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Priorities for an incoming Government

Some thoughts

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Priorities for an incoming Government: Some thoughts

Key points

This note discusses the economic situation the incoming Government faces, highlights the need for fiscal repair and proposes a possible mechanism to build community support for this.

The economic context

Over the past 25 years, Australia has outperformed most other OECD economies. During that time, we avoided recession and weathered a series of external shocks (most recently the global financial crisis). Living standards have grown strongly both absolutely and compared to our peers.

But we now face a number of short and longer-term difficulties. The RBA has recently cut the cash rate to a historic low, underlining its concerns about economic weakness and persistently low inflation. A prolonged period of below par growth cannot be ruled out. Indeed, real income growth in recent years has been negligible[1].

Our fiscal position has deteriorated. Federal spending, which spiked during the 2008 crisis, remains at elevated levels. The hoped-for revenue rebound has repeatedly failed to materialise, resulting in a series of deficits and rapidly rising public debt, albeit from a low base. At the same time, Australia's multifactor productivity performance has been flat, undermining our capacity to meet future challenges.

On 7 July, Standard and Poor's lowered its credit rating outlook for Australia from stable to negative, reflecting its view that 'without the implementation of more forceful fiscal policy decisions, material budget deficits may persist for several years with little improvement'.[2] Other major credit rating agencies have expressed similar concerns.

The strategic decision: A spending-led approach to budget repair

If we assume (as the 2016-17 Budget does) that a recovery in economic activity (and therefore prices and wages growth) is just around the corner, stronger revenues can do most of the work of budget repair. The Budget projects a small surplus being achieved in 2020-21. While this revenue surge might happen, prudence, not to mention the implied view of central bankers, suggests we should not count on it.

Indeed, at times of heightened uncertainty, budgeting should have a cautious, rather than an optimistic, bias. A cautious approach would highlight the need to take action, within the forward estimates, rather than wait for things to get better. A credible timetable for repair cannot be as long as ten years. This is the clear message the credit rating agencies are sending us.

If a revenue rebound cannot be relied upon, current spending plans need to be re-thought. As Paul Keating pointed out in February, 'the rest of the world has trimmed us down', so 'the penny ought to drop that what we should be doing is cutting spending'[3].

These spending plans, which include initiatives on health and education funding, disability services, defence and income support payments, were conceived in budgetary and economic circumstances which no longer apply. This reality is yet to be squarely faced and explained to the public, as evidenced by the election campaign.

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[1] Real net national disposable income, which adjusts GDP for changes in our terms of trade, has been flat or slightly negative since 2012. In the year to March 2016, it fell by 1.1 per cent while real GDP rose by 3.2 per cent. Source: ABS, *National Accounts*, March 2016.

[2] Standard and Poor's press statement, 7 July 2016.

[3] 2GB radio interview, February 2016.

While tax changes can contribute to needed consolidation, their role should be a supporting one. A policy case can be made for action in several areas, including capital gains, superannuation concessions and even negative gearing. While some additional revenue could be raised in this way, it would fall well short of what is required. Moreover, bracket creep, the *de facto* fiscal repair tool of choice, can no longer be relied on.

Building community and political support for needed budgetary repair

We think that the Government's rhetoric on budget repair needs to be accompanied by specific action, going well beyond budget 'business-as-usual'. Public attitudes on government spending do not reflect the current budget reality.

Our first suggestion is that a more cautious fiscal baseline be established. The assumption, employed in a string of budgets, of a revenue surge (starting in the second half of the forward estimates), needs to be dropped or deferred. This would be a better risk management strategy, given global economic uncertainties. It would highlight the need for spending plans to be tackled and help prepare the community for this challenge. An optimistic revenue-rebound scenario, if anything, undermines this message.

Our second suggestion is that the Government consider an arm's-length, comprehensive federal spending review. This is not a proposal for a secretive, narrowly-focused audit. The review panel should include representatives from community groups (supported by a secretariat from Treasury and Finance), hold public hearings, examine all spending areas and report by the end of the year. This process could be run by the Productivity Commission, given its inquiry experience and reputation, or be stand-alone. The panel's recommendations would be considered in the normal Budget process.

