Economists' Statement on Commonwealth Budgetary and Economic Priorities

September 2014

The austere measures contained in the proposed Commonwealth budget have been justified by fears that Australia's public debt is expanding rapidly and dangerously, and must be arrested through a dramatic change in fiscal policy. These fears are misplaced.

Australia does not face any present or imminent debt crisis. Australia's deficit and accumulated debt are both low, relative to international experience and Australia's own history. According to the Organization for Economic Cooperation and Development, the current net debt (for all levels of government) in Australia is equivalent to 13.8 percent of GDP – less than one-fifth the average debt burden carried by other industrial economies (and an even smaller fraction of the debt in countries like the U.S., the U.K., and Japan). Since the GFC, debt has grown less rapidly here than in other countries. Interest rates paid on Australian debt are at record-low levels (and likely to stay that way for years), further reducing the burden of net interest payments. In short, Australia's ability to manage public debt is very strong.

The major cause of the current gap between revenues and expenditures of the Commonwealth government is continued cyclical weakness in macroeconomic performance. The employment rate has declined markedly, and continues to decline in the face of recent lay-offs and weak job-creation. Incomes have been growing at their slowest pace in decades (consequently constraining consumer spending). These trends, combined with large tax cuts during the early stages of the mining boom, have undermined tax revenues from personal income taxes, corporate income taxes, and the GST.

The most effective route to restored fiscal balance is to help more Australians find work, earn incomes, and pay taxes. But major and unnecessary reductions in government program spending and public sector employment would have the opposite effect.

The goal of fiscal policy is not simply to eliminate the deficit as quickly as possible, nor is it to generate surpluses (government is not, after all, a "profit-making business"). The timing and method of deficit reduction must be balanced with other economic and social goals, including job-creation, infrastructure needs, and social conditions. Governments' economic responsibility is to establish policies which support Australian firms, workers, and communities to utilise their full potential to work, produce, generate income, and sustainably consume.

When spending and demand conditions in the private sector of the economy are sub-optimal (as they have been, and continue to be), government has a responsibility to play a leading role in supporting economic activity and job-creation. At times, this responsibility requires deficit financing of public programs and infrastructure investments.

There are many projects and priorities which would enhance Australia's productive capacity in the future, and hence are deserving of more government support, not less. These include investments in transportation, energy conservation and alternative energy, and affordable housing. When a new public investment project enhances the economy's long-run productive potential, it is economically prudent to finance it with public debt (just as private firms and households finance long-lived investments with their own debt).

The true goal of fiscal policy is the need to ultimately stabilise the level economic activity at full employment. We should not be satisfied until unemployment is back to rates Australia enjoyed in the early post war decades. Debt and deficits should not be targets in their own right but simply treated as by-products of the required fiscal strategy.

International agencies (such as the International Monetary Fund and the G-20) have urged extreme caution in future fiscal retrenchment, for fear that indiscriminate spending reductions will undermine growth and job-creation – ultimately defeating the goal of fiscal balance. They have acknowledged that past polices of austerity in other countries have had large negative effects on growth and employment.

Australia should not make the same mistake. Major spending reductions by the Commonwealth government are economically unnecessary and socially damaging. The first priority of Australian fiscal policy should be to strengthen investment, employment, and growth. Government can and should pursue this priority without jeopardizing its long-run fiscal strength and stability.

Signed,

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