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STANDING COMMITTEE ON FINANCE AND PUBLIC
ADMINISTRATION

**Reference: Appropriation (Nation Building and Jobs) Bill (No. 1) 2008-2009; Ap-
propriation (Nation Building and Jobs) Bill (No. 2) 2008-2009; Commonwealth In-
scribed Stock Amendment Bill 2009; Household Stimulus Package Bill 2009; Tax
Bonus for Working Australians (Consequential Amendments) Bill 2009; Tax Bonus
for Working Australians Bill 2009**

THURSDAY, 5 FEBRUARY 2009

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**SENATE STANDING COMMITTEE ON
FINANCE AND PUBLIC ADMINISTRATION**

Thursday, 5 February 2009

Members: Senator Polley (*Chair*), Senator Fifield (*Deputy Chair*) and Senators Cameron, Collins, Hanson-Young, Moore, Parry and Ryan

Participating members: Senators Abetz, Adams, Arbib, Barnett, Bernardi, Birmingham, Bishop, Bilyk, Boswell, Boyce, Brandis, Bob Brown, Carol Brown, Bushby, Cash, Colbeck, Coonan, Cormann, Crossin, Eggleston, Farrell, Feeney, Fielding, Fisher, Forshaw, Furner, Hanson-Young, Heffernan, Humphries, Hurley, Hutchins, Johnston, Joyce, Kroger, Ludlam, Lundy, Ian Macdonald, Marshall, Mason, McEwen, McGauran, McLucas, Milne, Minchin, Nash, O'Brien, Parry, Payne, Ronaldson, Pratt, Scullion, Siewert, Stephens, Sterle, Troeth, Trood, Williams, Wortley and Xenophon

Senators in attendance: Senators Abetz, Arbib, Boswell, Bob Brown, Cameron, Collins, Coonan, Fielding, Fifield, Forshaw, Joyce, Lundy, Milne, Moore, Polley, Pratt, Ryan, Xenophon, Williams

Terms of reference for the inquiry:

To inquire into and report on:

Appropriation (Nation Building and Jobs) Bill (No. 1) 2008-2009; Appropriation (Nation Building and Jobs) Bill (No. 2) 2008-2009; Commonwealth Inscribed Stock Amendment Bill 2009; Household Stimulus Package Bill 2009; Tax Bonus for Working Australians (Consequential Amendments) Bill 2009; Tax Bonus for Working Australians Bill 2009

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Committee met at 5.05 pm**GRIMES, Dr Paul, General Manager, Budget Group, Department of Finance and Deregulation****WATT, Dr Ian, Secretary, Department of Finance and Deregulation****GRUEN, Dr David, Executive Director, Macroeconomic Group, Treasury****HENRY, Dr Ken, Secretary, Treasury****PARKER, Mr David, Executive Director, Revenue Group, Treasury****RAY, Mr Nigel, Executive Director, Fiscal Group, Treasury**

CHAIR (Senator Polley)—Good evening and welcome to everyone. I welcome Dr Henry and representatives from Treasury, and Dr Watt and representatives from the Department of Finance and Deregulation. Information on parliamentary privilege and the protection of witnesses and evidence has been provided to you. As departmental officers you will not be asked to give opinions on matters of policy, although this does not preclude questions asking for explanations of policy or factual questions about when and how policies were adopted.

I invite you to make a short opening presentation. At the conclusion of your remarks I will invite members of the committee to put their questions.

Dr Henry—Thank you, Madam Chair. I have no statement to make at the commencement of these proceedings, other than to say that we are here to assist the committee in any way that we can and we will do our best to provide as much background to the package that is under consideration as we possibly can.

CHAIR—Thank you. I remind senators that obviously there is a lot of interest in this hearing so if we could be succinct with questioning and allow the witnesses to answer we should proceed through to 7.30 pm. Dr Watt, do you want to make an opening statement?

Dr Watt—I do not have an opening statement to make either, as is our normal wont in this committee when it is in its estimates format. We look forward to helping in any way that we can.

CHAIR—Thank you very much. Senator Abetz.

Senator ABETZ—Thank you to the officials for making themselves available at what I understand was relatively short notice. That is appreciated but, if I might say, also necessary. Let us start at the very beginning: who can tell us when work first started on the Updated Economic and Fiscal Outlook and the Nation Building and Jobs Plan? Sorry, I thought that was going to be an easy one to start off with!

Dr Henry—Perhaps I can start this one. I am not sure I can provide an answer with sufficient precision, but I will try. As senators would be aware, we regularly update our forecasts for the macroeconomy. We have regular updates through the course of a year, and this is a practice we have had for some time. We typically provide those updated forecasts to the government in order that the government can prepare budget statements and also Mid-Year Economic and Fiscal Outlook statements, but it has been our practice for a long time to provide governments with updated macroeconomic forecasts during the course of a year. We have a regular forecasting process, typically toward the end of the calendar year, and we did so on this occasion.

Particularly because of the rapidity with which macroeconomic circumstances are changing globally, we have updated our forecasts more recently. We have felt the need to take account of the IMF's updates to its forecasts for the global economy which, as the committee would be aware, have been numerous over the past nine months—that is, since the Australian government brought down its budget. So we have been factoring into our forecasts for the domestic economy changed assessments that the IMF in particular has been making, and we have been providing those updated forecasts to government as well.

This statement, the Updated Economic and Fiscal Outlook, is an update both of our macroeconomic forecasts—so that is part of the statement—and of the fiscal outlook and, of course, it provides the details of the government's macroeconomic package. We have been providing advice to the government on elements of the package for several weeks. I do not know if I can be more specific than that.

Senator ABETZ—Thank you very much for that. I was about to remind you that the question was: when did you first start work on the 'UFO' or UEFO, if I can call it that for short. Would it be fair to say that you started work on UEFO after MYEFO, which came out in early November? So it was after that or substantially after that? I now understand from Dr Henry's answer that it started several weeks ago. Is that right? Did work on UEFO start in 2009, for example?

Dr Watt—Insofar as you are referring to the measures, perhaps I can help.

Senator ABETZ—What I am asking about is the UEFO document.

Dr Watt—As Dr Henry said, the document has two parts: an updated economic and fiscal outlook—that is, economic outlook and budget outlook—and a series of measures. Dr Henry has explained that the economic and fiscal outlook was regularly updated through the course of the second half of 2008. So, in one sense the work on the economic and fiscal outlook never stopped. The work on the measures that are the other part of the document began in 2008 and in early December.

Senator COONAN—When was this work being carried out in relation to the first cash package—the \$10.4 billion stimulus package?

Dr Gruen—That package was announced in early October, and the work that led up to it was in the weeks preceding that.

Senator COONAN—That was for the December quarter.

Dr Gruen—That was for the ESS package, which had the elements of the cash payments starting in early December and the first home owners component as well.

Senator COONAN—We will come back to that.

Senator ABETZ—As I understand it we do not often get a UEFO provided to us, as a result of which I think this is a fair question to ask. I understand that work goes on continually. When was a decision made to provide us with a UEFO?

Dr Henry—Obviously it was a decision taken by the government rather than by officials that there would be a UEFO. It was a government decision that there would be a package of economic stimulatory measures in the early part of this calendar year. Those were both government decisions.

Senator ABETZ—The government would have made that decision and, I assume, then communicated it to Treasury and Finance to produce this document. If we do not know when the government made the decision, when were you informed of that government decision so that you could commence producing this booklet?

Dr Henry—The production of the booklet is one thing. I am not trying to be evasive, Senator—

Senator ABETZ—All right, the contents of the booklet.

Dr Henry—Or that the measures be announced in the context of an updated economic and fiscal outlook; that is also a decision. Without in any way trying to be evasive, obviously government decisions can be announced in many forms. They are not always announced in a major economic and fiscal update document. I cannot recall when the decision was taken to announce the measures in that way—that is, the decision to have an updated economic and fiscal outlook as opposed to, for example, a statement of measures with no macroeconomic and fiscal context. I cannot remember when that decision was taken. It was some weeks ago, but I cannot be more precise.

Senator ABETZ—Can we be agreed that you would have started working, for example, on the National Building and Jobs Plan after the first stimulus package? You would not have worked on it before that?

Dr Henry—I think that is true—

Senator ABETZ—I cannot see the difficulty in providing us with a date.

Dr Henry—The only reason I am hesitating is that it is possible—and I would need to check on this—that some of the measures which have been announced in the Updated Economic and Fiscal Outlook were considered at least at some level in our advice to government even before the October statement. That is possible. As you would understand, in the—

Senator ABETZ—Can I interrupt you there, if I may. The October package was followed by the MYEFO in November, yet you are saying that you started working on this prior to that first stimulus package, which was then followed by the MYEFO.

Dr Henry—No.

Senator ABETZ—I am not following the chain of events.

Dr Henry—Yes, I understand the difficulty. All I was saying was that it is possible that on some of the decisions which the government has taken, obviously decisions they have taken since the first stimulus package, we were tendering advice to government on some of those matters in that earlier period last year.

Senator ABETZ—So, for example, you might have suggested the boom gates measure to them, but it was not adopted in the October package but was translated into this package.

Dr Henry—Yes.

Senator ABETZ—All right. I get the drift now. When did work start on the Nation Building and Jobs Plan? Was it in the calendar year 2009? I am trying to get a handle on what we mean by several weeks ago.

Dr Watt—I think I suggested that work on the measures started in early December.

Senator ABETZ—So that is roughly eight weeks ago.

Dr Watt—Seven or eight weeks.

Senator ABETZ—It is a bit more than several weeks ago.

Senator COONAN—When was a decision made to publish or to base this package with all the macro settings as a UEFO, and would you regard that as a mini-budget, in effect?

Dr Henry—I guess it is not unlike statements that governments in earlier times have made which, whether the government at the time called them mini-budgets or not, have been given that label. I can recall the days when budgets used to be delivered in August. I can recall, for example, a May 1987 statement that was described as a mini-budget. I do not think the government at the time did, but it was described that way in popular discussion.

Senator JOYCE—Obviously we are belting around trying to get one concrete date, so let us try this: at what stage did you refer the assertions in the package off for modelling to check their veracity? What date was that?

Dr Gruen—Senator, I think the best way to think about this is as an ongoing process of discussion, suggestions and papers written, which include estimates based on modelling of the effect of various suggestions, and it is an iterative process.

Senator JOYCE—But you have referred this off for modelling, haven't you?

Dr Gruen—Yes.

Senator JOYCE—And it has been peer-reviewed and come back to you?

Dr Gruen—Sorry; peer-reviewed?

Senator JOYCE—Have you had it peer-reviewed? Did someone else check it?

Dr Gruen—Outside the public sector?

Senator JOYCE—Yes.

Dr Gruen—No.

Senator JOYCE—Has it had an internal peer review?

Dr Gruen—It kind of depends what you mean, in the sense that—again, I am not trying to be evasive—papers are written, they are distributed amongst people with expertise in the area and comments are requested. So you could certainly call that a peer review if you wish.

Senator JOYCE—So it has been peer-reviewed by Treasury—so you are happy with the assertions made in it?

Dr Gruen—If you want to give me a specific example. As a general proposition, the analysis and modelling was done by Treasury and was subject to discussion within Treasury.

Senator JOYCE—I will get back to that later on.

Senator ABETZ—All right. We seem to have had a bit of difficulty in nailing down when it started. Can I try 'when was it finalised'.

Senator BRANDIS—Senator Abetz, before you go on with when it was finalised, can I pursue a question about when it started. Dr Henry, in appendix B to the UEFO, there are 15 measures described. There is one revenue measure and there are 14 expenditure measures. Now, it is the case, isn't it, that various iterations of some of those measures in fact have quite a long history—that various iterations of some of those measures, in particular the 14 spending measures, have been proposed by the spending departments in previous budget rounds, not only to this government but to previous ones? That is what Mr Costello said in the House of Representatives yesterday, incidentally.

Dr Henry—I could not possibly comment on that. As Madam Chair indicated at the start of these proceedings, I am not able to comment on policy advice that may or may not have been provided—

Senator BRANDIS—No, I am not asking about that.

Dr Henry—to the government, and certainly not to former governments.

Senator BRANDIS—I am not asking about policy advice. Senator Abetz has quite properly asked you about time lines, and without any objection from the government senators or the chair you have felt free to respond to him, as you ought to his questions about the time lines for the document in aggregate. I am really just disaggregating the document to ask you about the time lines for specific measures. Let me give you one example—on page 65, under the Nation Building and Jobs Plan, energy efficient homes. This is not the first time, is it, that a proposal along these lines has been considered by government but rejected?

