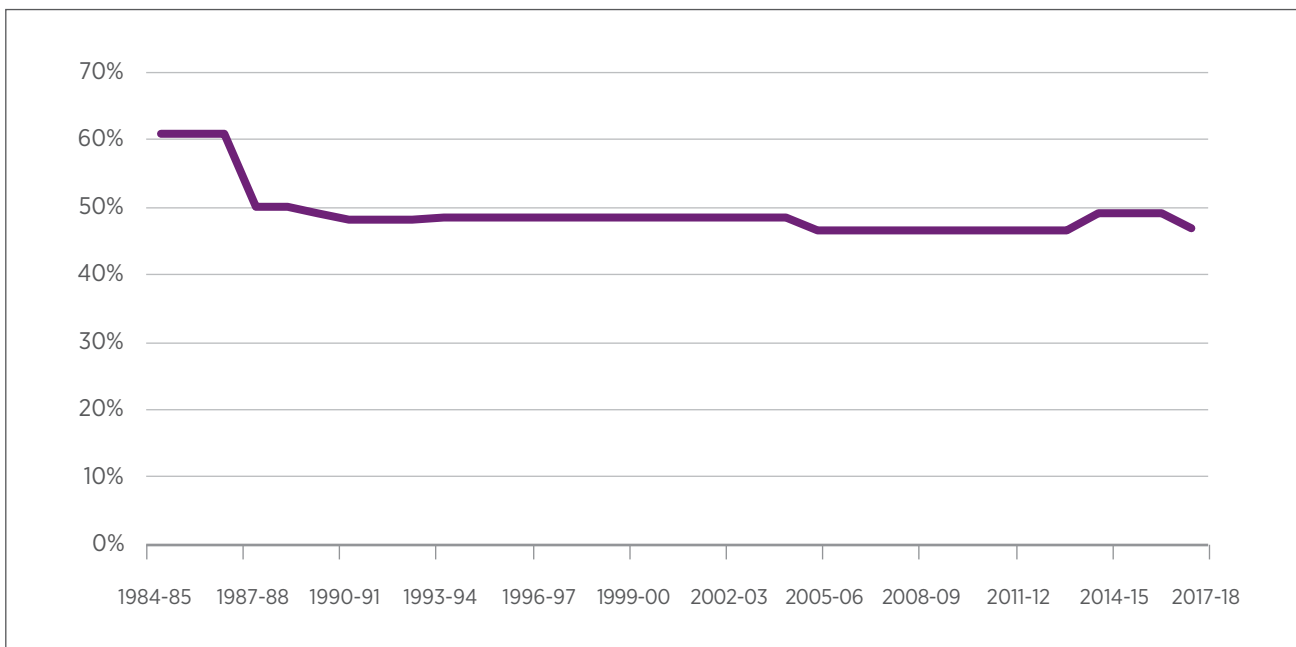
Source:



Beginning in 2003, and in the context of strong revenue growth from the resources-fuelled boom, concerns that personal income tax remained too high were addressed in a series of reductions in marginal rates and large increases in bracket thresholds. Those changes concluded in 2010. They brought the top personal rate down to 46.5 percent and lifted the threshold for that rate from AU\$60,000 to AU\$180,000. However, there was no further reduction in the corporate rate.

As a result of these episodes of tax reform, income tax rates have come down significantly, as Figures 6 and 7 illustrate. However, effective overall income tax rates have not come down as much or at all, because reductions in statutory rates have tended to be offset by base-broadening and bracket-creep effects. Furthermore, the Medicare levy – an additional tax applied to all personal income and in effect a second personal income tax – has already been doubled from its original rate of 1 percent in 1984, thereby offsetting some of the reductions in personal income tax, and is set to rise again in 2019.