We are not naïve about this suggestion. The election result has made the politics of fiscal repair more difficult than ever. The electorate has not appreciated the need for fiscal repair and political parties have avoided the topic. No external review process can lessen the political pain of budget repair. A credible and transparent panel, however, would at the very least raise public and wider political awareness of the need for action. Recent budgets have conspicuously failed in this regard.

A final word on structural reform

In their PEFO statement, the Secretaries of Treasury and Finance said that structural reform must be pursued with renewed vigour given its importance for productivity. A more productive economy raises living standards, but also enables medium-term fiscal pressures (ageing and health care costs) to be dealt with.

The reforms of the 1980s and 90s opened key markets to competition, benefitting consumers, but also spurred innovation and productivity. Crucially, they dismantled arrangements which locked resources into inefficient and unproductive uses, equipping the economy to seize opportunities and respond to shocks.

In our current politics, some are arguing for a retreat from hard-won reforms. Protectionism, erodes competitiveness, lowers living standards and eventually weakens employment in protected sectors. It is a discredited doctrine, regardless of how it is dressed up. Structural reform can be pursued incrementally, avoiding disruptive big-bang changes. But if it is not backed by compelling political advocacy, it will not win public support. Slogans and appeals to modelling results should not be relied upon.

Background

This briefing note discusses the economic difficulties the incoming Federal Government will face, poses some strategic choices and offers constructive suggestions for action.

It adopts a different approach to similar documents issued by other organisations. These set out extensive policy shopping lists, with many topics receiving attention. This is not realistic, given the constraints policy-makers face: political, constitutional, budgetary and external. The election result will make effective governing more difficult. An effective administration must be selective and disciplined in what it does. For every priority embraced and pursued, other calls on government attention must be jettisoned or deferred. The policy wish-lists issued by think-tanks and lobby groups often fail to recognise this.

The first section of this note outlines the economic and fiscal context. We then discuss the key strategic choice confronting the Government: can a case be made for a new approach to fiscal repair, focussing more sharply on spending adjustment? In the final section, we offer a suggestion on how community support for this might be fostered.

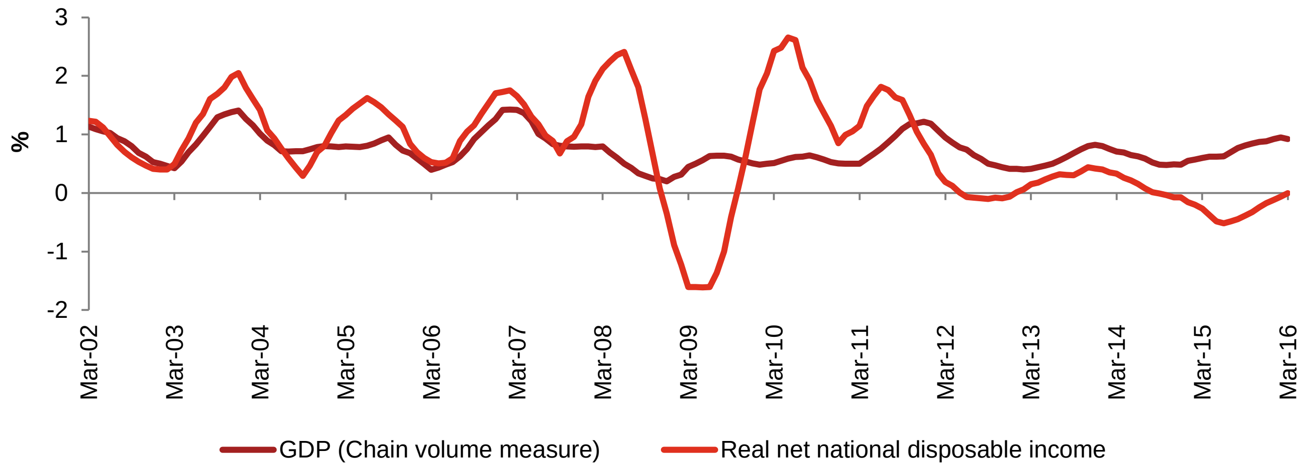
Economic and fiscal context

The broad outlines of this context are well-known. Over the past 25 years, Australia has outperformed most other OECD economies. During that time, we have avoided a recession, weathering a series of external shocks (most recently the global financial crisis) well. Living standards have grown strongly both absolutely and compared to our peers. The benefits of this prosperity have been widely shared, in contrast to what we've seen in other countries. The economy, while retaining its traditional resource strengths, has been transformed. It is more market-oriented, flexible and open than it ever has been.