Dr Henry—As I indicated, I cannot possibly answer that sort of question. Obviously, I can answer a question along the following lines: in respect of this particular measure and the decision making of the present government in respect of this particular measure, when might advice have gone to the present government? I think that question is something that I could certainly respond to. But a question which asks whether this particular measure or a measure like this has ever been provided in the way of policy advice from advisers to former governments or to this government at any prior time is not one that I feel that I can answer, because that seeks from me details of policy advice provided to a former government and I do not feel comfortable answering those sorts of questions.

Senator BRANDIS—I do not want to make you uncomfortable, Dr Henry, but you are not in a position, are you, to dispute Mr Costello's statement in the House of Representatives yesterday that some of these measures are old measures that have been, to use his words, 'dusted off' and put forward and adopted now by the new government, which had been rejected by the previous government. Some of these are old measures that have now been dusted off. You do not dispute that, do you?

Dr Henry—I have not seen Mr Costello's statement, I did not see him making the statement and I have not read a transcript of his statement so for that further reason—and it is a further reason—I would not feel comfortable answering that question.

Senator ABETZ—All right. Can I ask when it was finalised.

Dr Henry—I think the best answer to that question is that it went to the printer on Sunday.

Senator ABETZ—When did it come back from the printer?

Dr Henry—Monday.

Senator ABETZ—And did the printer have to work overnight, a bit like HK, or not—you know, 37 hours straight?

Senator CAMERON—Ask me about printers; I know a bit about them.

Dr Henry—I would wish it were otherwise but it is a long time since we have provided a printer with a document that did not require them to work overtime.

Senator ABETZ—I did not hear that.

Dr Henry—I am saying that I really wish it were otherwise but I cannot remember the last time we would have provided a printer with a document, the printing of which required them to—

Senator ABETZ—Work overnight?

Dr Henry—Well, certainly work overtime.

Senator ABETZ—That is fine. I am just asking; just tell me the times and dates we will move on.

Dr Henry—Mr Ray may have something to add to this.

CHAIR—Dr Henry had the call and Mr Ray would like to make a comment.

Mr Ray—I think that the document was printed on Monday. So we need to check whether they actually had to work overtime to print it.

Senator ABETZ—So it was received by the government on Tuesday?

Mr Ray—Certainly, copies were printed on Monday.

Senator ABETZ—And when was the text of the document finalised?

Mr Ray—As Dr Henry said, the document went to the printer to be put into digital proof form on Sunday and I think you can assume that that is when the text was finalised.

Senator ABETZ—So it was only finalised on Sunday. Can we be given an idea as to the hour of the day? Dr Henry, can I ask if you signed off on the document? How does this work? Did you proof read it? Did Mr Ray?

Dr Henry—I did not. It is of course a government document and I do not sign off on such documents as such and nor do I proof read such documents. But we do have processes within the department that check the contents of the documents—the normal thing—and those normal processes I am sure would have been followed on this occasion.

Senator ABETZ—So who undertook that? Providing the advice to make sure that this text would be appropriate to go to the printers? Sure, the final decision to send it to the printer was the government's, but I assume the government sought advice as to the robustness of this document before they sent it off to the printer? I do not want to know what your advice was, just when the last time was that you gave them advice concerning the contents.

Mr Ray—The document would have been checked across the department during the course of its production and the final sign-off of the content would have been made by relevant general managers—that is at division head level—on the Sunday.

Senator ABETZ—And are you willing to share with us whether it was late afternoon Sunday, 11 pm, or—

Mr Ray—We are having the time checked.

Senator ABETZ—Thank you for that. I have a few other quick questions. I do not want a turf warfare starting. Was Treasury or Finance the lead agency in this, or are you a happy marriage of equal partners?

Dr Henry—We are happily married.

Senator ABETZ—Equal partners, which you know a lot about I understand Dr Henry!

Dr Henry—Thank you, Senator. Thank you for reminding me.

Senator ABETZ—Well done on that milestone.

Dr Watt—Happily married for life, Senator.

Senator ABETZ—So the two of you did it together as a joint lead agency, if I can use that phrase?

Dr Watt—I think I can say that Treasury took the lead, we played a second role and agencies were involved in measures as appropriate.

Senator ABETZ—That was going to be my next question: which agencies, departments et cetera were consulted in the development of this package? Do we have a handy list? I do not want this to be a memory test but, for example, was the Australian Rail Track Corporation consulted in any way about boom gates? Was the Defence Housing Authority consulted about the need for the 860 homes? What sort of consultation between the departments took place? I would have thought that the environment department would have been consulted about the efficacy of home insulation as opposed to other environmental measures. I just want to know all the agencies so that when we do drill down into the detail later we can have some idea. Who can give us that list?

Dr Watt—I think I can answer your question. Why don't we go to a convenient table so we can work through it systematically—let's try from page 59 on the measures. The revenue measure I will leave to our Treasury colleagues to answer. The defence housing issue was worked up with the Defence Housing Authority.

Senator ABETZ—So can I ask, for example, when was the Defence Housing Authority consulted about this particular measure? I give you notice now that this is the sort of detail we are seeking. If you do not have it ready now, officials could start getting that sort of information ready for when we go into more detailed analysis.

Dr Watt—The Nation Building and Jobs Plan was discussed with the Department of Education, Employment and Workplace Relations. Similarly, the trade training centres in schools—

Senator ABETZ—All right. Rather than taking time, you are assuring us that each of the measures were discussed with the relevant agency or department?

Dr Watt—Let me just keep turning the pages, Senator, because I cannot.

Senator ABETZ—In that case, rather than having to go through all that again and asking what time you first consulted, I will leave that bracket of questions for later on in the evening so we do not take up too much time. We were promised that the last package, of \$10.4 billion, would create 75,000 jobs. Was there any

modelling to support that assertion that that package would create 75,000—I think the term was—‘additional’ jobs? Was there any modelling or any basis for that assertion being made?

Dr Gruen—The way that one should think about all of these employment effects, whether one is talking about that package or the current package, is relative to what would otherwise have been the case.

Senator ABETZ—With due respect, the language has changed significantly from the last package, which said that 75,000 additional jobs would be created, to now spending four times as much supporting up to 90,000 jobs. So the language between the two packages has changed. With great respect, Dr Gruen, I know how the government might now want us to interpret those figures, but the fact is that the government promised in a very clear statement that \$10.4 billion would create 75,000 additional jobs, and I would have thought that in the natural meaning of language that would mean the creation of additional jobs, not ones that are already there; it would mean the additional creation of new jobs. But the language has now changed and I am wondering what economic factors have come into play—or is it the issue of the political sale of the measures that has come into play? Sorry, I withdraw that last part for you; you should not be asked that.

Dr Gruen—I was going to say that I do not intend to—

Senator ABETZ—I am used to a minister being at the table from time to time as well. I withdraw that.

Dr Gruen—I do not intend to comment on the political question but, if you remember, in the Mid-Year Economic And Fiscal Outlook we made the point that we thought that the \$10.4 billion Economic Security Strategy would help to create jobs relative to what otherwise would have been the case—we can check the exact language—but we also made the point that the—

Senator ABETZ—I can assist you, Dr Gruen, on that very point. And this is from the second reading speech, at the bottom of page 1:

When combined with other measures, this investment means that the Economic Security Strategy is expected to create about 75,000 additional jobs for Australians.

So that is clear language of the second reading speech, to remind you.

Dr Gruen—It is certainly the case that we were in an environment in which we were forecasting, as was clear in the MYEFO, a rise in unemployment at the same time. So we are talking about relative to what would otherwise have been the case.

Senator JOYCE—I have one point for clarification. What is the difference between ‘create’ and ‘support’?

Senator ABETZ—I think a builder would understand the difference between creating a building and supporting a building.

Senator JOYCE—Just let Dr Gruen answer the question. What is the difference between ‘create’ and ‘support’?

Dr Gruen—I do not really want to engage in a semantic discussion about the difference. I am very happy to explain what the basis of the modelling was.

Senator JOYCE—No. I, on behalf of the Australian people, want to know what the difference is between ‘create’ and ‘support’. I really do.

Dr Gruen—Jobs are constantly being created and destroyed in the economy. That happens all the time.

Senator JOYCE—Yes, I know that.

Dr Gruen—There are huge flows of people in and out of the labour market every month. The sense in which the calculations that underpinned the claim that up to 75,000 additional jobs would be created goes to the question of what the employment would be with the stimulus relative to what the employment would be without the stimulus. It does not attempt to identify whether a particular person went from the unemployment queue into employment or whether they stayed in employment. There is no attempt to distinguish between those things.

Senator ABETZ—If the language employed in the first package is so clear, why on earth was the language changed in the second package to ‘support’? If ‘creating’ additional jobs means exactly the same thing as ‘supporting’ them, why wasn’t the same language used in the second package? Can I suggest to you that the government has no new jobs to point to, let alone 75,000 jobs to point to as a result of the stimulus package No. 1.

Dr Gruen—I am not going to comment on specific language in government documents, but I will make the point that we have evidence that the package stimulated consumption. We have strong reason to believe that that would have led to more people being employed than would otherwise have been the case.

Senator BOB BROWN—I want to come to the basis of why we are here, which is the extraordinary economic situation that the nation faces. Could you please tell the committee what economic situation Australia is now in? Six or 12 months ago we were talking about us being in a better situation than the rest of the world. Now it appears the rest of the world is dragging us down with it. Could you tell the committee what the current circumstances are which have led to this package and what the outlook for Australia is in a period in which other countries have dipped into full-on recession?

Dr Henry—I will start and I am sure Dr Gruen will have further to add. At the time that the 2008-09 budget was released the International Monetary Fund was forecasting world growth for 2009 of four per cent. Less than nine months later the IMF is now forecasting world growth of about one half of one percentage point. That is a very substantial deterioration in forecast growth. It is the largest downward revision to forecast growth by the IMF that I can recall. Certainly it would be the largest since the Second World War—Dr Gruen reminds me that, of course, the IMF did not exist before then—so in that sense the global circumstances confronting Australia are simply unprecedented.

There are other respects in which circumstances confronting Australia are unprecedented. The forecast growth for our major trading partners is as weak as we have seen quite possibly since the 1930s. Virtually all of the countries that we regard as our major trading partners, when we talk about our major trading partners in an economic sense, are growing at well below trend rates of growth. Most of them are projected by the IMF to be in recession in 2009. Many of them, indeed, are already in recession and have been for some period of time. It remains the case that, on our assessment and on the assessments of the International Monetary Fund and the OECD, Australia's macroeconomic performance is relatively strong both in respect of actual performance and forecast performance.

Senator COONAN—What is that due to?

Dr Henry—It is due to a whole range of circumstances. It is due to very careful management of the Australian economy over a long period of time with respect to both macro policy and microeconomic reforms in the Australian economy. It is also due to—

Senator COONAN—Good regulation?

Dr Henry—Indeed—effective regulation of our financial system in particular. It is also due, of course, to the considerable benefits that have flown to Australia from the run-up in commodity prices that accelerated at the end of 2003, although commodity prices have fallen back considerably since then, largely as a consequence of the deterioration in growth of our major trading partners, including China. Nevertheless, commodity prices and our forecast commodity prices remain well above levels that were experienced in the first half of this decade. So there are a whole range of reasons why Australia's relative economic performance is still quite good, but in an absolute sense the economic prospects confronting the Australian economy have obviously deteriorated very substantially.

The Updated Economic and Fiscal Outlook produces updated economic forecasts for the Australian economy. For 2008-09 we are now forecasting gross domestic product to grow by one percentage point. The committee would be aware that in 2007-08 real gross domestic product grew by 3¾ percentage points, which is pretty close to our long-run trend growth rate, although maybe 3½ would be a little closer. We are now forecasting one percentage point growth in gross domestic product in 2008-09, and that is even taking into account the very considerable loosening in monetary policy that has occurred, the significant depreciation in the Australian dollar that has occurred, the October macroeconomic stimulus package and, of course, this macroeconomic stimulus package. That forecast takes all of those things into account, all of which are acting to support growth and, certainly, our forecast of growth for 2008-09. So, even after taking all those things into account, we are forecasting growth of one percentage point in 2008-09, which is well below trend growth for the Australian economy and which explains fully why, in our forecasts, we have the unemployment rate increasing.