**FIGURE 7: Personal income tax top rate, 1985-2018**



Source:

In the field of indirect taxation, Australia has not followed the experience of many other countries (except Canada) that have introduced a value-added tax at a low rate and then increased it. Australia’s 10 percent GST has not been raised since it was introduced in 2000, nor has the base been broadened. There is support among economists for increasing the rate and/or broadening the base to raise extra revenue or fund cuts in direct taxes, but community and political opposition is strong and this may help limit the overall tax burden.

Since 2010, despite attempts by two governments to restart comprehensive tax reform, little has been achieved. The personal tax-free threshold was increased in conjunction with the imposition of a new carbon tax, which was subsequently abolished. A new and ill-conceived federal minerals resource rent tax was introduced as part of a plan to cut the corporate tax rate to 25 percent, but the tax was reshaped prior to implementation and then abolished in the midst of intense political controversy and the corporate rate cut was shelved. The current government has restored the policy of lowering the rate to 25 percent over a number of years, but this has so far been rejected by the Senate in favour of a smaller cut confined to small companies. Another recent and surprising policy change is the adoption

of a tax on major bank liabilities, along the lines of the bank levy in force in the UK since 2011. There have been other tax policy changes, but they are mostly small to medium size changes implemented for the purpose of raising additional revenue, usually dressed up as measures to address perceived inequities and inefficiencies.

In summary, the tax policy changes of recent years have lacked strategic purpose and a coherent reform theme. Their main purpose has been to raise extra revenue in politically opportunistic ways to fund popular expenditure programs. Prior to the recent outbreak of tax increases, the tendency of tax policy in Australia was for increases to be imposed through the stealth policy of bracket creep, while major explicit policy changes or packages of changes were usually revenue-neutral or revenue-reducing. Governments have tended towards the cautious approach of not giving up revenue at times of chronic budget deficits. The series of personal income tax cuts implemented from 2003 to 2010 were consistent with budget surpluses at the time but have been criticized by some for handing back to taxpayers too much of what proved to be temporary surplus revenue and thereby contributing to the current budget problems. However, a stronger case can be made that the government increased spending too much in that period. Had the tax cuts been smaller the extra revenue would have been used to fund and lock in even higher spending, not higher budget surpluses.

Bracket creep has been muted by low inflation in recent years but is still present, gradually lifting effective personal income tax rates and undoing the benefits of earlier tax cuts. The government is relying on bracket creep as well as explicit tax increases to restore budget balance. Further tax reform is needed, but has fallen victim to the general budget malaise, which increases the political challenge of reconciling popularity with fiscal responsibility in shaping tax policy changes. As with expenditure restraint as described above, tax reform has also fallen victim to the politics of inequality and populism, which stand in the way of reductions in upper personal income tax rates and corporate income tax.

## Efficiency in resource allocation

There have been some advances towards greater efficiency in public sector resource allocation, particularly through privatization and corporatization of public enterprises. Historically, the federal government owned a significant number of commercial enterprises – many of them large – but

most have been privatized since the late 1980s. These include businesses in banking, aviation, telecommunications, and health services. As a result, the largest bank, airline, airport, telecommunications company, health insurance company, and biotech company now listed on the Australian stock exchange were once wholly owned by the Australian government. Their market capitalization far exceeds what they were sold for – a fact some say demonstrates that they were sold too cheaply. However, this criticism overlooks the substantial growth and increases in profitability these companies have achieved since being freed from government shackles, not to mention the general increase in stock market valuations.

“*Privatization has undoubtedly been a plus for efficient resource allocation.*”

Privatization has undoubtedly been a plus for efficient resource allocation. It was also a plus for the public finances, as privatization proceeds enabled governments to pay down debt and build up financial assets. However, this benefit may have dissipated over time as the reduction in net debt created more latitude to increase it again in the fiscally less favourable conditions of recent years.

