Budget challenges for the next government

8/12/2021

This background briefing has been prepared by the Australian Council of Social Service.

The next government will struggle to close serious gaps in services, payments and programs with the revenue available

Budget expenditures have grown over the last four decades to meet our expectations of improved payments and services

For decades, Australian governments have attempted to fund European-standard services and income supports with American taxes.

In some ways, social expenditure in Australia is very cost-effective. For example, our social security system pays people according to their present needs rather than their previous wages. Yet our system of 'low-cost government' has failed us in the many ways discussed in the Statement, leaving unsustainable gaps between community needs and expectations and government capacity and investment.

Over the past 40 years, successive governments have played catch-up:

- Commonwealth budget expenditures rose by an average of 2.9% a year per person, after inflation.[i]
- Over this period, Medicare was introduced, pensions (but not unemployment payments) were linked to wage increases so living standards kept pace with the wider community, and the National Disability Insurance Scheme was introduced.

This is consistent with trends in other wealthy nations:

> *"Stopping further growth of government over the coming decades will be close to impossible. The most important debates to come will be about the state's nature, not its size." (The Economist, 20 November 2021)*[ii]

As people become wealthier, they expect better health, education and income support and modern public infrastructure. As the populations of wealthy nations age, we sensibly devote more resources to health and care services.

Austerity policies tried to reverse this, causing social harm

In the years leading up to the pandemic, progress on improving our services and safety nets was blocked by austerity policies. In 2014, we had to fend off harsh budget cuts including denying young people income support, cutting pensions, and co-payments for doctor's visits:

- From 2010 to 2018, real growth in Commonwealth expenditure per person fell to just 0.2% a year, well below historical average levels.

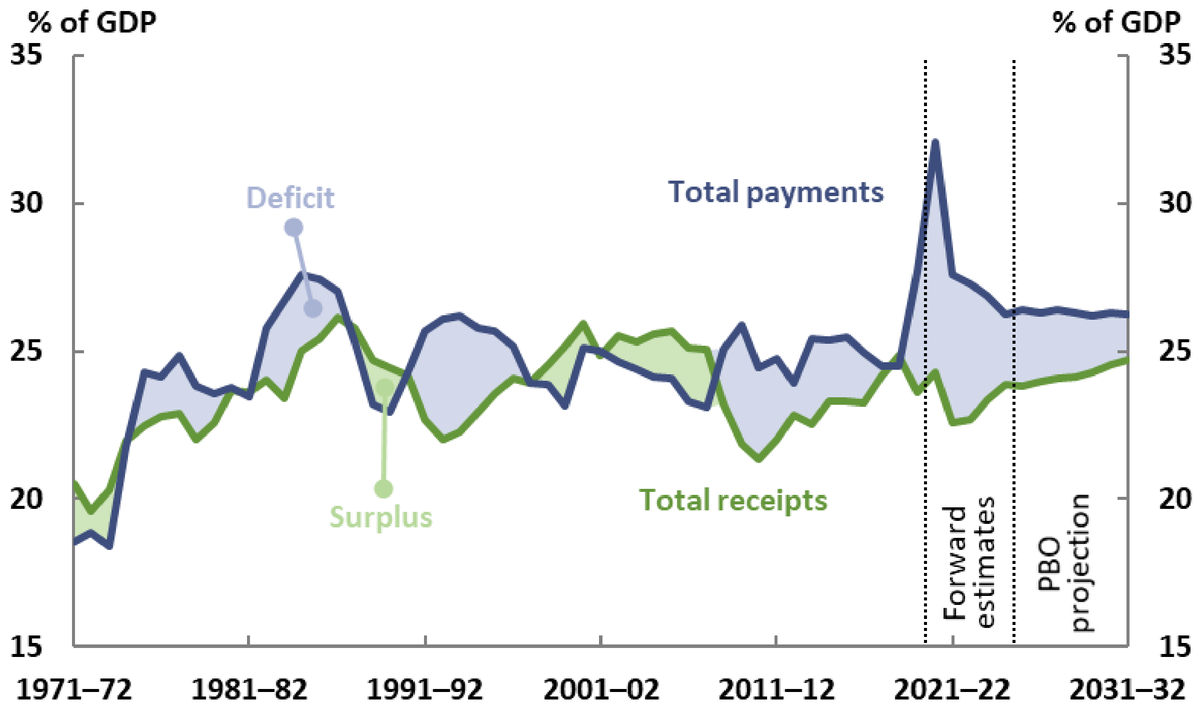
Ph (02) 9310 6200 E: info@acoss.org.au
www.acoss.org.au
ISSN: 1326 7124

Austerity policies were put on hold when the pandemic struck

The Government sensibly halted austerity policies in the face of the pandemic and the deepest recession in a century. Along with governments across the world, it recognised that a quick return to budget surplus is neither possible nor desirable, if we want the recovery in jobs and incomes to endure (see graph below). Lower interest rates mean that the annual cost of financing the budget deficit is no greater than it was in the past.