Going out to 2009-10, we are forecasting even weaker gross domestic product growth of only three-quarters of one percentage point, and again that is after taking into account all of the factors that I mentioned earlier and, indeed, after taking into account a further cut in official cash rates—that is, further monetary policy loosening by the Reserve Bank on top of what was announced on Tuesday. If one compares the outlook for

Australia with the outlook for the rest of the industrialised world, ours is in some respects a pleasing outlook. The rest of the industrialised world taken together is forecast by the International Monetary Fund to go backwards in 2009. But in other respects, and certainly relative to Australia's trend rate of growth, the figures in the UEFO have to be regarded as very weak.

Senator BOB BROWN—The prospect of recession, of course, is one that we have to face, because other countries are already experiencing it. What signals led to the timing and size of this package, and to what degree has this package been shaped to keep our economy's growth in the black?

Dr Henry—To a very considerable extent. I am happy to indicate here that we have put advice to government that, given the macroeconomic circumstances confronting the Australian economy, there was a clear case and there is a clear case for a very substantial fiscal stimulus and for that to be delivered to the Australian economy before unemployment starts to increase. From our history and also from the experience of other countries, the evidence is that the earlier a macroeconomic policy response is taken, the better the prospects for the macroeconomy going forward. Given the macroeconomic circumstances that the Australian economy is confronting, and particularly given the very rapid reduction in forecasts for world growth and for those of our major trading partners, we have been saying to the government that there is a clear need to act now.

Senator BOB BROWN—But why \$42 billion? Why not \$21 billion or \$84 billion? How do you get to the figure of \$42 billion?

Dr Henry—I guess the starting point is to recognise that if one were to look at the forecasts we have in front of us as well as the forecasts we had in front of us—that is, the counterfactual, although he did not use that expression, that Dr Gruen posed earlier: 'What do we think the Australian economy would look like without this package?'—one would observe a very significant gap between forecast growth and trend growth. Whenever growth is forecast to be below trend, the unemployment rate is by definition forecast to increase—that is just a tautology.

Senator JACINTA COLLINS—Could it also prolong the downturn?

Dr Henry—Indeed there is an obvious feedback effect into aggregate demand from rising unemployment. Once unemployment starts to rise, household disposable income falls, household consumption activity falls and business investment falls as well, so aggregate demand is negatively affected. That is a negative feedback loop that macroeconomists used to talk about quite a lot and, in recent times all over the world, have been talking about quite a bit. There is a very substantial gap between where gross domestic product would be if it were to grow at trend and unemployment were not to increase and where we think gross domestic product is going to be. The question, then, is how much of the gap can be closed by monetary policy, both monetary policy action which has been taken to date and possibly future monetary policy action; how much of that gap might be closed by the depreciation of the exchange rate that has occurred to date; and so on. Having made an assessment of all those things, one is left with the question: how much of that gap could reasonably be closed by an expansion of government spending, tax cuts or whatever—by reducing the size of the government's surplus or by increasing the size of a budget deficit?

Senator BOB BROWN—Just on that question, if I may, there is considerable questioning, I can tell you, in parliamentary ranks as well as in the public about how well the cash bonus elements of this package will, in fact, stimulate the economy. From earlier questioning, you will know that, regarding the October package of some \$10 billion, retailers are saying—if I am not wrong—that they think \$1 billion of that may have actually ended up being spent, which raises the question—

Senator JOYCE—Where's the rest?

Senator BOB BROWN—whether it could be the case that five, six, seven, eight or nine billion of that actually went into savings and has not been released into the economy. What confidence do you have that the even bigger component of cash bonus elements that is in this package is actually going to stimulate the economy and not be put into savings by a populace that is increasingly conservative and not out there to shop?

Dr Henry—Let me make some remarks about that. I understand the debate, and Dr Gruen may wish to add to this as well. I guess the first thing to say is that, for retail spending, thus far we have data for one month: December. It has certainly never been our expectation that all of the fiscal stimulus provided as a consequence of the October package would occur in the month of December. That was certainly never our expectation; it is not what we were saying at the time. But the first point to make is that retail sales is the minor proportion of household consumption. If you think of the national accounts aggregates of household consumption,

investment, the government, of course, and net exports, household consumption is, I think, about 60 or 70 per cent of the demand components of gross domestic product—gross domestic product (E), as the statistician refers to it. Of household consumption expenditure, I think retail sales make up about 40 per cent, or something like that, of consumption. So the retail spending figures relate to about 28 per cent of GDP, I suppose—something like that—which is to say that one should expect the fiscal impact of the October package to come through not only in retail sales. That is the first point.

The second point is that some of the stimulatory impact of the October package would be expected to come through in the present quarter and, indeed, subsequent quarters. Why might this be the case? Well, what is saving? Saving is merely deferred consumption.

Senator BOB BROWN—If I may interrupt there: can you just tell me if savings are up?

Dr Henry—We do not know.

Senator BOB BROWN—You do not know?

Dr Henry—No, we do not know. We will get an estimate of what happened to household savings in the December quarter in the first week of March. That is when the statistician will release estimates for the December quarter national accounts. That will be in the first week of March. Those accounts will provide estimates for household saving in the December quarter. Recall, though, that, as I said earlier, the October package would impact only at most three weeks out of the full three months of the December quarter. So we are only going to get by the first week of March a very partial reading of the impact on both household consumption and household saving of the October package. In the first week of June, we will get the March quarter national accounts. That will tell us what has been happening in the present quarter that we are about halfway through.

Senator BOB BROWN—The difficulty is that we cannot revisit this package in June. I would like to know where in the economy you estimate the \$10 to \$20 billion in direct bonuses and stimuli will go.

Dr Henry—We have set that out in this document—only in aggregate, of course. We have indicated in the document what we estimate to be the impact of the package on aggregate demand both in 2008-09 and in 2009-10. This is set out on page 11 of the document. That shows the profile of the fiscal stimulus. That is the profile of the impact on the government budget balance. We also set out at the top of page 17 what we consider will be the impact of that fiscal stimulus on GDP growth. We say:

As a result of the Plan, GDP growth will be around $\frac{1}{2}$ per cent higher in 2008-09 and around $\frac{3}{4}$ to 1 per cent higher in 2009-10.

Senator BOB BROWN—I will change tack a bit. Raising money in the bond market could lead to an increase in the exchange rate as foreign investors purchase Australian dollars to buy the bonds. Tell me if I am wrong about this: a higher Aussie dollar might make it harder for export oriented industries—for example, agriculture—and therefore for jobs in those sectors. As I see it, there is a concentration in this package on the construction and retail industries. What about the impact on the sectors of the economy that do not do so well out of this package? Could the package make it more difficult for them and the maintenance of jobs in those sectors?

Dr Henry—Let me try my hand at this one—Dr Gruen might interrupt me on this occasion! A general view among macroeconomists would be that, if one country acting in isolation were to undertake an expansionary fiscal policy and that country had a freely floating exchange rate, then one of the consequences of that unilateral fiscal expansion would be that its exchange rate would appreciate. Obviously we are not in those circumstances. It is the case that governments around the world are undertaking expansionary fiscal policy. It may well be the case that, were Australia not to undertake an expansionary fiscal policy, our dollar would depreciate even further than it already has. Maybe that would provide some measure of support for some sectors of the economy that would benefit from a depreciating exchange rate, but it would also reduce forecast growth in the Australian economy in 2008-09 by $\frac{1}{2}$ a percentage point and in 2009-10 by $\frac{3}{4}$ to one percentage point. Even taking into account the impact on the exchange rate of the fiscal stimulus, that would be the effect.

To put it another way: in making these forecasts, our modelling would have taken into account, at least to some extent, impacts on the exchange rate of the economic stimulus package that is here. Any economic stimulus package is going to directly benefit some sectors of the economy more than it does others; I suspect that is unavoidable. The same is true of monetary policy, as you know. Not everybody likes to see interest rates fall. Yet I think we all accept that, when the economy weakens, it is desirable that interest rates fall.

Senator BOB BROWN—I presume your modelling takes into account that potential negative impact in both sectors and in the jobs they hold?

Dr Henry—Yes, it does, though whether the modelling is sufficiently disaggregated to identify those effects is another thing. But the modelling implicitly takes those effects into account.

Senator BOB BROWN—I have two more questions I would like to ask briefly if I can.

CHAIR—Then we will go on to Senator Xenophon.

Senator BOB BROWN—Our understanding is that some taxpayers who pay no tax because tax offsets are greater than liabilities will not be eligible for the tax bonus for working Australians. Can you confirm or otherwise whether that is the case and whether it practicably means that some very, very low income earning taxpayers will not get the bonus?

Mr Parker—The tax bonus will be paid to taxpayers who have, in effect, tax liability for the 2007-08 income year. That is a tax liability after the various offsets and credits are taken into account.

Senator BOB BROWN—You are not concerned that this is going to be unfair to some people who are going to miss out from that arrangement of getting a tax bonus that the people next door are getting?

Mr Parker—The question of unfairness is a policy choice and it goes to a policy choice made by the government. I am not sure that my opinion about that is particularly relevant.

Senator BOB BROWN—Do you know, Mr Parker, how many people are going to miss out because they are at that lower level of income?

Mr Parker—Yes, I think we can provide that number. I am not sure whether I have it in front of me. I do not have that number in front of me here. I will ask my colleague to see if he can extract that number and come back to it after dinner for you.

Senator BOB BROWN—I thank the committee but a general question back to you, if I may, Dr Henry: Nicholas Stern, when he was in Australia a year or two ago, said that those economies which are ecologically oriented will be the strongest economies as we go down into this century. Was that taken into account when shaping this package or indeed the last one, and what is Treasury's attitude towards the emerging evidence that the ecological component in technology, manufacturing, food production, tourism and a whole range of industries not only is going to be strong for the economy but is going to be a prodigious export income earner and job creator?

Dr Henry—I do not think that this is a factor that we have taken into account. In fact I am sure it is not a factor that we have taken into account explicitly in our modelling. As I recall the basis of Nicholas's remarks was to the effect that consumer tastes were moving globally in the direction of ecologically sustainable products, both goods and services, that would affect tourism flows over time. I think also he had in mind that governments would be compelled to introduce policies that would, over time, benefit relatively more ecologically sustainable production, if you like, that policy settings would change in a way that provided greater incentive for those sources of growth to emerge. And I think he was suggesting that countries that got ahead of that trend might, both with respect to consumer tastes and with respect to global policy settings, experience relatively stronger growth than otherwise.

Senator BOB BROWN—So is that a factor that the Treasury builds in?

Mr Ray—No, as I said, we have not done any explicit modelling of what the size of that effect might be.

Senator BOB BROWN—Why not?

Mr Ray—In the way that we do our longer-term modelling, with the exception of modelling demographic impacts—which, as you know, we do over a 40-year period to support the *Intergenerational Report*—and with the exception also of the modelling that we did of the government's Carbon Pollution Reduction Scheme, our longer-term modelling tends to be quite crude, frankly. We simply make projections of what we expect the trend rate of GDP growth to be. I would prefer that we had a capacity that allowed us to model these trends more precisely over a longer period of time, but we simply do not have that capability.

Senator BOB BROWN—Thank you. I have more questions, but I will wait for later.

Senator XENOPHON—Perhaps if I could pick up on Senator Brown's questions in relation to modelling, can you tell the committee what kind of modelling was done in relation to this particular package—what approaches were used and over what period?

Dr Gruen—I guess the way to think about it is that the modelling is done in a series of steps. The first step is to make an assessment of what we think is a reasonable estimate of the fiscal multiplier for different sorts of spending. Perhaps I should preface my remarks by saying the modelling is done predominantly at a fairly aggregate level, which is the way that macroeconomists tend to model these things. There is a range of evidence from a variety of sources—the IMF, but lots of other sources as well—that fiscal multipliers are of the order of perhaps half to one. Those are the sorts of estimates. You can actually find broader ranges than that, but that is a reasonable order of magnitude—and I will explain what that means. A multiplier of one means that, if you spend a dollar—sorry, I will preface my remarks again. In principle, it might depend on what sort of fiscal stimulus you are talking about—whether you are talking about investment spending, whether you are talking about a tax cut or whether you are talking about a one-off payment.

Senator XENOPHON—So there are different effects, depending on what it is?