Both luck and good management have played roles in this story. The economic reforms of the 1980s and 90s coincided with, and enabled us to profit from, China's economic emergence, a resources boom and historically high terms of trade, once-in-a-century technological breakthroughs and the substantial deepening of global capital markets. These external developments may appear inevitable in retrospect, but they were not foreseen at the start of our reform period.

An uncertain and vulnerable economic outlook

But we face a number of short and longer term difficulties. While the economy has adjusted reasonably well to the end of resource investment boom and unemployment remains low, growth has been modest at best. [4] Real net national income, which adjusts GDP for our terms of trade, has been flat since 2012, falling by 1.1 per cent in the year to March.



Source: ABS

The legacy of the 2008 global financial crisis, the weak global economic outlook, and clear signs of vulnerability in China have damaged consumer and investor sentiment. The RBA, in common with other central banks, has cut its interest rate to new lows, underlining its concerns about growth and persistently low inflation. It would have preferred to save its ammunition for a possible global shock, but it felt it had no choice but to act. Economists disagree on the causes, but an extended period of below-par growth looks increasingly likely.[5]

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4 The economy grew by 2.2 per cent (year on year) in 2014-15, with the 2016-17 Budget forecasting 2 ½ per cent growth in 2015-16 and 2016-17 and 3 per cent in the following year. This is barely enough growth to close our output gap (or spare capacity in the economy). The risks, moreover, are likely to be skewed to the downside. The Budget forecasts a strong recovery in nominal GDP growth, from 1.6 per cent in 2014-15, to 2 ½ per cent, 4 ¼ per cent and 5 per cent in the following three years.

5 In a speech delivered in New York in April 2016, RBA Governor Glenn Stevens discusses this prospect. While he rejects the idea of secular stagnation (a world of excess desired savings, zero interest rates and low growth) he accepts that trend growth rates might have fallen. 'If trend growth is lower', he points out, 'and we can't or won't do anything about that, then expectations about future incomes [and] tax bases ... will have to be reconfigured.'

A weakening budget position

Our fiscal circumstances have deteriorated. Federal government spending, which reached historical highs during the 2008-9 economic crisis, remains at elevated levels. [6] Substantial financial commitments on pensions, disability payments and funding for education and health remain on the books. Meanwhile, the expected revenue rebound has repeatedly failed to materialise, resulting in close to a decade of deficits and rising public debt (from a low base).

This is a direct result of the changed economic circumstances we face: the disappearance of the income boost from higher commodity prices, a stalling and lacklustre global economy and minimal growth in local wages and prices. While the 2016-17 Budget foreshadows a gradual return to surplus, as the Secretaries of the Treasury and Finance have pointed out (in the Pre-election Economic and Fiscal Outlook, PEFO), this rests on benign assumptions. In particular, that the long hoped-for revenue rebound materialises. Should this not occur, we would be exposed.

All three major international credit rating agencies have recently expressed concern about Australia's budgetary position. On 7 July, Standard and Poor's (S&P) announced that it had revised its Australia's debt outlook from stable to negative, suggesting that our current AAA rating is under threat. S&P's statement was blunt: 'Without the implementation of more forceful fiscal policy decisions, material government budget deficits may persist for several years with little improvement'. It drew attention to our poor recent budgetary track-record, noting that the Government's projected date for a return to surplus (2021) 'is now eight years later than the previous Government's earlier [target] of fiscal year 2013'. A ratings downgrade could increase the Government's borrowing costs, adding to our current interest bill, and adversely affect our banks' access to international funding, with implications for domestic borrowers. That said, global interest rates are at historically low levels, reflecting investors' strong demand for bonds. And in light of S&P's decision, investors have shown little concern (reflected in the 10 year rate on government bonds and the exchange rate). But as S&P have pointed out, Australia's fiscal position needs to be stronger than other highly rated countries because of our high level of external debt (public and private) and large current account deficit (nearly five per cent of GDP).