Privatization has become more unpopular and politically contentious, particularly if it involves utili-

ties. Going against the direction of privatization, the Labor government of 2007-13 saw fit to create a new public enterprise for the purpose of building and operating (as a monopoly wholesaler to telecommunications retailers) a national network of high-speed broadband. The successor government has continued along this path with some modifications to the details of the network, the result still being that a business segment of the previously privatized Telstra has effectively been renationalized with negotiated compensation. The NBN Company, as it is known, is receiving some AU\$50 billion of equity and debt funding from the government but its commercial viability remains to be proven. Official policy is ultimately to privatize the company, but it is likely to be unsaleable, at least until its value is heavily written down. Recently, the Liberal-National government decided to build a second Sydney airport as a public enterprise, with the same intention of ultimately privatizing it.

The NBN company and any other business enterprises remaining in government hands (such as Australia Post) are required under the policy of corporatization to operate as commercial entities in that they must have boards, generate profits, be subject to the same taxes as private businesses, and make explicit any subsidies they receive from government.

While initiatives such as privatization and corporatization in the government business enterprise sector have been positive for efficient resource allocation, there is less evidence of improvements in the same direction in the general government sector.

## Fiscal federalism

Fiscal federalism needs to be canvassed here because fiscal relations between national and sub-national governments are an important determinant of economic efficiency and fiscal balance in a constitutional federation such as Australia. Unfortunately, despite false starts, reform has failed in an area that needs it.

At least since the Second World War, the Australian federation has been characterized by a very high degree of vertical fiscal imbalance – that is, the states are heavily dependent on central government transfers – and as a result, the central government has acquired a strong policy influence in functions that are constitutionally the preserve of the states. Currently the states in aggregate receive about 45 percent of their revenue as transfers from the federal government, divided about 50/50 between untied and tied grants. While the problems of functional overlap and duplication, confusion of accountability, and prevalence of “pass-the-buck” behaviour have been much discussed over many years, little has changed. The states have adjusted fully to a condition of financial dependency while the federal government has grown to enjoy wielding fiscal power beyond what the constitutional framers intended it to have.

The tax reforms of 1999-2000 discussed above had reform of fiscal federalism as one of its stated goals. The GST introduced in 2000, although legislated by the federal Parliament and administered by the federal tax administration, was assigned in its entirety to the states in lieu of the more discretionary untied grants that had been paid up to that point. In addition and by intergovernmental agreement, as the GST revenue exceeded the previous untied grants, the surplus was assigned to the abolition of a

“Fiscal relations between national and sub-national governments are an important determinant of economic efficiency and fiscal balance in [Australia].”

group of distorting and inefficient state financial transactions such as a levy on all deposits made to financial institutions.

While these arrangements delivered greater revenue security to the states and, perhaps, more revenue than they would have received had the previous arrangements continued, they failed to deliver greater control of revenue to states either individually or collectively. The relevant GST legislation prescribes that neither the rate nor the base can be changed without unanimous agreement of federal and state Parliaments. While this “lock” helps explain why the GST has not been significantly changed in its 17-year existence, and for that reason may be welcomed by those generally inclined to oppose tax increases, it has the disadvantage of limiting states’ fiscal flexibility.

It should also be said that the GST lock is not binding on successive federal Parliaments and could be undone by new legislation were a federal government so inclined and able to secure a majority in the upper as well as the lower house. The GST is “the states’ tax,” as federal ministers have often provocatively stated, only as long as the federal parliament wants it to be. Meanwhile, decades of High Court constitutional interpretation suggest that the alternative of a state-legislated GST or sales tax would not survive a constitutional challenge.

## Conclusions and key lessons

Looking back over the past 30 years, the record of Australia’s fiscal reform is substantial, although it looked more impressive 10 years ago than it does now.

On the positive side, the structural budget deficit was eliminated through policy action taken in the 1980s and 1990s, before very favourable external shocks pushed the budget into surplus in the first decade of the new century. As a result, net federal debt turned negative for a few years and gross debt dipped to 5 percent of GDP. Federal spending alternated between periods of restraint and accelerated growth, and there was substantial tax reform with reductions in personal and corporate income

tax rates, base broadening, and a new goods and services tax to replace highly inefficient indirect taxes. State enterprises were transformed by privatization and corporatization.