Dr Gruen—Yes, but I would not want to mislead you to think that economics is sufficiently precise to be able to give definitive answers about how big these things are exactly. So, when I said ‘half to one’, that gives you an idea of the extent to which there is uncertainty about the magnitude of these things. We do not know it any better than that. In principle, you might think that spending on investment would deliver you a somewhat higher multiplier than handing money to individuals. The reason you might think that is that some of the money might be saved by individuals, whereas if you spend a dollar on infrastructure then the dollar has been spent and contributes directly to GDP.

Senator XENOPHON—Does that depend on the type of infrastructure? There is a debate about what sorts of criteria were used to determine the choice of capital works programs. I think the three Ps are population, participation and productivity. How did they come into play in determining whether to spend it on upgrading schools or relieving infrastructure bottlenecks, for instance?

Dr Gruen—We are in a very unusual situation, which is that Australia is suffering from insufficient aggregate demand for the whole economy. So the package has been framed with the thought in the backs of our minds that it is important to come up with spending plans that will deliver stimulus to the economy quickly—let us say over 2009 and perhaps into 2010. That is based on a current assessment of what we think is the nature of the global recession; namely, we think it is deeper, and will be longer, than we thought several months ago. So we are focused on spending that will have a material effect on demand within the economy over that sort of time frame. In assessing the spending in this package, an important criterion is spending that will actually have an impact on the economy relatively quickly, because that is the nature of the problem that we are facing.

Dr Henry—I will just impose there. In response to a question of Senator Brown’s earlier, I indicated that the circumstances we are confronting are those in which gross domestic product is growing at a rate that is very much below its trend rate of growth—that is, the level of gross domestic product is falling as a result of an insufficiency of aggregate demand. It is falling below the trend level of gross domestic product. There is a gap emerging between the actual level of gross domestic product and its trend level. The three Ps that you refer to impact on the trend level of GDP. And so, perhaps somewhat ironically, were we to undertake action now which increased the trend level of GDP this year we would actually open even further the gap between trend GDP and actual GDP—unless those measures also increased aggregate demand by the same amount.

A further observation I will make in answer to your question is that in closing the gap between the actual level of gross domestic product and its trend level—that is, in minimising the impact on the unemployment rate—it does not matter a lot whether the increased investment spending is on maintenance, repairs or new capital. It might make a difference of course to trend growth some years down the track, but in terms of closing that gap and dealing with the deficiency of aggregate demand it does not actually make a difference.

Senator XENOPHON—I will just follow on from that. Some economists are posing the question: how will building assembly halls and sports centres increase the productive capacity of the Australian economy in the future to help repay the debt that the Australian public will have? The flip side of that is that it would make more sense to deal with much-needed infrastructure bottlenecks and spend the money there. It will make a difference, won’t it?

Dr Henry—Let me comment on that. What they are really saying, in terms of the language I was using earlier, is that if public investment expenditure were to be directed to dealing with infrastructure bottlenecks or enhancing the size of productive infrastructure, or the economy’s productive capital stock, that would increase the economy’s productive capacity, and so in future years it would allow the economy to grow at a faster rate. That is the argument.

Senator XENOPHON—It is pretty compelling though, isn't it?

Dr Henry—Yes, and if only it were that simple. If only one could find all of these high capacity building infrastructure projects and turn the tap on now everyone would do it. The difficulty is that they do not exist.

Senator COONAN—Would you be able to tell the committee why those 10 particular aspects were picked?

Senator JACINTA COLLINS—Just while we are on this point so we can cover the same ground at once, for instance, Dr Henry, why do we have a two-for-one leaning in favour of investment spending as opposed to cash payments? Can you explain the basis for the overall composition of the package?

Dr Henry—I think Dr Gruen has actually answered that question. If the spending is in the nature of direct government spending on goods and services—it could be employing public servants perhaps; I thought I would put that in—that adds directly to aggregate demand by the amount of the additional government expenditure. If the government spends money on maintenance of a school building, that adds directly to aggregate demand by the amount of the additional government spending. It is also true that if the government spends money on the development or acquisition of new items of capital equipment that also adds directly to aggregate demand, again by precisely the amount of the increase in government spending. All those things make a contribution to aggregate demand that is equal to the increase in government spending whereas if governments provide additional disposable income to households through whatever means then, as was noted earlier, for some period of time some proportion of those increases in disposable income per household will be saved so that something less than a full dollar of the addition to household disposable income will show up in aggregate demand in that year. Of course, it will show up in aggregate demand in some subsequent year because, as I was explaining earlier, saving is nothing more than deferred consumption, so by definition it is going to show up at some point. But less than a dollar will show up in the year in which the budget balance is impacted.

That is why I believe, and certainly in advice tended to government we were saying, there is clear argument for having the package containing a bias in favour of direct increases in government spending but that is not to say that the entire package should consist of increases in direct government spending because there are inevitably lags in government spending. With very few exceptions it is possible for a government to increase its spending overnight—maybe it could increase the salaries of public servants overnight. But with that exception it is very difficult for governments to increase their spending overnight. Macroeconomists talk about implementation lags involved in government spending increases. If you want to have a speedier, timely impact on aggregate demand it is quicker to provide additional purchasing power to households.

Dr Watt—Dr Henry's point is very neatly summed up in a table on page 17 of the document, where you can see the measures divided into two different groups. The top group is the direct government spending. As you can see, very little direct government spending occurs in 2008-09. With the best will in the world, with the fastest-acting infrastructure, capital or repair and maintenance programs that we could find, it was still extremely difficult to spend much money in the next five months.

Senator JOYCE—Then why are we in such a bun rush to get this package out, if it is not going to work in 2008-09?

Senator COONAN—Two days!

Dr Watt—Could I perhaps finish answering the senator's question and come back to that later?

CHAIR—Senator Xenophon has the call. You will have the call later on, Senator Joyce. We will all get through this much quicker if we just allow people who have the call to proceed. Senator Xenophon.

Dr Watt—If I could just finish. As you can see in the bottom panel on that table, the direct payments to families and individuals impact on 2008-09 disproportionately by comparison. So they give you the relatively rapid stimulus in 2008-09. The capital projects, the repairs and maintenance projects, pick up steam through 2009-10.

In response to the question about timing, it is also worth thinking this: you would have lags in direct government expenditure no matter when you commissioned it. If you decided to have a package in six or nine months and you did not do the work on it for six months, you would still have the same lags.

Senator JOYCE—I will have some questions for you later on.

Senator XENOPHON—Can I just follow on about this whole thing about the quality or the type of infrastructure spending if it is going to be spending directed to relieving bottlenecks for our export industry. There will be a bounce-back, hopefully sooner than later, in our export industries. Doesn't it make sense to be

allocating some of this package towards relieving those bottlenecks so that when there is a recovery in exports we can capitalise on that, or is there a concern that we will not get to last year's export figures for quite some time?

Dr Henry—No, I do not think that is the concern. I think rather the issue is: in dealing with the very rapid decline in aggregate demand that we have in our forecasts, can that form of infrastructure spending be brought online in a sufficiently timely fashion that it can impact on aggregate demand now? Those infrastructure bottlenecks are worth addressing, no matter what the macroeconomic circumstances are that Australia is confronting. They should be judged on their merits as supply enhancement initiatives. The government's consideration of those things, in my view—and this is advice I would tender to any government—should not be affected by the state of the macroeconomy. But those projects do not tend to be the sorts of projects that can be brought on stream very, very quickly in order to address a very rapid decline in aggregate demand. They tend not to be of that nature.

Senator XENOPHON—So having hundreds of schools having projects built at the same time—you are saying that will have a greater impact on the economy more quickly.

Dr Henry—It will. I do not think there is any question about that.

Senator XENOPHON—Is there a concern, however, that you will get labour shortages? Whilst building has slowed down, there will be this injection. Have there been any forecasts done in relation to whether there will be enough skilled labour to deal with these projects in every primary school in the country, for instance?

Dr Henry—Again, as Dr Gruen indicated, our modelling of the impact of this package is done at a fairly highly aggregated level. Again, the multipliers that he referred to implicitly take those things into account.

Senator COONAN—Could the multiplier be zero or even negative? I am just following on from what Dr Gruen said. Sorry, Nick, but it just fits in there.

Dr Gruen—It is hard to imagine it being negative, but zero would imply that, if you handed out a dollar, the full dollar was either imported—well, imported would not make it zero; even when you import things, you employ people to get them to shops. It would all have to be saved. For it to be negative, it would have to lead to even more savings as a consequence of doing it, and that seems unlikely.

CHAIR—Senator Xenophon has the call.

Dr Gruen—You are handing it to—sorry, should I answer his question?

Senator ABETZ—Sorry. I will ask that later.

Senator XENOPHON—Could I perhaps ask Dr Henry a question in relation to interest rates. To what extent will this package and the proposed cash handouts slow reductions in official interest rates? A couple of days ago I think Glenn Stevens, the chairman of the Reserve Bank, said that in making the latest interest rate decision the bank took into account the package of measures announced by the government earlier in the day. Does that in any way suggest to you that it may impact on any future interest rate reductions?

Dr Henry—You are putting me in a somewhat difficult position, because I, of course, am also a member of the Reserve Bank board. It is my usual practice to leave it to the governor to refer to any considerations that the Reserve Bank board may have undertaken. Of course, the governor has done so in his public statement and I imagine will be able to field those sorts of questions when next he appears before this parliament.

Senator XENOPHON—In terms of general macroeconomic policy, if you could comment.

Dr Henry—Sure. I was not going to conclude my answer there. That was a preface, which is a way of saying that this is a difficult question for me to answer. But I am going to try to provide an answer to it. Please do not interpret my comments as in any way speaking on behalf of the Reserve Bank board. I would not do that; it would be inappropriate of me to pretend that I am speaking on behalf of the Reserve Bank board. I can only tell you what my assessment is. My assessment is that the weakness in aggregate demand that we are confronting in Australian economy calls for both very substantial reductions in interest rates and very substantial fiscal stimulus. I think it is the case that—well, it is certainly the case—that these two arms of policy are working in the same direction and complementing one another. If your question was whether these measures were complements or substitutes, my answer is that they are complements.

Dr Gruen—Can I just add a little to that answer. The relevant international organisations that comment on this issue, the IMF and the OECD, have been making extremely strong statements lately about the need for advanced economies—and, for that matter, other economies—to provide rapid, sustained stimulus through

both monetary and fiscal policy. The tenor of their comments has been increasingly to try and make it clear to the international community just how serious the situation is and how important it is for all arms of macro policy to do as much as they can to stimulate the economy. We really are in a situation that none of us at this table has ever seen in our adult lifetimes.

Senator XENOPHON—Can I just follow on—I have just a couple more questions, chair. I do not know if any of you have had the time to see Professor Robert Shiller on *Lateline* last night.

Dr Henry—No.

Senator XENOPHON—He talks about one-off cash payments, tax cuts or a combination. Professor Shiller said:

... the thing is that tax cuts are, if they're spent and if you direct them to the people who are likely to spend them, will be very evenly distributed across the economy and so have an important impact.

He went on to say:

Infrastructure unfortunately tends to be focussed on certain areas and it may cause bottle necks in those areas ...

There is that debate—or having a combination, as I think is planned in the United States. Do you have a particular view on that mix between tax cuts and cash handouts?

Dr Henry—This was a consideration that the government focused on in the formulation of the package. The government sought advice from us on capacity in the construction sector. We did provide advice to the government to the effect that we considered that there would be, in aggregate, sufficient capacity in the construction sector to undertake the projects that have been included in this package.

Senator XENOPHON—On that, Professor Quentin Grafton has called for spending on the Murray-Darling Basin, saying that that would do more for long-term productivity and the national infrastructure. Were big picture projects like that the sorts of things that were considered in the context of this package providing that productive capacity and dealing with major environmental and economic problems such as in the Murray-Darling Basin?

Dr Henry—I can only refer to the answer that I have given previously: that supply enhancing public and private infrastructure projects should be considered on their merits, irrespective of the state of the cycle and irrespective of whether the economy is growing at trend, above trend or below trend. This package has been designed, like the one before it, to deal quite explicitly with a deficiency of aggregate demand.

Senator XENOPHON—What implications does this package have for your tax review?

Dr Henry—That will be revealed in December.

Senator CAMERON—There has been much commentary about the economic irresponsibility of the government in implementing this package. I understand that governments around the world are implementing similar packages. Could you give us some idea of what is happening worldwide. Is this package consistent with the action that the IMF and the OECD are recommending for governments to take? If it is, then is the government acting responsibly in doing what it is doing?