Figure 1: A quick return to Budget surplus would be foolhardy

Commonwealth Budget expenditure and revenue as a % of GDP



Source: Parliamentary Budget Office (2021), Beyond the Budget - 2021-22: Fiscal outlook and scenarios, Report No 2/2021.

Beneath the temporary boost to public expenditure in the recession, stringent curbs remain in place.

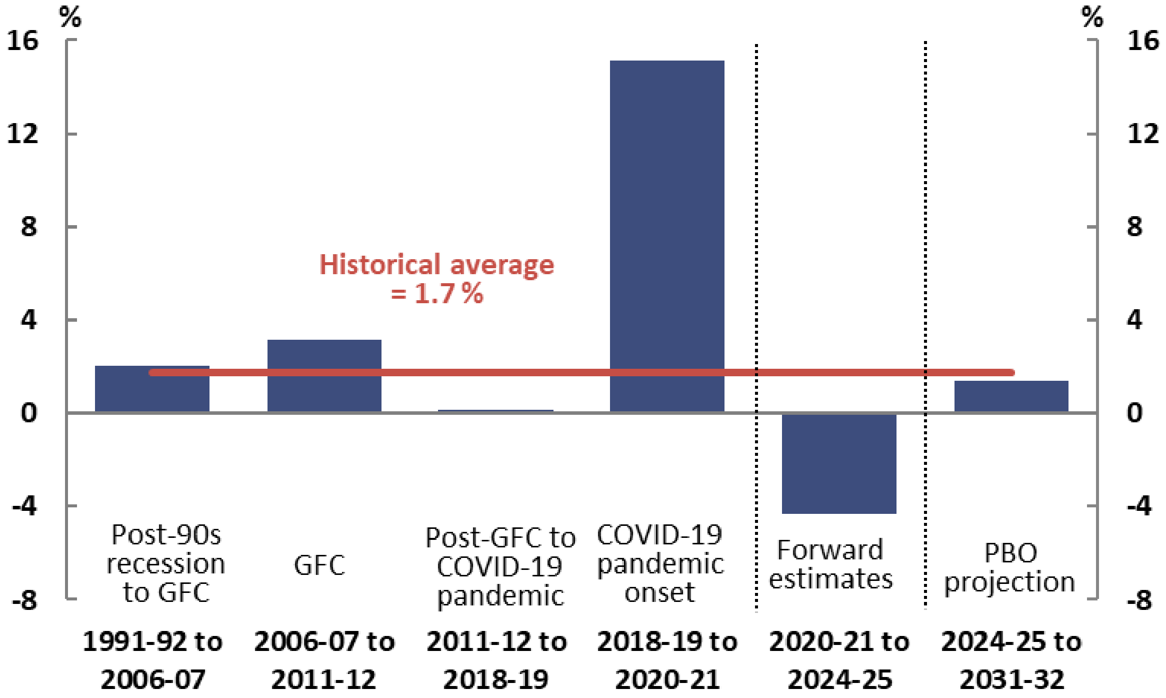
Yet the Government remains committed to the stringent curbs imposed before the pandemic, for example by not properly indexing most social security payments and funding for essential community services. It gives priority to income tax cuts (now backed by the Opposition) and an arbitrary cap on tax revenue of 23.9% of Gross Domestic Product.

If the present Commonwealth budget settings remain in place, they will deprive future governments of the resources they will need:

- The 2021 Budget Papers estimate that real growth in Commonwealth expenditure per person will f*all by an average of 0.7% per year from 2022 to 2024,* when major tax cuts commence (see graph below).

Figure 2: Overall budget expenditures are set to decline

Average annual growth in Commonwealth budget expenditures per person, after inflation.



Note: Long run average calculated over 1991-92 to 2018-19. The average including the onset of COVID-19 and associated policy response in 2019-20 and 2020-21 would increase to 2.6 per cent. GFC refers to the global financial crisis.
Source: 2021-22 Budget and PBO analysis.

Source: Parliamentary Budget Office (2021), Beyond the Budget - 2021-22: Fiscal outlook and scenarios, Report No 2/2021.

Under current budget settings, expenditure on many essential payments and services will fall over the next decade.