“Australia’s fiscal reform is substantial, although it looked more impressive 10 years ago than it does now.”

As a result of these achievements, when repercussions from the financial crisis in the Northern Hemisphere hit Australia, it was in a strong fiscal position to withstand the shock.

On the negative side, a structural budget deficit has again opened up and it remains to be seen if, when, and how it will be resolved. There are sharp disagreements among economists and political parties about the appropriate pace of fiscal consolidation and whether the emphasis should be on increasing

taxation or reducing spending. What is clear is that current government projections show the budget being balanced by around 2020, with both tax revenue and spending above their long-term averages as proportions of GDP. Given that outlook, and the fact that new spending programs continue to be rolled out, it is clear that the political forces favouring higher spending and taxes are edging out those favouring lower taxes. In that sense, unless there is a change of course soon, Australia is set to become more like the developed countries with bigger public sectors.

Meanwhile, the tax system – leaving aside deficit reduction considerations – remains in need of further reform. There is excessive reliance on direct taxation, with high rates of personal and corporate

income tax that make it increasingly difficult for Australia to compete. Expenditure programs are also in need of reform to make them more efficient and more affordable in the long term as the effects of population aging build up. Both tax and expenditure reforms need to occur alongside reform of fiscal federalism, as there are major imbalances between federal and state governments, and Australia is missing out on many of the benefits of competitive federalism.

Australia's experience holds lessons for other countries contemplating fiscal reform, such as:

- It takes serious problems, if not a crisis, to jolt the political system into taking corrective action.
- Temporary revenue windfalls can sap a country's fiscal strength in the longer term if they are used in ways that lock in fiscal costs.
- Getting the institutional and fiscal governance arrangements right is necessary for fiscal reform, but they won't guarantee it unless there is also the political will to act.
- Comprehensive reform is desirable but rarely achieved. Reform episodes are never complete. Some things that need to be done prove too hard and are left undone for another time.
- Victories in fiscal reform are never permanent. Backsliding can occur and the same lessons have to be learned over and over. The price of fiscal discipline is eternal vigilance. Having seemingly eradicated deficits and debt, Australia is plagued by them again now.
- Times of fiscal plenty make reform easier to achieve – because it is then that the number of losers from reform can be minimized through compensation – but also make the need appear less pressing.
- Fiscal consolidation (or “austerity”) that corrects over-spending and chronic deficits is not contractionary. To the contrary, it strengthens the foundations for economic growth – for example by relieving upward pressure on taxation, lowering uncertainty, improving business and household confidence, taking pressure off interest rates, and improving international competitiveness.
- Conversely, chronic fiscal laxity such as is now evident in Australia has the opposite effects; is not expansionary and contributes to economic drift or worse.
- The forces for higher government spending have become well organized in our democratic systems, while the forces for lower taxation are more disparate.

## About the Author

---



Robert Carling is a Senior Fellow at The Centre for Independent Studies, an independent public policy research and educational institute based in Sydney. He undertakes research into a wide range of public finance issues, writes papers for publication, and regularly comments in the media on taxation and other budget issues. His most recent publication under the CIS banner was *Report Card on State Finances*.

Before joining the CIS, Robert was a senior official with the New South Wales Treasury, where his last position was that of Executive Director, Economic and Fiscal, responsible for advice to the state government on fiscal strategy, taxation and expenditure policies, and Commonwealth/state financial relations. Prior to that he served in a number of roles in a long career at the Commonwealth Treasury.