Dr Henry—Without commenting on the last part of that question, it is certainly the case that governments around the world are acting now to develop fiscal stimulus packages. In fact, a number of governments around the world announced a fiscal stimulus package last year. The USA did, as did Spain, Japan, Korea and Taiwan. Obviously Australia did, as did Thailand, Germany, China, Malaysia, Italy, Israel, Russia, the UK—I could go on. Many, many countries around the world have in the last 12 months announced—

CHAIR—Could you table that list for the committee?

Dr Henry—Sure. We are happy to do so.

CHAIR—Thank you. Sorry to interrupt.

Dr Henry—Many, many countries around the world have in the last 12 months announced fiscal stimulus packages. If one adds up all of the fiscal stimuluses that have been announced globally, they come to 2.8 per cent of global gross domestic product. Details of that are set out in the table, which we are happy to table. It is also the case that governments have been encouraged by the international institutions, particularly the International Monetary Fund and the OECD, to develop and implement fiscal stimulus packages. Indeed, the government's statement released on Tuesday refers to some of the statements that have been made by the International Monetary Fund and the OECD.

Senator ABETZ—What page is that on?

Dr Henry—Page 16, box 2.3. For example, in its World Economic Outlook released on 28 January, the International Monetary Fund stated:

Monetary and fiscal policies need to become even more supportive of aggregate demand and sustain this stance over the foreseeable future, while developing strategies to ensure long-term fiscal sustainability.

The document goes on to quote from Olivier Blanchard, the IMF's Economic Counsellor and Director of Research. G20 leaders, you will recall, on 15 November last year—

Senator FIFIELD—A point of order. Dr Henry is nothing if not comprehensive in his answers, but I think it probably takes up a little bit of the committee's time to have slabs of the document read out to the committee.

CHAIR—I take your point of order, but I remind committee members that when we ask questions I cannot direct witnesses on how to answer.

Senator CAMERON—I am finding it very interesting, actually.

CHAIR—I am sure Dr Henry will keep his answers as succinct as possible.

Senator FIFIELD—I refer you to page 16, Senator Cameron.

Senator CAMERON—I would like it from the horse's mouth.

Senator JACINTA COLLINS—On that point of order, Senator Abetz asked Dr Henry if he could take him to the page on which he was referring to these matters, so the opposition is interested in the points that he is making as well.

Senator ABETZ—On the point of order, I was concerned that we were having slabs read to us, and that has now been confirmed.

Senator JACINTA COLLINS—He was not at that stage.

Senator CAMERON—I am not asking him where they printed it.

CHAIR—We are all mindful of the time. Dr Henry has the call. Please conclude your answer.

Dr Henry—I will avoid reading from the document. I probably should note that, at their November meetings, G20 leaders—and of course Australia is represented in the G20—committed to using expansionary fiscal policies to support aggregate demand. The OECD—for the sake of completeness—whilst noting that, in normal circumstances, macroeconomic management would be left to monetary policy, found that these are not normal circumstances for OECD member countries and that therefore there is a case for OECD member economies to use fiscal policy to support aggregate demand.

Senator CAMERON—There has been some commentary this morning that we should sit and wait to see how the global recession pans out. Is there any economic basis for that statement that you would be aware of?

Dr Henry—For how long should one sit and wait? Obviously that is not a view that we have taken in providing advice to government. These are highly unusual circumstances, and we have advised government—and I indicated in questioning before a parliamentary committee on an earlier occasion that we had provided advice to government—that there was a need for fiscal policy action and that it was quite urgent.

Senator CAMERON—There has also been a proposition put forward that, as part of a stimulation package, government should pick up the superannuation responsibilities of small business. Has the Treasury costed that? Have you any idea how much that would cost the economy?

Dr Henry—I understand that Senator Sherry was asked a question along these lines in parliament today—in fact, I have just been provided with a copy of his answer. I have not had a chance to—

Senator FIFIELD—Senator Cameron was in the chamber.

CHAIR—The question has been asked; let him answer it.

Senator FIFIELD—I thought that might be of assistance.

Senator CAMERON—That is nearly as good as the printing question.

Dr Henry—I think it is the case that Senator Sherry referred to some costings that the Treasury department had provided to him as the minister responsible for superannuation. I have not had an opportunity to compare what he said with the costings that we have provided. Let me put it this way. Superannuation guarantee payments amount to a very substantial amount in a year, obviously. Superannuation guarantee is nine per cent

of earnings, and that amounts to a very large amount. I do have in front of me a copy of the advice that we provided to the minister. This is preliminary advice but what it indicates is that, if the government were to make the full superannuation guarantee payments of all small businesses in Australia, the cost to the budget would be of the order of \$10 billion or \$11 billion a year. That would be in full, all of the nine per cent, for small business.

Senator ABETZ—Nobody has suggested that.

Dr Henry—I am not aware of what people have suggested, Senator. I do not know.

Senator FIFIELD—So that is not purporting to be a costing of an opposition policy?

Dr Henry—I certainly have not presented it that way.

Senator FIFIELD—I think Senator Sherry may have today.

Dr Henry—I am certainly not presenting it that way. I am just indicated that costing.

Senator CAMERON—Ten or 11 billion a year, eh? There you go!

Senator FIFIELD—Except that is not our policy, Senator Cameron.

Senator ABETZ—Make up our policies and then condemn them, Dougie: that is your style.

CHAIR—Thank you very much, Senator Cameron. We now go to questions from Senator Joyce, and can I remind you that at 7.15 we will be going to Senator Fielding.

Senator JOYCE—Thank you, Madam Chair. With the deepest respect, a lot of what I have heard tonight is the most convoluted and extensive load of waffle that has stood in proxy for decisive answers. Let's try and get to some decisive answers. What particular model did you use to support the assertion that you would be supporting 90,000 jobs?

Dr Gruen—I think, Senator, that I got through half my answer to Senator Xenophon. We would love to have a particular model that was sufficiently reliable that it could answer all economic questions, but we do not have such a model.

Senator JOYCE—Did you use any model?

Dr Gruen—Sorry, I have not finished my answer. We use the evidence available to us, which is from a range of sources, both Australian and international sources. We have the TRYM model, which we run as part of the process of putting together our forecasts; we do that as a matter of course. We also have a series of single equation models for different parts of the economy which include employment equations, consumption equations, investment equations. We do a variety of these things and we apply judgement. And on the basis of all of those things we put together estimates.

Senator JOYCE—And you came up with the number 90,000?

Dr Gruen—The phrase is 'up to 90,000 jobs'. We start with an estimate of how much we think the package will raise GDP and then from there we use an employment equation to give us an estimate of what increase in employment that will lead to, relative to not doing it. So that is how we do it.

Senator JOYCE—Okay, up to 90,000. So that also includes the number one?

Dr Gruen—It does.

Senator JOYCE—So it is more than one?

Dr Gruen—There would be a range around 90,000 but it would not include one.

Senator JOYCE—So, more than 50,000?

Dr Gruen—I started by saying when I was answering Senator Xenophon's question that our estimate of the fiscal multiplier is something like a half to one, as in spending to GDP. We would like to be more precise than that, but if you look at the literature, including papers produced by the IMF, that is exactly the sort of range that people quote. We do not have these numbers to the degree of precision that we or anyone else would like. We have estimates with a range of the order of half to one for the multiplier.

Senator JOYCE—Dr Gruen, in the probability bell curve of numbers what was the mean number?

Dr Gruen—Let me just go through and tell you how we get to the 90,000 and then we can have that discussion. Our estimate is that an increase of one per cent of GDP leads to up to 75,000 jobs and we have a package here which raises the level of GDP by the middle of 2010 by between 1/4 and 1/2 per cent.

Senator JOYCE—Let us go through some of the other things that you have told us about.

Dr Gruen—That is how we get the 90,000.

Senator JOYCE—Let us talk about some of the other things. Just quite simply: we are borrowing money, the US is borrowing money, the EU is borrowing money and the UK is borrowing money. Everybody is out there borrowing money. Where is the piggy bank with all this money in it that we are going to get? Where are the excess funds looking for a home? Do you think that there will be a tightening in the market because everybody is out there looking for money?

Dr Gruen—On the side of private investors there has been a huge reduction in appetite for risk, so investors are crying out for government assets, which they deem to be safe, so yields on government bonds all around the developed world are falling because demand is extremely strong for those sorts of assets.

Senator JOYCE—Like the US\$1.5 trillion; there is strong demand out there for that?

Dr Gruen—Judging by the 10-year US bond, the demand for that is extremely strong.

Senator JOYCE—I just want to go through your key components for the Nation Building and Jobs Plan.

Dr Gruen—It is not mine; it is the government's plan.

Senator JOYCE—Okay. In the last one before Christmas there was \$8.7 billion with no modelling and it did not deliver an extra 75,000 jobs. But we do know that there was an extra \$1 billion in retail spending and if we seasonally adjust that there is about \$700 million. So \$700 million of the \$8.7 billion—let us say that we divide it by an eighth. So \$12.7 billion divided by eight is about \$1.5 billion and \$1.7 billion up above in building prosperity for our future. We are really talking about \$3.2 billion possibly. If things trilled we are talking about \$3.2 billion in the 2008-09 period.

Dr Gruen—Can I just respond to some of those comments. When you said there was no modelling done, I think that may be based on a conversation we had at Senate estimates last time. I said that we had not done any formal modelling of the details of that package. That was the statement that I made. I did say that we had done analysis of that package and we had certainly done analysis based on empirical estimates of fiscal multipliers on how much we thought that would translate into jobs. So it was based on detailed economic analysis, not formal modelling using a formal economic model.

Senator JOYCE—Did you use formal modelling this time?

Dr Gruen—As I said actually at the time, in the process of putting together forecasts, one of the things we do is run formal economic models.

Senator JOYCE—So you did do it this time?

Dr Gruen—Sorry?

Senator JOYCE—You have done it with this package?

Dr Gruen—That is something we always do in the process.

Senator JOYCE—But not the last one.

Dr Gruen—No, no. When we put together economic forecasts, which is what we did for MYEFO. When we were having the discussion last time we were in the process of putting together MYEFO and I made the point at that time that in the process of putting together MYEFO we were in the process of running economic models. I made that point to you on 22 October. You may have more faith in economic models than I do.

Senator JOYCE—I just like to see them done.

Dr Gruen—No, I am genuine about that. They are an input. They help you to refine your judgments but they are not the be-all and end-all. We do a variety of things. That is one of the things we do but we do other things as well.

Senator JOYCE—I want to go to your aggregate level modelling regarding the IMF and the fiscal multiplier. If I were to use the fiscal multiplier model, would I get more bang for my buck out of a new rail system bringing connectivity between ports to a higher level or, for example, ceiling insulation?

Dr Gruen—If you are interested in the effect on aggregate demand and you spend the dollars at the same time, the answer is likely to be very similar.

Senator JOYCE—So ceiling installation is about the same bang for my buck as new capital infrastructure such as rail and ports?

Dr Gruen—I think I am just traversing ground that Dr Henry traversed earlier. You are talking about things that change the supply potential of the economy, and I think Dr Henry made the point that there are a range of things that you should consider doing whatever the state of the business cycle is. Whatever the situation, there are things that you should do for the long-term productive capacity of the economy. The nature of this package is unusual because we are in extremely unusual times. The situation we are confronted with is one in which aggregate demand is very substantially below the supply capacity of the economy—it is not necessarily currently, but all the indications are that, left to itself, the economy will grow significantly slower than its supply capacity.

Senator JOYCE—There are two things there. You have said that we have the capacity in the short term to fulfil our requirements on things that are laid out in this package for the current aggregate capacity in the economy. So, at this current point in time, is there capacity in the economy to provide pink batts for 2.2 million homes?

Dr Gruen—I am not sure. I think I will leave to others the issue of pink batts. I am happy to talk about the kind of broad picture but I am not in a position to talk about the details of specific programs. But others are, so if you wish to ask about that, I think I would leave it to someone else.

Dr Henry—I would say that the time profile over which that particular measure will be implemented is reflected in the profile of costs to the budget that Dr Watt referred you to earlier—page 17—and, in developing that profile of impact on the government budget, we have done our best to take into account the time period over which that measure could realistically be implemented.

Senator JOYCE—What about boom gates? Have we got them all out there ready to go? How are boom gates going to increase the aggregate capacity of the economy?