Glenn Stevens, speaking in February 2015, warned that the budget deficit could more than double to almost $100bn in a serious economic downturn. In these circumstances, our already rapidly-growing debt would accelerate. If this happened, Stevens added, financial markets would afford the government 'much less discretion'. While funding costs were currently low, investor sentiment can change quickly.[7] His firm advice was to repair the budget sooner rather than later.

International experience shows that when investor confidence is lost, governments have no choice but to adopt harsh short-term austerity measures. These hurt the most vulnerable in the community who rely most on government transfers, destabilise politics further and weaken domestic economies. While a credit rating downgrade would not necessarily trigger such an event, it would make us more vulnerable to one. The only insurance available is to take early action on budget repair.

And an apparent slowing in productivity growth

While it is natural to focus on demand, we should not forget the supply side. Australia's productivity performance has deteriorated since the 1990s. To a large extent, this has been a by-product of the resource investment boom (and will be reversed in the production phase). But it may also reflect a fading of the economic dividend from the structural reforms of earlier decades. It is a truism that in a world of weaker commodity prices, current living standards cannot be sustained without a lift in our productivity performance. With a more productive economy, we will be better able to respond to emerging fiscal pressures, including population ageing.

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[6] Government payments are budgeted to be 25.8 per cent of GDP this year. They will still be over 25 per cent in 2019-2020. In the last Howard Government Budget, spending was at 23.1 per cent of GDP.

[7] Testimony to the House of Representatives Economics Committee, reported in the Australian Financial *Review*, *Fix budget now before crisis hits, urges RBA's Glenn Stevens*, Jacob Greber and Max Mason, 13 February 2015.

A strategic response

The budgetary risks we face stem from our failure to adjust to changed economic circumstances. We have suffered a reduction in national income (in absolute terms and relative to pre-crisis projections), but cling to pre-crisis beliefs. If, as is assumed, revenue growth can do most of the work of budget repair, the spending task is to hold the line. If we wait, the rewards will come. Every Budget since the global financial crisis has counted on this. This scenario might be realised, but prudence (not to mention the implied view of central bankers around the world) would suggest that we not count on it.

The 2016-17 Budget forecasts a deficit of 2.2 per cent of GDP ($37.1bn) this year and 1.4 per cent in 2017-18. In the ensuing two years, which are projections rather than forecasts, the deficit falls further (to only 0.3 per cent in 2019-20). This budget improvement is not achieved by policy decisions, which only improve the bottom line by $1.7bn (or less than $1 in every $1000 to be spent over this period) over this four year period. Tax receipts are assumed to rise from 22.2 per cent to 23.5 per cent of GDP over the forward estimates, largely due to bracket creep. This optimistic scenario relies on an assumed acceleration in nominal GDP growth, which reaches 5 per cent in 2017-18 (from 1.6 per cent in 2014-15) and continues to expand at that rate. Similar assumptions have been made in a succession of post-GFC budgets.

A case for a cautious budget bias

During times of heightened uncertainty, which we undoubtedly face today, budgeting should have a more cautious bias. At the very least, we should not discount the possibility of a prolonged low growth, low inflation period, which many central bankers fear.

A prudent fiscal stance requires that we not wait for revenues to recover, but take action. If we accept that, the question is: how do we adjust. Do we raise taxes, cut spending or a combination of both?

How to achieve budgetary repair?

We argue that the focus must be on spending restraint. Spending, in our view, must be modestly yet clearly scaled back over the next four years.[8] The main share of required budget repair must come from this quarter. In other words, the strategy of holding the line on spending, reflected in the 2016-17 Budget, needs to be reconsidered. Longer consolidation timeframes (of up to 10 years) cannot be relied upon. The IMF, and others, warn against these, arguing that they lack credibility (given shorter political cycles), can easily be derailed and foster fatigue in the public.