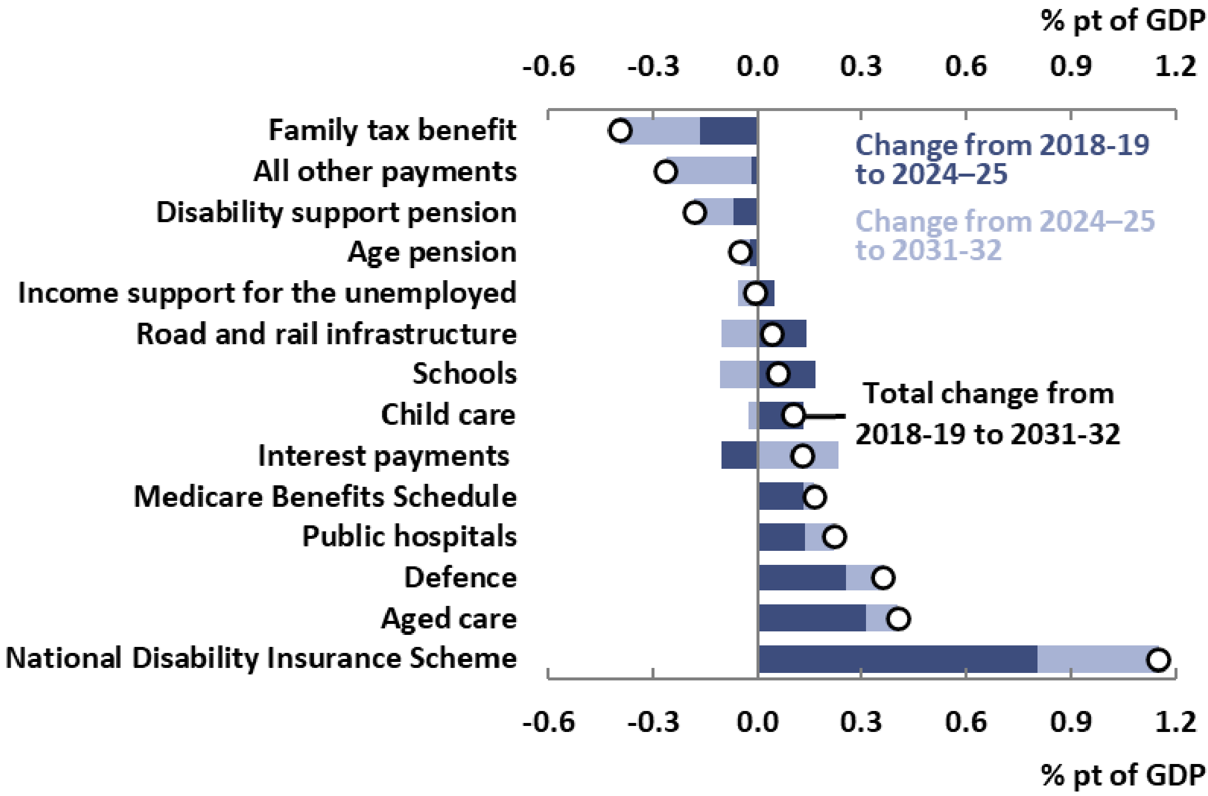
The Parliamentary Budget Office (PBO) warns in its recent report on budget projections to 2030 that *"Australians' expectations about the volume and quality of services provided by government mean greater risks that [public expenditures] will be higher".*[iii]

That report shows that public expenditure is projected to decline as a proportion of GDP over the next decade in areas such as unemployment and family payments, child care and schools (see graph below). In some areas where governments have committed to address unmet needs, such as the NDIS and aged care, spending is projected to rise, though much less so beyond 2024 when the large tax cuts commence. There is no sign of new investment in badly neglected areas such as social housing or dental and mental health.

Essential community services such as aged care and child care face challenges to recruit and maintain the skilled workforce and volunteers they need within the budgets available to them. This will impact the quality of services for years to come.

Figure 3: Most payments and services will see little or no growth

Projected change in Commonwealth budget expenditures as a % of GDP (2018-2031)



Note: 'All other payments' includes the total of all payments programs not separately identified in this chart.
Source: 2021-22 Budget and PBO analysis.

Source: Parliamentary Budget Office (2021), Beyond the Budget - 2021-22: Fiscal outlook and scenarios, Report No 2/2021.

Basic facts on tax and public expenditure in Australia:

- Australia is one of the wealthiest countries in the world, measured by median household wealth.[iv]
- Australia is the sixth lowest in social expenditure and ninth lowest in overall public revenue among the 36 OECD nations.[v]
- Australia's personal income tax revenue (at 11.5% of GDP in 2017) is lower than the average for wealthy nations (17.4% of GDP) when we take account of social insurance taxes.
- An average fulltime worker pays 24.1% of their overall income in income tax, lower than an average American worker (24.4%)
- The Stage 3 tax cuts cost at least $16 billion a year. Recent analysis from the Parliamentary Budget Office indicates that around two thirds of this will go to individuals on $120,000 or more, and only one third will go women.[vi] – PBO (2021), *'Distributional analysis of the Stage 3 tax cuts'*
- The 2021 Budget projects negative growth in Commonwealth budget expenditures per person, of minus 0.7% per year from 2022 to 2024.

[i] Frydenberg J (2021), *Intergenerational Report 2021*.

[ii] The Economist, *Governments are not going to stop getting bigger*. (20 November 2021).

[iii] Parliamentary Budget Office (2021), *Beyond the Budget - 2021-22: Fiscal outlook and scenarios,* Report No 2/2021.

[iv] Credit Suisse (2021), *Global wealth report 2021*.

[v] OECD, *Revenue statistics* and *Taxing wages*.

[vi] Frydenberg J (2021), *Commonwealth Budget Paper No 1* (2021-22).