Dr Henry—I suspect that my answer to all of these questions—assuming that you have a series of them—is going to be the same. And it is in two parts: first, that every one of these measures can be expected to make a contribution to aggregate demand. They are all in the nature of additional government spending and they will, as I said earlier, make a contribution to aggregate demand precisely equal to the increase in government spending that is involved in those measures. So that is the first part. That is true of the rail measure that you refer to. It is true of repairs and maintenance expenditure and so on. It is also true of supply-enhancing infrastructure projects. So in that respect they are the same. As Dr Gruen said, and as I said earlier, of course there can be differences among these things with respect to the contribution they make to the future supply capacity of the economy. That is true. But a project which would make a substantial enhancement to the future supply capacity of the economy is a project that should be done anyway. And it should be done on top of these measures.

Senator JOYCE—You cannot possibly sit here in front of us and tell us that the fiscal multiplier effect of infrastructure spending is the same as ceiling insulation over the long term. I know, Dr Henry, you do not believe that.

Dr Gruen—Over the long term, you are quite right.

Dr Henry—Sorry, Senator, I was not saying that.

Dr Gruen—Neither of us were saying that.

Dr Henry—I understand your question to be: would expenditure on home insulation, ceiling bats, today make the same increase to Australia's GDP in five years—let's say 10 years to be safe—as expenditure on some supply enhancing infrastructure project would make to GDP in 10 years time?

Senator JOYCE—Yes.

Dr Henry—The answer to that question is no.

Senator JOYCE—So you can see that roof bats are a very—

Dr Henry—Assuming that the Australian economy is growing at trend in 10 years time, the answer to that question is no. Obviously our level of potential gross domestic product in 10 years time would be higher if the spending were to occur on some supply enhancing infrastructure project. That is obviously the case. The problem we are dealing with at the moment, as Dr Gruen and I have tried to explain, is that we are in very unusual circumstances, quite unlike the circumstances we have been in the last 10 years, in which the aggregate demand in the Australian economy is about to fall dramatically below potential gross domestic product. This package is about trying to minimise the extent to which aggregate demand falls below potential gross domestic product. The reason for that is that, as I said earlier, if aggregate demand falls markedly below

the potential level of gross domestic product, then so too will the actual output in the Australian economy fall markedly below its potential, and many people will end up unemployed.

Senator JOYCE—There are a whole range of packages that fulfil that premise. Do we fervently believe that pink bats and boom gates and school halls are the optimum investment for this nation to give efficacy to this package? When they came to this you said, ‘No doubt about it: if you’re going to kick-start the economy in the short term pink bats are the way to do it.’

Dr Henry—Clearly that is the judgement the government has made.

Senator JOYCE—It is a political decision.

Dr Henry—It is not for me to comment on whether it is a political decision or not, but these are measures which, as the table on page 17 that Dr Watt referred you to earlier indicates, can have a timely impact. These are measures which could be introduced reasonably quickly—not sufficiently quickly, as Dr Watt noted, to impact terribly much on the five months left in the first half of 2009, but nevertheless, as you can see from the table, they will have a very substantial impact in 2009-10 and 2010-11. There seems to be a view in your questioning that there are a very large volume of supply enhancing infrastructure projects out there on which government expenditure could be undertaken tomorrow. That is not the case. It is obviously the case that there is a lot of infrastructure spending that is being undertaken, but could that be doubled, tripled or quadrupled overnight? No, I do not think it could be.

CHAIR—Can I interrupt for a moment just to remind committee members that Dr Watt will be leaving us now and returning at 8.15, so if people have questions relating to his area they should ask them now.

Senator JOYCE—Do you agree with the assertion that of that \$8.7 billion there was only about \$1 billion that actually ended up in retail spending, which fiscally adjusted to about \$700 million? Is that a fair comment?

Dr Henry—I would not endorse that number. I cannot endorse that number, for the very obvious reason that you are talking about the month of December retail sales figures. The October package started being paid out on 8 December, I think.

Mr Ray—In that week.

Dr Henry—In the week of 8 December. So maybe we are talking about an impact on retail sales in two weeks of the month of December. That is the first point. Secondly, the proposition that the \$8.7 billion package increased retail sales by only \$700 million involves a judgment about where retail sales would have been in the absence of the \$8.7 billion package.

Senator JOYCE—Retail sales include alcohol, don’t they?

Dr Henry—I guess so.

Senator JOYCE—And retail sales also include gambling, don’t they?

Senator CAMERON—No, retail sales do not include gambling.

Senator JOYCE—We are trying to get an answer, Senator Cameron. I am not sure about that.

Dr Henry—As I indicated earlier—

Senator JOYCE—It definitely includes alcohol; I can assure you of that.

Dr Gruen—We do not believe it does include gambling, but we can check for you.

Senator JOYCE—Okay. Would it make sense that if retail sales include alcohol and the package went out before Christmas—and I have seen your assessment of that package and the ARA out there saying how wonderful it was—then it is not surprising that you are going to get a spike in the sale of grog if you are giving people money for free?

Senator JACINTA COLLINS—You normally get one at Christmas anyway, so you have to look at seasonally adjusted figures.

Dr Henry—I do not know. I do not even know if that is what happened. We would have to have a look at a product-by-product breakdown of retail trade to even know whether that occurred. But, as I said earlier, retail trade makes up about 40 per cent of household consumption activity, so there are a lot of things that households spend income on that are not included in retail trade. The other point is that, as Dr Gruen noted, our assessment of that earlier package—correct me if I am wrong, Dr Gruen—is that over some quarters it would contribute about one percentage point to gross domestic product.

Dr Gruen—Half to one.

Dr Henry—Half to one—that is right. That half to one per cent of gross domestic product is between \$6 billion and \$12 billion—is that right?

Dr Gruen—Yes.

Dr Henry—That was the judgment we made at the time, it is the judgment we continue to make and it is obviously not consistent with a judgment that the \$8.7 billion has added only \$700 million to aggregate demand.

Senator JOYCE—It is all that can be detected at this point in time. I have one more question and then I will leave it to my colleagues. We know that the US is getting to the point—some would say they have gone beyond the point—of the money that they should be in deficit by. How much can Australia go into deficit for before, in your view, we have gone into deficit for too much? I know you are going to think, ‘How do I not answer this question?’ and give us a long exposition of the whole myriad of possible circumstances, but in your gut feeling what would be a number that would make you sit up and say, ‘Boy, you’ve gone too far when you are in deficit for that amount’?

Dr Henry—Yes, I am going to do my best to—

Senator JOYCE—Not answer the question.

Dr Henry—not answer the question. I think the way most economists think about the deficit question is to think about public debt dynamics. We have had since the mid-1980s a concentration in this country on the level of public sector debt, I would suggest, as in no other country on earth. As you know, Senator, today Australia has negative net debt. There is a chart, chart 4.2 on page 46 of the document, that looks at the net debt position of selected countries in the years 2008, 2009 and 2010. You can see the negative net debt position of Australia; I think it is minus 1½ per cent.

Senator JOYCE—Those crazy neoliberals and all their bad economic management.

Dr Henry—It is minus 1½ per cent of gross domestic product in 2008, and you can see by how much that is projected to grow over the three-year period from 2008 through to 2010. This chart compares—

Mr Ray—Minus 1.3.

Dr Henry—Minus 1.3, I am sorry; not minus 1.5. I think this document records that by 2012 in Australia’s case it will grow to 5.2 per cent of GDP—so that is June 2012. That is on the basis of all of the figuring that appears in this document. This chart shows how that compares with other countries.

Senator JOYCE—I can see them. What is Australia’s GDP then?

Dr Henry—It is about \$1.2 trillion.

Senator JOYCE—Do you think that Japan has excessive debt?

Dr Henry—Do I think that Japan has excessive debt? Well, this is where the stuff gets really tricky.

Senator JOYCE—For you.

Senator FIFIELD—I think we should have gone into that years ago.

Dr Henry—The reason it gets really tricky is that Japan has not had a lot of difficulty financing that debt, and this is the question.

Senator JOYCE—I know. Obviously, you know what I am framing. I am saying that when we get to \$1.2 trillion in debt, do you think that will be too far or do you think that will be all right?

Senator JACINTA COLLINS—What?

Senator JOYCE—It is just an honest question.

Senator JACINTA COLLINS—What makes you think we are going to go up to 45—

Senator JOYCE—We have a facility out there for \$200 billion. We are on our way.

Senator ABETZ—Why do you want it if you are not going to use it?

Senator JOYCE—I think it is far too much debt, but I want to hear from Dr Henry that \$1 trillion in debt is too much. Or does anybody believe that it is not too much? Does anybody have an opinion on it?

Senator FIFIELD—I think debt is a sign of virtue now.

Senator CAMERON—If you have the assets you can do it.

Senator JACINTA COLLINS—It depends on whether you are having a financial crisis.

Senator ABETZ—Until we have to start repaying that debt.

Senator JACINTA COLLINS—Generated by global factors, not by the current government.

Senator JOYCE—I am giving Mr Henry the courtesy to answer.

Dr Henry—Are you asking: would a net debt to GDP ratio of about 100 per cent for the Australian economy prove unsustainable?

Senator JOYCE—Yes.

Dr Henry—Yes, I reckon it would.

Senator JOYCE—Thank you very much. It is an obvious question. It is not weighted. I just wanted to get something on the record. How do we start servicing this debt, less \$200 billion? What are we looking at there? One per cent is \$2 billion so we are just roughly working it out with what Senator Conroy said today, which was about \$2.6 billion, so that must be about five per cent costs. That is \$10 billion a year at \$200 billion. Is \$10 billion a big drain on excess cash to the long-term future?

Dr Henry—There is a need to draw a distinction between gross debt and net debt, of course.

Senator COONAN—Could you outline the details of gross and net?

Dr Henry—Do not hold me to particular numbers but at the moment I think we have gross debt on issuance of about \$60 billion. Mr Ray suggests \$58½ billion, which is about 5½ per cent of gross domestic product; something like that. This is gross debt.

Senator COONAN—This is as a result of forecasting the package.

Senator JOYCE—No. This is actually now.

Dr Henry—This is now. So we are making interest payments on that gross debt. We make interest payments in the form of coupons for people who hold Commonwealth government securities on that debt. But at the same time, we hold financial assets on the balance sheet; obviously in the Future Fund and other financial assets that we hold that more than offset that gross debt on issuance. Obviously, as we go forward in financing these deficits, gross debt on issue will increase.

Senator COONAN—How quick will it accelerate?

Dr Henry—That depends. There are a number of ways in which deficits can be financed, of course. Deficits can be financed out of cash before one has to borrow. One might nevertheless choose to borrow and increase gross debt and put the cash aside for later; that might be a prudent debt management operation. It might not be strictly necessary in order to finance the budget but it might nevertheless be considered prudent as a debt management operation. If one were to do that one would experience not only an increase in gross debt but also an increase in financial assets of exactly the same amount and with no impact on net debt. The impact on net debt is not necessarily the same as the impact on gross debt, and it is the impact on net debt that determines the financing cost to the government. Right?

Senator COONAN—Yes.

Dr Henry—I think Mr Ray has some numbers on the anticipated increase in financing cost. That is consistent with the increase in net debt that is presented in this document.

Mr Ray—No, I don't.

Dr Henry—I thought you did. All right, he doesn't!

Mr Ray—I suspect it is the number that Senator Conroy used.

Senator COONAN—It is \$2.66 billion. Is that right?

Senator JOYCE—It is \$41.534 billion, and it has \$2.66 billion or something in interest. I am doing some rough figures and thinking the cost of funds is about five per cent.

Mr Ray—The cost of funds is going to depend on the maturity structure of the debt that gets issued, and we have not yet determined that because it would depend on market conditions. But at the moment I think our average cost of funds for new issuance is around about four per cent.

Chair, I need to correct an answer I gave earlier to a question asked of me by Senator Abetz. The document first went to the printers at six o'clock on Monday morning; it did not go on Sunday. When Senator Abetz is back, maybe after the dinner break, I can run through the time line.

CHAIR—I would appreciate that. I am sure he would like that information.

Senator FIELDING—Dr Henry, you covered this a little bit before. Where do you expect unemployment to be in one year, and in two years, before this package and after this package?