We do not underestimate the political difficulties this presents. Proposed spending reductions are fiercely opposed by affected groups, political representatives and commentators. The recent federal election demonstrates that the public does not appreciate the dangers our budgetary position entails. Some Keynesian economists worry about adverse effects on demand. We base our support for spending-led budget repair on the following points.

The case for a spending-led approach

First, it is common sense that if windfall revenues have disappeared (and there are little grounds to expect a revenue recovery) spending should be pared back.[9] Current spending commitments, which include initiatives on health and education funding, disability services, defence and income support payments, may be worthy in their own right, but are now not affordable. They were conceived in budget and economic circumstances which no longer apply. This reality is yet to be squarely faced and explained to the public.

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8 Paul Keating has said the Hawke Government cut spending by 6 per cent of GDP between 1985 and 1990 (2GB radio Interview, February 2016). While the relative contributions of economic growth and deliberate spending restraint can be hard to disentangle, from 1985-86 to 1989-90 Federal spending as a share of GDP fell from 27.4 per cent to 22.9 per cent. Spending fell in real terms in the three years from 1986-87 to 1988-89. The early Howard-Costello budgets were also disciplined. From 1995-96 to 1999-2000, the spending to GDP ratio fell from 25.6 to 23.2.

9 Paul Keating, speaking on radio in February 2016, put it well. 'The real point is the rest of the world has trimmed us down ... When commonwealth revenue has been so affected, the penny ought to drop that what we should be doing is cutting spending.'

Second, even if revenues were not so weak, experience shows that currently-budgeted program costs will be difficult to contain. This calls for the application of a stringent, multi-year budget envelope to overall government spending. If properly enforced, such an envelope would force the setting of clear priorities, allowing scope for unchanged or even higher funding for some activities, but scaling back the ambitions of others. It would also spur reform at the micro level, including better targeting of mandates, a stronger focus on effectiveness (rather than resource inputs) and public sector innovation and creativity[10].

Third, the alternative to a spending-led strategy, that is to rely mainly on revenues, would be problematic. In the past, bracket creep has been the favoured fiscal repair tool.[11] But if we reject, as our operating assumption, a return-to-normal revenue scenario (which relies, in part, on bracket creep), discretionary tax increases will have to be considered. This approach, while politically tempting, would be costly. Tax-led fiscal adjustments do more economic harm than spending-led ones, according to most international evidence. [12] Besides, there is not much room for manoeuvre on taxes. In their PEFO statement, the Secretaries of Treasury and Finance warn that, without considerable effort to lower spending growth, tax receipts will rise above their pre-crisis average (23.9 per cent).[13]

In recent years, some have argued that tougher tax enforcement, particularly for large companies, would generate substantial additional revenue. The idea of potential revenue bonanza from this source is unrealistic, ignoring the enforcement efforts of governments and our revenue authority (the ATO). But the business community's interventions on tax have sometimes been counterproductive. If arguments for corporate tax relief are not accompanied by an acknowledgment of genuine integrity concerns (related to base erosion and profit shifting or BEPS) and the need for greater tax transparency, public support will not be forthcoming.

But tax can make a supporting contribution

We do not deny that discretionary tax increases can play a role in fiscal repair, but this role should be a supporting one. A policy case can be made for action on a number of areas. The fifty per cent capital gains tax discount (which, in the current low inflation environment is arguably too generous) could be reduced. Both major political parties want to pare back superannuation tax concessions for higher income earners. And while views on the negative gearing tax deduction are divided, targeted action could be taken to address apparent abuses. These measures, if properly designed and calibrated, would improve both efficiency and fairness. Similarly, tougher action on BEPS could well play a role. These initiatives would raise some revenue, although not enough to close the budget gap.

We would caution against excessive reliance on savings taxation initiatives. The savings tax base is relatively small. The superannuation changes announced in the 2016-17 Budget, for example, raise (in net terms) only $3bn across the forward estimates. In 2011-2012, capital gains tax collected from individuals was around $3bn. Savings income is more volatile and harder to forecast than other revenue sources, including wages and consumption. Costings in this area will never have a high degree of reliability.