# References and Major Data Sources

---

- Australia. 2015. *Intergenerational Report 2015*. Government of Australia.
- Australia. 2017. Budget Paper No. 1: Budget Strategy and Outlook. Part of *Budget 2017-18*. Government of Australia (May).
- Australia. Undated. *Parliamentary Budget Office: Establishment, Role, and Legislation*. Web page. Government of Australia. Available at [https://www.apb.gov.au/About\\_Parliament/Parliamentary\\_Departments/Parliamentary\\_Budget\\_Office/role](https://www.apb.gov.au/About_Parliament/Parliamentary_Departments/Parliamentary_Budget_Office/role).
- Australia, Treasury. 2013. *Estimating the Structural Budget Balance of the Australian Government: An Update*. Treasury Working Paper 2013-01. Government of Australia (May).
- Australian Bureau of Statistics. 2017a. *Australian National Accounts: National Income, Expenditure and Product, Mar 2017*. Catalogue No. 5206.0 (June). Government of Australia.
- Australian Bureau of Statistics. 2017b. *Government Finance Statistics, Australia, 2015-16*. Catalogue No. 5512.0 (April). Government of Australia.
- Banks, Gary. 2010. *An Economy-wide View: Speeches on Structural Reform*. Melbourne: Productivity Commission.
- Carling, Robert and Kirchner, Stephen. 2012. *Future Funds or Future Eaters? The Case Against a Sovereign Wealth Fund for Australia*. Policy Monograph 126. Sydney: Centre for Independent Studies.
- Carling, Robert. 2009. *Are We All Keynesians Again?* Issue Analysis number 106. Sydney: Centre for Independent Studies.
- Economist. 2000. "A Survey of Australia: Miracle Cure – How Australia Won Economic Success." *The Economist*, September 7.
- Gruen, David. 2009. *The Return of Fiscal Policy*. Australian Business Economists Annual Forecasting Conference 2009 (December 8).
- International Monetary Fund [IMF]. 2010. *Fiscal Monitor. Fiscal Exit: From Strategy to Implementation*. World Economic and Financial Surveys (November). IMF. Available at <http://www.imf.org/en/Publications/FM/Issues/2016/12/31/Fiscal-Exit-From-Strategy-to-Implementation>.
- International Monetary Fund [IMF]. 2017. *Fiscal Monitor: Achieving More with Less, April 2017*. World Economic and Financial Surveys (April). IMF. Available at <http://www.imf.org/en/Publications/FM/Issues/2017/04/06/fiscal-monitor-april-2017>.
- Makin, Tony. 2016. *The Effectiveness of Federal Fiscal Policy: A Review*. Treasury External Paper 2016-1. Government of Australia (November).
- Potter, Michael. 2016. *The Case Against Tax Increases in Australia: The Growing Tax Burden*. Research Report number 15. Centre for Independent Studies (June).
- Uren, David. 2017. "Wages May Have Stalled but Inequality Is Not Rising in Australia." *The Australian*, April 20. Available at <http://www.theaustralian.com.au/business/opinion/david-uren-economics/wages-may-have-stalled-but-inequality-is-not-rising-in-australia/news-story/0152537c892aa67ed0f7e7e3c68b1818>.