Dr Henry—I do not think we have provided estimates of where unemployment would be in this package, although we can probably get fairly close from information that has been provided. I refer you to table 3.2 on page 33 of the document, which contains a summary of domestic economic forecasts. You will see, under the labour market section towards the bottom of the table, estimates of the unemployment rate. As the footnote (g) indicates, these are actually estimates for the June quarter of that year, so the 5½ per cent forecast for 2008-09 is an estimate of the unemployment rate in the June 2009 quarter—that is, this year; in fact it is the next quarter. For the subsequent year, 2009-10, the seven per cent figure is the estimated unemployment rate in the June quarter 2010. Dr Gruen indicated earlier that, in our view, were it not for the package there would be an additional 90,000 people who would not have a job in the June quarter 2010.

Senator FIELDING—So you basically added to that number?

Dr Henry—Yes.

Senator FIELDING—Roughly.

Dr Henry—Yes, roughly. There could be some offsets on the participation rate and all sorts of things, but roughly you could add the 90,000 to that seven per cent figure.

Senator FIELDING—Could you give me a feel for how many more Australians will be out of a job at seven per cent from, basically, today or last June? Can you tell me roughly how many Australians will be out of a job to get to seven per cent? I do not need it down to the last 10 or the last hundred.

Dr Henry—I think is about 300,000, or something in that order. But bear in mind that not all of those 300,000 presently have a job, in fact the majority do not. We are talking about out to June 2010, so that is more than 12 months away. What happens over that 12 month period is that the labour force grows because new people come into the labour force—from education or immigrants or just people who are returning to the labour force after having a child or whatever—and some of those will not be able to find a job. In addition, some who presently have a job will lose it.

Senator FIELDING—So out of that 300,000, roughly how many may have had a job and lost it over that period? You know the numbers pretty well.

Dr Henry—I think it is about one-third.

Senator FIELDING—What I am trying to get to is that this package supports or helps 90,000 jobs but another 100,000 Australians are going to fall off the edge through this period. Out of the \$42 billion being spent, could you outline what those 100,000 Australians would get in addition if the \$42 billion was not there? I understand there may be another 90,000 joining them if it was not there, but I am interested: how does the \$42 billion help those 100,000 Australians? I think it is lower, but we will leave it there. I am struggling to find it that is all.

Dr Henry—Some of those people will obviously receive some of the payments that are included in this package.

Senator FIELDING—950 bucks. And? Let me go one step further: 950 bucks and a very low prospect of getting work given that they are unemployed. I am worried about those 100,000 people. How is the \$42 billion going to help them? I understand there may be another 90,000 joining them if we do not spend the \$42 billion.

Dr Henry—Sure. I do not know if this is going to help, but—

Senator FIELDING—No, it is not going to help.

Dr Henry—No, I meant what I am about to say.

Senator FIELDING—Go ahead.

Dr Henry—Maybe I should not bother if it is not going to help. What I was going to say is: to the extent that one can minimise the number of people losing a job, the better the prospects are of those people going forward being able to find a job—that is, the greater the extent to which one can minimise the number of people who lose a job, the smaller the period of time for which those people might find themselves out of work.

Senator FIELDING—I can understand what you are getting at there, but I am looking at it from the point of view that they are not numbers on a bit of paper. These are 100,000 real Australians, families that will go to the wall with very little prospect of finding a job. It is not their fault—that is okay. So the \$42 billion being spent: I understand that another 90,000 may join them if we do not spend it, but tell me which part of the package directly helps them.

Dr Henry—Okay. I will point you to the measures identified on pages 62 and 63. The measure on page 62 refers to trade training centres in schools, accelerated activity. The measure on page 63 deals with training and learning bonus and education entry payment supplement.

Senator FIELDING—Yes, I have got that, but I think there is a huge gap. How much more would you need to spend? You have 90,000 jobs—I understand it is not accurate, that it is a ballpark figure—with \$42 billion. Is it double that amount to save another 100,000?

Dr Henry—Pretty much if you were to use this set of measures. If you were to use this set of measures, you would pretty much have to double the size of them to have that effect—maybe even more.

Dr Gruen—Just to add to that: we have talked a bit about the capacity of finding projects to spend this sort of money on relatively quickly. If you were to double all of the packages, it might be the case that it would be genuinely very difficult to find projects for that amount of money.

Senator FIELDING—Do you think the No. 1 concern in the community is disposable income or jobs? Out of those two, which do you think Australians are more concerned about at the moment? You are the Treasury, so you must have a good feel for it.

Dr Henry—Mr Ray is just saying to me that they are linked. And it is true that they are linked. I would answer the question this way: there should be no doubt that efforts should be made to minimise the extent to which the unemployment rate increases. I do not think there is any doubt about that. But I would add to that that the biggest risk to unemployment in Australia at the moment is the deficiency of aggregate demand emerging and we have been talking about that here this evening. The surest way of minimising the increase in unemployment in prospect is to do what we can to close that emerging gap between—

Senator FIELDING—And that is the idea of the spending.

Dr Henry—Sure.

Senator FIELDING—Okay. Can I just go to the spending part? The Economic Security Strategy was about spending. For every dollar spent on retail—just keeping it very simple—how many cents go into the profits of the retailers; how many cents go into overseas costs that are not local production; how many of those cents end up in tax, the GST? For every dollar spent, do you know roughly? You have got a good handle on it. That way we can work out how efficient it is. In other words: for every dollar spent, is 50c going to overseas products? That would be an awful, inefficient way of trying to stimulate the Australian demand in jobs.

Dr Henry—Sure. Without putting numbers on it, let me put it this way: what you are referring to is the second round effect of the increase in government spending. This affects the size of the multiplier that Dr Gruen was referring to earlier by between half and one per cent of GDP. There are various what we call leakages from either an increase in government spending or an increase in transfer payments or a tax cut.

Senator FIELDING—Keep on going in a second, but I just want to interrupt to ask you to take that on notice to come back to the committee to say, as a rough estimate, for every dollar spent in retail, how is it broken down, in cents, into the components where it goes to: tax, GST, profits to retailers—as a model, if you can. Now keep going with your answer. I interrupted just in case I did not get the chance to ask you later on.

Dr Henry—Okay. We will take that on notice. One of the leakages, and we have spent quite some time this evening discussing it, is there could be a leakage into household saving. If households are provided with a tax cut, whether it is temporary or permanent, or they are provided with a cash grant, or provided with an increase in family payments—it might be permanent or whatever—of course it is the case that some proportion of that will go into household saving. For present purposes that would be regarded as a leakage from aggregate demand that occurs immediately, so it detracts from the direct impact of the measure.

Senator FIELDING—Just to clarify, I did not ask about what leakage, I asked about for every dollar spent on retail.

Dr Henry—Sure. What is left over does not leak into saving—

Senator FIELDING—The question was, for every dollar spent on retail, not if it is. It is an actual question. For every dollar that is spent on retail.

Dr Henry—I understand. Some might leak into household saving, and then the households present themselves at the retail with the bit that is left. They say, 'I have already decided to save that bit but now I am going to come to the retailer and I am going to spend a dollar.' In the dollar that they spend, some proportion of it—and you have asked us to take this on notice and we will do that—some proportion of that dollar, some cents, will go to wages of the workers who work in the retail sector. Those workers belong to Australian households. Some of the increase in wages they will save. That is another leakage. Some of it they will say, 'I'm going to spend this,' and they will come back and present themselves to other retailers, and so on and so on. That process is referred to as a multiplier process.

Some of the dollar in that first bit of retail spending will not go in wages, it will go in interest because the retailer might have some debt the retailer has to service, and that interest will be income to a whole variety of people some of whom obviously will be domiciled overseas, because the Australian banking system borrows from overseas to finance its lending to Australian businesses, including retailers. The bit that goes overseas is an income leakage. But the bit that goes to Australian households, like the wages and salaries that go to Australian households, some of it will be saved and some of it they will bring back into the retail sector and you get that multiplier process.

Some of the dollar received by the retailer will not go in wages, it will not go in interest, it will go as income to the equity owner of the retail enterprise. If it is a big retail enterprise, the equity owners tend to be shareholders and so they will receive dividend income. Some of those shareholders will be domiciled overseas, and that is further leakage. The other shareholders will be domiciled in Australia obviously and, just like interest receipts, just like wages receipts, they will decide to save some of that. The other bit they will spend and they will come back and re-present themselves to retailers.

Senator FIELDING—GST?

Dr Henry—You are quite right. Some of it will go in GST revenue to state governments.

Senator FIELDING—And income tax.

Dr Henry—Indeed. There is of course company tax that might be paid as well, and that is a receipt to the Australian government. With respect to the wages and with respect to the interest receipts of the workers and the people who have lent money to the retailer, there is income tax paid on that as well and there may even be interest withholding tax paid in respect of interest payments that go to foreigners.

So there are several leakages here. The Australian government gets a bit, the state governments get a bit through GST and some is saved, and some goes overseas. It is the net of that bit that comes back into the system and goes round and round and round, obviously with smaller increments to aggregate demand on each occasion.

Senator FIELDING—How much better would it be if it was Australian made products?

CHAIR—Sorry, can we just wrap this up. We have already lost a number of senators and it is past time for the break. Senator Collins has one follow-up question and then we will take a dinner break.

Senator JACINTA COLLINS—With regard to the figures you undertook to give Senator Brown in relation to people who do not pay tax, can you provide, related to those figures, an estimate of what proportion of the people who do not pay tax and would not receive this rebate would receive one of the other payments or would have received a payment in December? I know it is probably going to be very complicated to try to deal with that factor.

Mr Parker—It gets progressively complicated. We will look at what information we can provide.

Senator JACINTA COLLINS—One reason I asked that question is that the questions that Senator Fielding was just asking relate to people who may be newly unemployed, who of course under this package will benefit from the tax payments in terms of the financial year being 2007-08 and, if they have children, will benefit from the family tax payments. I am not sure of the basis for the 100,000 figure that Senator Fielding referred to. Was that the figure, Senator Fielding? Certainly a portion of those people would be in families with children or with other income earners—all the other various factors of the package. I just want some feedback to the committee that deals with the fact that there is a mixed package of proposals here, and where people miss out in one area there is a fair likelihood that there is going to be some coverage in one of the others.

Mr Parker—We will endeavour to paint that picture for you. It is highly complicated, as you have begun to sketch out; indeed, there are many other layers of complication under that, but we will endeavour to do what we can.

Proceedings suspended from 7.36 pm to 8.18 pm

CHAIR—Thank you and welcome back.

Senator COONAN—I wanted to come to the mantra of ‘timely, targeted and temporary’ and to ask the witnesses this question. The \$42 billion is over the forward estimates and the stimulus in 2008-09 is \$12.7 billion. What are the key reasons for announcing a large \$42 billion package now rather than a more modest package of, say, around \$12 billion in this financial year and then announcing subsequently, if required, further packages for stimuli in 2009-10 and later? In other words what I am getting at is whether or not—and if so, why not—one-off payments could have been announced later.

Dr Henry—We traversed some of this ground, although I guess not directly, in our answers before the dinner adjournment. As we indicated earlier, on every occasion at which you would be facing decisions of a fiscal stimulus variety, you will be confronting the issue that every measure that you decide to implement will be subject to an implementation lag. As Dr Watt indicated earlier, and as table 2.1 on page 17 illustrates quite well, the length of that implementation lag depends upon the type of measure that one is talking about. The implementation lag is somewhat shorter for direct transfer payments to households and somewhat longer for direct government spending. So if one were to decide that on this occasion one was going to reserve for a future period any decisions about measures impacting in, let us say, 2009-10, for example, then when one came to make those decisions, one would be confronting precisely this problem again. The problem with sequential decision making is that it will never prove efficacious to deciding to undertake activities that have an implementation lag longer than the period of time between the two decision making points.

Senator FIELDING—Talk in plain English, sir.

Dr Henry—Well let me see—I will talk in plain English—

Senator FIFIELD—I think that one of the key elements of the question was: what is magic about the number 42?

Senator COONAN—Why have \$42 billion now?

Dr Henry—Let me put the answer in somewhat more direct terms. Were decisions not taken now, very little of the impact that you see in 2009-10 would be there. So if you want to have a fiscal impact in 2009-10 and you want that fiscal impact to be through direct government spending—the measures which are in the top part of this table—then you have to take the decisions now. If you leave it for another 12 months, for example, you will not be able to have an impact in 2009-10 in respect of those measures. Well, you will not be able to have much of an impact. The earliest you will be able to have much of an impact will be 2010-11 and so on. You will be continually pushing out for about a year the time at which those measures would have an impact on the economy. There is an inevitable implementation lag. Is that sufficiently clear—an inevitable implementation lag. You have to take the decision and you have to be prepared to live with the implementation lag.