Some have called for an increase in the Medicare Levy or retention of the Temporary Budget Repair Levy [14], but this would increase our already-high reliance on taxing personal incomes; a key tax system flaw identified by Federal Government's 2015 *Re: think* Tax Reform Discussion Paper. The broader point to make is that piecemeal tax changes, if not guided by a medium-term reform blueprint, could exacerbate current taxation costs and distortions.

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[10] Proposed spending reductions are sometimes identified, in the public's mind, with adverse on-the-ground impacts. Indeed, the opposite can be the case. The Costello and Keating budget consolidations spurred, rather than hindered, public sector efficiency and innovation. Indeed, when budget constraints are relaxed, existing inefficiencies become embedded and worsen over time. Arguably, this is something we saw creep into public sector management during the mining boom.

[11] Bracket creep occurs because the income tax thresholds are not indexed to either inflation or average real wages growth. Income gains, whether nominal or real, result in higher average tax burdens for individuals, raising the Government's income tax to GDP ratio. While bracket creep is regressive, inefficient and lacks transparency, it has proven a remarkably successful revenue raiser in the past, when incomes were growing strongly. In recent years, however, wages growth has been disappointing, limiting the scope for bracket creep to help repair the budget

[12] IMF (2010), *Strategies for Fiscal Consolidation in the post-Crisis World, Box 2.*

[13] The lopsided nature of Australia's tax system is a further problem. Our current tax mix is skewed heavily towards income, a relatively inefficient tax base, and away from consumption, a more efficient one. If a change to the GST's rate and base is ruled out, at least in the short-term, income taxes would have to be raised.

[14] The Medicare Levy is levied at 2 per cent of taxable income for most income earners. The Temporary Budget Repair Levy is 2 per cent of taxable income over $180,000 and is scheduled to end at the end of the current financial year.

What should be done?

We face significant and growing budget and economic risks, yet it is not clear that this message is resonating with the community. Public expectations of government, and the services and payments they can provide, remain unrealistically high. Rhetorical appeals to the importance of living within our means have not cut through. One reason for this is that mixed messages are being sent. The Government's optimistic revenue scenarios detract from its main message: the urgent need for further spending restraint. Our suggestions below are offered for sound policy reasons, but they are also intended to 'shock' the public out of any complacency they might have.

Getting our starting point right: establish a more cautious fiscal baseline

The first priority for the Government must be to establish a more cautious fiscal baseline. This would highlight the vulnerability of our current fiscal position, bring into sharper relief the need for spending reductions and help prepare the community for this challenge.

A more cautious fiscal baseline can be achieved in a variety of ways. A specific provision, or uncertainty buffer, can be built into the budget. While the current budget repair scenario can be retained, a discount factor might be applied to the revenue forecast. Alternatively, Treasury might look at some of its assumptions, in particular the idea that (at the end of the two year forecast period) the economy's output gap is eliminated over five years. This period could be lengthened to seven or even ten years. A third option, and one which has not been employed before, would be to develop alternative revenue scenarios. These would apply following the two year forecast period.

No assumed baseline, whether cautious or optimistic, will necessarily be correct. At a time of heightened uncertainty, it is rational for governments (as well as firms and individuals) to plan for the worst. [15] In part, this is because the risks are not symmetrical. If a pessimistic assumption proves to be incorrect, our fiscal position will be stronger than we planned for. If, however, an optimistic assumption is shown to be wrong, it will be worse, with all the negative consequences that implies.

Above all else, a more cautious fiscal baseline sends a clear signal to the community. It brings into sharp relief our spending problem. It establishes a shared problem definition, focussing political and community attention.

An arm's length, comprehensive public spending review

The Government should consider establishing a comprehensive spending review, undertaken by an arm's length panel but supported by Treasury and Finance officials. This is not a proposal for a secretive audit nor to establish a 'razor gang'. The panel would hold public hearings and seek community views, it would focus on improvements in services as well as savings, and it would then make recommendations on spending priorities, program efficiencies and implementation questions. The panel's work would be an input into the Government's budget process over a sustained period.