# Endnotes

---

- 1 Real GDP growth slowed to 1.2 percent and real GDP per capita fell by 0.7 percent in the year to 2009 Q3 and unemployment rose from 4.0 to 5.9 percent.
- 2 For a more complete review of the reforms, see Banks (2010).
- 3 See, for example, Carling and Kirchner (2012).
- 4 The measure of the budget balance used in this paper is that defined in the federal budget (Australia 2017, *Budget 2017-18*) as the "underlying cash balance", which the government has used for many years as the key measure of fiscal balance. Other measures reported in the budget are the headline cash balance (which is little different from the underlying cash balance on average over the long term, but currently exhibits a larger deficit); and the fiscal balance and net operating balance (which are accrual accounting concepts).
- 5 Seventy percent of the growth came from corporate income tax (up 14 percent a year) and individual income tax (up to 6 percent a year despite large discretionary tax cuts).
- 6 This finding is confirmed by estimates of the structural budget balance in Australia, Treasury (2013) and Australia 2017, *Budget 2017-18*, which suggest an average structural deficit of around 1.5 percent of GDP in the 15 years to 2016-17 and that the current and projected deficits are entirely structural rather than cyclical.
- 7 According to the IMF, Australia's fiscal stimulus in 2009-11 totalled 5.7 percent of GDP, compared with an average of 5.2 percent for advanced G20 countries (IMF 2010, 6).
- 8 The case for fiscal stimulus in the circumstances of 2008-09 is set out in Gruen (2009), while the other side of the debate is articulated by Carling (2009) and Makin (2009).
- 9 In each year of the expenditure restraint episodes of the 1980s and the 1990s and immediately after, real GDP grew by at least 3.5 percent.
- 10 Total general government debt for federal and state governments combined using IMF standardized definitions is 43 percent (gross) and 21 percent (net) for 2017.
- 11 Federal net debt was negative (that is, financial assets exceeded debt) from 2007 to 2009, while gross debt fell to 5 percent of GDP.
- 12 Since Australia is a net international borrower, infrastructure spending needs to generate a return to the economy at least above world interest rates to generate higher national income.
- 13 The IMF's internationally standardised measure is 37.3 percent for 2016, compared with an average of 39 percent for the advanced countries (IMF 2017).
- 14 David Uren (2017) recently summarized the evidence.
- 15 Major published tax reviews include the Commonwealth Taxation Review Committee (the Asprey review) (1975) which first recommended many of the reforms taken up and refined by later reviews and in some cases adopted by government: A New Tax System (1998) which led among other things to the Goods and Services Tax, Ralph Review of Business Taxation (1999) which led to the cut in corporate income tax to 30 percent, and Australia's Future Tax System (the Henry review) (2010).



- 16 The top marginal rate was increased to 49 percent in 2014 as a “temporary budget repair levy,” but was restored to 47 percent as scheduled in July 2017.
- 17 Corporate income tax revenue increased from around 3 percent of GDP to 4 percent as the headline rate was cut to 30 percent. Personal income tax revenue has declined from a peak of around 13 percent of GDP in the mid-1980s to around 11 percent currently, but is projected to increase to 12 percent by 2020.
- 18 The tax of 0.06 percent on the selected liabilities of five banks took effect on July 1, 2017 and is expected to raise about AU\$1.5 billion a year.
- 19 Such policy changes may be small to medium relative to overall revenue but they may have a large impact on the individuals affected. Examples in recent years include increased taxation on private retirement savings and earnings, increased excise duty on tobacco, curbing of various tax deductions, and resumption of the indexation of fuel excise to inflation.
- 20 The case against tax increases in Australia’s current situation is made by Potter 2016.
- 21 The list includes the Commonwealth Bank of Australia, Telstra, Qantas Airways, Sydney Airport, CSL (formerly Commonwealth Serum Laboratories) and Medibank Private.



True North in  
Canadian public policy

## Critically Acclaimed, Award-Winning Institute

**The Macdonald-Laurier Institute fills a gap in Canada's democratic infrastructure by focusing our work on the full range of issues that fall under Ottawa's jurisdiction.**

- One of the top five think tanks in Canada and No. 1 in Ottawa according to the University of Pennsylvania.
- Cited by five present and former Canadian Prime Ministers, as well as by David Cameron, the British Prime Minister.
- First book, *The Canadian Century: Moving out of America's Shadow*, won the Sir Antony Fisher International Memorial Award in 2011.
- *Hill Times* says Brian Lee Crowley is one of the 100 most influential people in Ottawa.
- The *Wall Street Journal*, the *Economist*, the *Globe and Mail*, the *National Post* and many other leading national and international publications have quoted the Institute's work.



"The study by Brian Lee Crowley and Ken Coates is a 'home run'. The analysis by Douglas Bland will make many uncomfortable but it is a wake up call that must be read." former Canadian Prime Minister Paul Martin on MLI's project on Aboriginal people and the natural resource economy.

## Ideas Change the World

Independent and non-partisan, the Macdonald-Laurier Institute is increasingly recognized as the thought leader on national issues in Canada, prodding governments, opinion leaders and the general public to accept nothing but the very best public policy solutions for the challenges Canada faces.

## Where You've Seen Us



# About the Macdonald-Laurier Institute

## What Do We Do?

When you change how people think, you change what they want and how they act. That is why thought leadership is essential in every field. At MLI, we strip away the complexity that makes policy issues unintelligible and present them in a way that leads to action, to better quality policy decisions, to more effective government, and to a more focused pursuit of the national interest of all Canadians. MLI is the only non-partisan, independent national public policy think tank based in Ottawa that focuses on the full range of issues that fall under the jurisdiction of the federal government.

## What Is in a Name?

The Macdonald-Laurier Institute exists not merely to burnish the splendid legacy of two towering figures in Canadian history – Sir John A. Macdonald and Sir Wilfrid Laurier – but to renew that legacy. A Tory and a Grit, an English speaker and a French speaker – these two men represent the very best of Canada’s fine political tradition. As prime minister, each championed the values that led to Canada assuming her place as one of the world’s leading democracies. We will continue to vigorously uphold these values, the cornerstones of our nation.



## Working for a Better Canada

Good policy doesn’t just happen; it requires good ideas, hard work, and being in the right place at the right time. In other words, it requires MLI. We pride ourselves on independence, and accept no funding from the government for our research. If you value our work and if you believe in the possibility of a better Canada, consider making a tax-deductible donation. The Macdonald-Laurier Institute is a registered charity.

## Our Issues

**The Institute undertakes an impressive program of thought leadership on public policy. Some of the issues we have tackled recently include:**

- Aboriginal people and the management of our natural resources;
- Making Canada’s justice system more fair and efficient;
- Defending Canada’s innovators and creators;
- Controlling government debt at all levels;
- Advancing Canada’s interests abroad;
- Ottawa’s regulation of foreign investment; and
- How to fix Canadian health care.

# Macdonald-Laurier Institute Publications



Winner of the Sir Antony Fisher International Memorial Award BEST THINK TANK BOOK IN 2011, as awarded by the Atlas Economic Research Foundation.

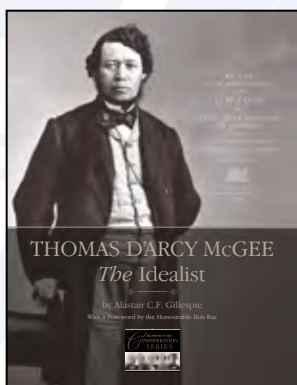
**The Canadian Century**  
By Brian Lee Crowley,  
Jason Clemens, and Niels Veldhuis

Do you want to be first to hear about new policy initiatives? Get the inside scoop on upcoming events? Visit our website [www.MacdonaldLaurier.ca](http://www.MacdonaldLaurier.ca) and sign up for our newsletter.