Previous governments have succeeded to reducing spending levels without incurring economic damage or losing office. This was achieved by both the Hawke-Keating and Howard-Costello administrations. That said, a case can be made that the politics of this may be more difficult today, as the experience of the 2014 Budget showed.[16]

A question for the Government to consider is setting up a special body to examine, and make recommendations on, how best to rein in spending. This would not be an audit commission. These have been established in the past, most recently in late 2013 by the Abbott Government, but in practice they have had little impact.[17]

As an alternative to an audit, the Government might consider appointing a small panel to develop recommendations on required spending reductions. This has been done with some success overseas, although there is no single template. This body would include representatives of potentially affected sectors (including community representatives), be supported by a secretariat from Treasury and Finance, hold public hearings and report publicly by the end of the year.

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15 The economic literature on decision-making under uncertainty (that is, when specific probabilities cannot be attached to different scenarios) supports this approach.

16 That Budget suffered from a number of substantive and presentational flaws, but that was not the whole story. Key initiatives were blocked by a hostile Senate. Media reporting focussed, perhaps inevitably, on opposition to specific proposals. In the process, the larger picture, the need for urgent fiscal repair, was lost.

17 Audit teams have been viewed as unbalanced, with an over representation of businesspeople. Their work has often lacked transparency, with no hearings where affected groups can plead their case. As a result, the resulting recommendations have failed to garner wide support.

The Government would set the panel a clear global spending target, focussing first on the forward estimates period. The goal would be to help return the Budget to surplus as soon as practicable, consistent with the Government's budget repair strategy but reducing the reliance on an assumed revenue rebound. The panel would make recommendations on relative spending priorities, program effectiveness and efficiency, and implementation questions.

The panel could operate on a stand-alone basis or be run by the Productivity Commission (PC), which has extensive review experience and credibility. While the PC typically examines policy questions from a microeconomic rather than budgetary perspective, it is well placed to advice on how public services can be more efficiently delivered. Specialist commissioners could be seconded to the PC for the review.[18]

We are not naïve about this suggestion. A panel, by itself, is no substitute for determined political leadership. But experience shows, not least in the work of the Productivity Commission, that a credible, transparent review process can play a constructive role. They can help change public attitudes on the need for change. Business-as-usual budgets, at least in recent years, have failed to gain political or community traction. Now is the time for creative thinking. The activities of a panel, including its hearings, would at the very least raise community awareness of the fiscal challenges we face. [19] Governments have struggled to do this in recent years in the face of determined political and stakeholder opposition.

Conclusion

In this note, we make the case for a more urgent approach to budget repair given the economic risks we face. We suggest that the current strategy, which assumes a rebound in revenue, cannot be relied upon. It is an optimistic scenario which has repeatedly failed to materialise, resulting in a string of larger-than-expected deficits. At the political level, it has undercut the message that we need to live within our means.

We argue that fiscal repair must focus on phased spending reductions, with tax increases playing a supporting role. The timeframe should be over the forward estimates rather than a 10 year period. We offer two specific suggestions to the Government: the adoption of a more cautious budget baseline; and an arm's-length, transparent spending review. In the absence of the former, the scale of our budget problem will not be clear. The latter is no silver bullet, but would potentially engage the community and parliament in ways which Budgets, by themselves, have failed to do. There may be better ideas on how foster public support for needed action, but it is clear that the business-as-usual approach will fall short.

A final word is required on structural reform. The living standards Australians enjoy today are a legacy of the economic reforms pursued in the 1980s and 90s. Without a continuation of these efforts, our economic and budgetary prospects will suffer. If a halt is called on reform, our living standards will be lower than they otherwise would be, our capacity to fund needed public services will diminish, and we will be more, not less, exposed to external economic shocks. At this time of heightened uncertainty, protectionism has superficial appeal. But if our history demonstrates one thing, it is that this is a recipe for less, not greater, economic security.

While the prospects for ambitious reform, including to our antiquated tax system, may have receded for the time being, the need for economic leadership remains undiminished.

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[18] The PC is formally independent of government, but would work within terms of reference set by the latter.

[19] By examining all spending proposals, and not a politically-determined subset, it would be seen as even-handed. And by examining particular options in some detail, including teasing out possible risks and hidden costs, it would give the Government some comfort that they could be implemented.

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