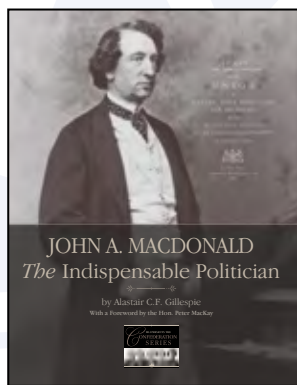
## RESEARCH PAPERS



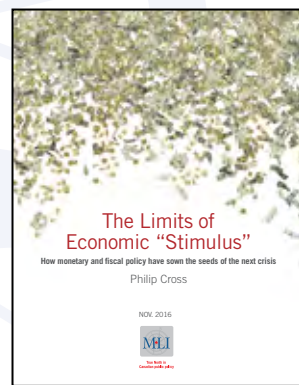
**Smoking Gun**  
Christian Leuprecht



**Thomas D'arcy Mcgee: The Idealist**  
Alastair C.F. Gillespie



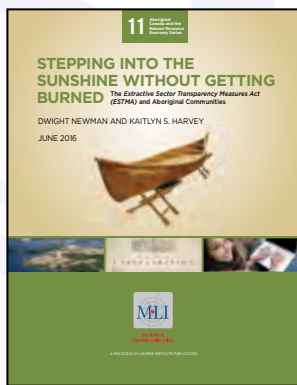
**John A. Macdonald: The Indispensable Politician**  
Alastair C.F. Gillespie



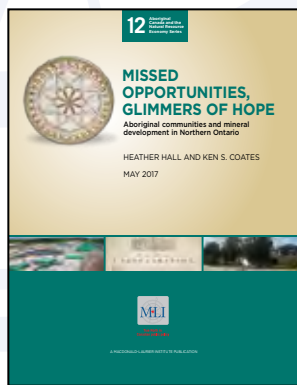
**The Limits of Economic "Stimulus"**  
Philip Cross



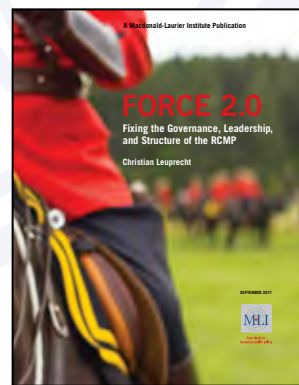
**Getting the Big Picture**  
Bram Noble



**Stepping Into the Sunshine Without Getting Burned**  
Dwight Newman and Kaitlyn S. Harvey



**Missed Opportunities, Glimmers of Hope**  
Heather Hall and Ken S. Coates



**Force 2.0**  
Christian Leuprecht



True North in  
Canadian public policy

---

**CONTACT US:** Macdonald-Laurier Institute  
323 Chapel Street, Suite #300  
Ottawa, Ontario, Canada  
K1N 7Z2

**TELEPHONE:** (613) 482-8327

**WEBSITE:** [www.MacdonaldLaurier.ca](http://www.MacdonaldLaurier.ca)

**CONNECT  
WITH US:**



@MLInstitute



[www.facebook.com/  
MacdonaldLaurierInstitute](http://www.facebook.com/MacdonaldLaurierInstitute)



[www.youtube.com/  
MLInstitute](http://www.youtube.com/MLInstitute)

---

## What people are saying about the Macdonald-Laurier Institute

---

*In five short years, the institute has established itself as a steady source of high-quality research and thoughtful policy analysis here in our nation's capital. Inspired by Canada's deep-rooted intellectual tradition of ordered liberty – as exemplified by Macdonald and Laurier – the institute is making unique contributions to federal public policy and discourse. Please accept my best wishes for a memorable anniversary celebration and continued success.*

THE RIGHT HONOURABLE STEPHEN HARPER

---

*The Macdonald-Laurier Institute is an important source of fact and opinion for so many, including me. Everything they tackle is accomplished in great depth and furthers the public policy debate in Canada. Happy Anniversary, this is but the beginning.*

THE RIGHT HONOURABLE PAUL MARTIN

---

*In its mere five years of existence, the Macdonald-Laurier Institute, under the erudite Brian Lee Crowley's vibrant leadership, has, through its various publications and public events, forged a reputation for brilliance and originality in areas of vital concern to Canadians: from all aspects of the economy to health care reform, aboriginal affairs, justice, and national security.*

BARBARA KAY, NATIONAL POST COLUMNIST

---

*Intelligent and informed debate contributes to a stronger, healthier and more competitive Canadian society. In five short years the Macdonald-Laurier Institute has emerged as a significant and respected voice in the shaping of public policy. On a wide range of issues important to our country's future, Brian Lee Crowley and his team are making a difference.*

JOHN MANLEY, CEO COUNCIL

---