Senator COONAN—Yes, I understand that. What the committee is really interested to know, if I am interpreting it correctly, is that given this is a mixed package and that what the government has sought to do is to try and provide an immediate and direct fiscal stimulus with one part of the package and take some decisions now to be implemented later that will continue hopefully to have that effect, why then does it add up to \$42 billion? What is the significance of \$42 billion as opposed to a mixed package of \$50 billion or a mixed package of \$20 billion? What makes you any more certain that \$42 billion is the number?

Dr Henry—The thinking that informed the development of this package was that the current calendar year, 2009, is likely to be in the absence of any fiscal stimulus a particularly weak year and to some extent also 2010. These are the key years. That is true globally. You can see that in the IMF’s forecasts for world growth. Particularly 2009 is anticipated to be the weak year but with some risk on 2010. So the advice that we provided to government was that it would be appropriate to have a fiscal stimulus which in calendar year 2009 was at least, at a bare minimum, one percentage point of GDP and considerably more than that if it were feasible to develop a package that would have that impact on government spending in calendar year 2009 with some amount being spent in 2010. I guess it was that thinking about the shape of the package which ultimately determined the size of its budgetary cost in each year and its profile.

Senator FIFIELD—Dr Henry, the \$42 billion figure underpins 90,000 jobs. Surely underpinning 100,000 jobs or 200,000 jobs would be better. Why not a bigger package? Why not \$50 billion or \$60 billion? I am still not clear as to why \$42 billion is the quantum. Was it the target to underpin 90,000 jobs?

Senator ABETZ—No; ‘up to’.

Senator FIFIELD—If you could underpin more jobs, why wouldn’t you have a bigger package?

Senator COONAN—There are 100,000 unemployed coming by June.

Senator FIFIELD—I am issuing that the figure of \$42 billion is not arbitrary. I am assuming that seeking to underpin 90,000 jobs is not arbitrary.

Senator ABETZ—It says:

The Plan will help support and sustain up to 90,000 jobs ...

Senator FIFIELD—Yes.

Senator ABETZ—So that is the purpose.

Senator FIFIELD—If you are able to support and sustain more than 90,000 jobs, why wouldn’t you do that?

Senator ABETZ—Because the focus group said \$42 billion.

Dr Henry—I think we are getting into the territory of policy decisions taken by government. I have explained the policy advice that we tendered to government, which is considerably more than I normally do. You are now asking me to reflect on the quality of the decision taken by the government, which is much more than I would ever do.

Senator FIFIELD—Not at all, Dr Henry. Part of the purpose of this package is to inspire confidence I assume in business and amongst consumers and the public that the government is doing everything that it can.

Dr Henry—Sure.

Senator FIFIELD—Part of the confidence in this package surely comes from understanding why this quantum has been chosen. It is a very large number. I do not think it is good enough or acceptable to say, ‘We can’t tell you why \$42 billion is the figure because that goes to advice to government.’ With a figure of this size and with the purpose to underpin jobs, surely part of instilling public confidence in this stimulus package is explaining why it is \$42 billion and why more jobs cannot be underpinned.

Dr Henry—No, Senator, I did not say that I was unable to answer the question because it went to advice tendered to government.

Senator FIFIELD—I might have misheard you.

Dr Henry—I have in fact been more than usually open with you about advice tendered to government.

Senator FIFIELD—That is certainly correct.

Dr Henry—But what I did say is that your question is asking me to reflect on the quality of a decision taken by government, and that is asking me to take a further step.

Senator FIFIELD—I am not seeking to have you reflect on advice to government, because I know that is not a reasonable thing to ask of you, but what I am asking is what the rationale is for this figure of \$42 billion. I cannot think of a more fundamental question about this package. Otherwise, the public is quite entitled to think that this is an arbitrary figure, chosen for—I could hazard a guess as to reasons but—

Senator FORSHAW—Dr Henry has just said is correct about why he cannot ultimately reflect on this—

Senator FIFIELD—He is not being asked to.

Senator FORSHAW—Excuse me. It would be the same as if a question were asked of the previous government: why did you choose a certain level of tax cuts that amounted to \$X billion rather than some other formula for tax cuts that might have resulted in a different amount or in a different distribution?

Senator ABETZ—We would have answered it.

Senator FORSHAW—It is that type of question, which ultimately I think is just—

CHAIR—The question has been asked and answered on a couple of occasions.

Senator ABETZ—But do not ask about the size of it!

CHAIR—The question has been put and it has been answered and there are two other senators who want to ask something in relation to that. Maybe that will help clarify it for you.

Senator FIFIELD—I do not think the question has been answered, but—

Senator COONAN—I actually had the call.

CHAIR—Senator Fifield actually had the call. I acknowledged that.

Senator FIFIELD—Well, I interposed on Senator Coonan.

CHAIR—That is right, he did. He asked a question. There are now two senators who have questions relating to that issue. As we did earlier, Senator Coonan, we allowed that to happen. We will go to Senator Cameron, then Senator Brown and then I will come back to you.

Senator FIELDING—And I have a point of clarification too.

CHAIR—We will deal with these and if you still need that clarification, Senator Fielding, you will get the call.

Senator CAMERON—Dr Henry, I understand economics is not simply about numbers and that jobs are absolutely important, but the economics of this package go back to something that was really driving all of the debate some time ago, and that is to get confidence back into the economy and get people spending—try to overcome some of the deleveraging that is going on in banks. Is that part of the overall issue?

Dr Henry—Yes, it is. It definitely is.

Senator CAMERON—And it is very important to do that—to try and get some normality in the face of this global economic crisis, to try and get as normal an operating economy as possible. And confidence is fundamental to that economic approach. Is that right?

Dr Henry—Yes. We would certainly agree with that, and that is consistent with the view that we have taken in the advice that we have provided to government. There is absolutely no doubt that real economic weakness is typically preceded by weakness in consumer and business confidence. You can see it in the consumer and business confidence indices that are published by various organisations. Part of the key to getting through this period without an even larger increase in unemployment—part of the key—is restoring business and consumer confidence. There is no doubt about that.

Senator BOB BROWN—My question follows straight on from Senator Cameron's question and that answer. It seems to me that this package is well designed to keep Australia's growth in each of the four quarters of this year—March, June, September, December—in the black. Is that so? What is Treasury's estimation of the impact on consumer confidence and confidence in the economy if we did move into a technical recession?

Dr Henry—I cannot answer the second part of that. I think there is very little doubt that confidence is impacted by perceptions of the strength of growth in the economy. There is no doubt about that. And I do not think there is any doubt either that confidence is affected by what is happening to employment and unemployment. But I would not want to put a number on it. I could not possibly put a number on it.

As to the first part of your question, it is true that the fiscal impact of this package has a profile that, as I said earlier, is designed to fill in the periods of greatest economic weakness that we had in our forecast.

Senator BOB BROWN—And to keep the growth pattern in the positive?

Dr Henry—Sure, I think we should all be wanting to see positive growth—and if that can be achieved in every quarter, we should all be very happy about that.

Senator BOB BROWN—Finally on that issue, it is becoming better known in economic discourse that psychology is important and that if we can stay out of a recession and stay in the positive, that is self-enhancing—

Dr Henry—Sure, that is right.

Senator BOB BROWN—It does have a material impact on the economic wellbeing of the country.

Dr Henry—Yep.

Senator BOB BROWN—And it is having the effect—you have said that—but was the modelling for this package designed to ensure that as best as possible we avoid going into a recession?

Dr Henry—I don't know about the modelling but, as I said earlier, the construction of the package, and the timing of its fiscal impact, the profile of its fiscal impact, has been designed to address the periods of greatest weakness that we had in our forecasts.

Senator BOB BROWN—So it may be that a \$12 billion or a \$21 billion package would not have achieved that goal?

Dr Henry—I think the document allows you make an assessment of that matter yourself, because the document, on the top of page 17—I have previously referred to this—refers to the fact that we estimate that as a result of this package, with the profile that is in table 2.1, GDP growth will be around half a per cent higher in 2008-09 and around $\frac{3}{4}$ to one per cent higher in 2009-10. It follows, I think, that a smaller package, even a smaller package with the same profile, would contribute smaller amounts to GDP growth in 2008-09, and with a package that had the same profile and the same composition as this package—I know those are two big qualifications—but that had a lower level, a lower aggregate amount, there would be some point at which GDP growth in 2009-10 in particular might well have been negative.

Senator Fifield interjecting—

CHAIR—If Senator Brown can just ask his final question on the same issue, we will then go to Senator Fielding, who wants to clarify the issue.

Senator FIFIELD—This relates directly to the what Dr Henry said just then. Dr Henry, if you could invert what you said, would a larger—

Senator JACINTA COLLINS—Chair, he needs to get in the queue. Everyone is trying to deal with supplementary issues.

Senator FIFIELD—This is actually the coalition's call. Senator Brown said he was following up a point that related directly to a question in answer to a coalition senator. I am now picking up a point—

Senator JACINTA COLLINS—But you are not the only one. That is the point. There are others who are waiting to do exactly the same as you.

Senator FIFIELD—I am speaking, Senator.

Senator FORSHAW—But you have started interrupting.

Senator JACINTA COLLINS—Yes.

Senator FIFIELD—This relates directly to something Dr Henry said.

Senator JACINTA COLLINS—Yeah, well get in the queue!

Senator FIFIELD—This is actually our call at the moment.

Senator JACINTA COLLINS—No, it is not 'our' call.

Senator FIFIELD—Senator Coonan had the call. She generously allowed me to interpose—

Senator JACINTA COLLINS—No she didn't—I didn't hear that.

Senator FIFIELD—Senator Brown was following up an answer to a question from me, so we yielded. I am now wanting—

Senator BOB BROWN—You do not want the next question asked, do you?

CHAIR—You have the opportunity, can I remind people—

Senator FIFIELD—I have a point which relates directly to something Dr Henry said then. I think this is the appropriate time to have it answered.

Senator JACINTA COLLINS—Senator Fifield, the point is that you are not the only one in that situation.

Senator FIFIELD—I am not the only one but I am one and I have a right to put a question.

CHAIR—Senator Fifield has the call. After we have clarified this, we will go to Senator Fielding who still wants clarification and then we are going back to Senator Coonan.

Senator FIFIELD—Thank you, Chair. Dr Henry if I could just ask you to invert what you said before. If you had a larger package which was of the same profile and composition, would it therefore follow that you would see higher GDP and be supporting and underpinning even more jobs?

Dr Henry—That is quite possible. Of course, the fiscal impact as you would imagine would probably not be linear—you know what I mean by that.

Senator FIFIELD—Yes.

Dr Henry—If you double the size of the fiscal package you should not necessarily expect to see twice the impact on GDP. So maybe at some point, one would have to start worrying about the capacity issues that other senators were asking me about earlier. As I indicated, this particular package takes account of judgements that we and Finance have made about the capacity of the economy to, if you like, digest these programs. If these programs, for example, were to be doubled, maybe we would make different judgements about the capacity of the economy to digest those programs in that same time profile. I suspect we would and for that reason we should not expect the multipliers to be constant. Therefore, you should not expect a linear impact.

Senator FIFIELD—Did you model a larger package?

Dr Henry—We modelled the government's package.

Senator FIFIELD—But did you model a larger package?

Senator JACINTA COLLINS—I do not think they can answer that question. That is advice to government.

Dr Henry—It is advice to government.

Senator FIFIELD—There might not have been advice provided to the government. It might just have been something modelled.

Dr Henry—I see. Then I will rest on my earlier answer: we modelled the government's package.

CHAIR—Senator Brown, we will go back to your final point that you are following up on.

Senator BOB BROWN—Thank you Chair. You indicated that the package of the same structure but of smaller dimensions would have led towards a failure to have the impact of keeping the growth rate in the black. That leads me to ask: what of a package of the same dimensions that was half the size? Would that have allowed a technical recession to be a much greater danger for the Australian economy in the coming 24 months?

Senator FIFIELD—That would depend on the structure and profile of the package I would think.

CHAIR—There is a question before Dr Henry.

Senator JACINTA COLLINS—If he keeps on like this, we will never get back to Senator Coonan.

Dr Henry—I can go so far as to say that with those qualifications—that is, it was a package with the same time profile and the same composition as this particular package and half the size—those are big qualifications—then there would be greater risk of negative growth at some point. I would not want to be any more precise about it than that. After all, as Dr Gruen has indicated, our forecasting methodology is not as precise as would be required for me to answer that question with absolute confidence. There is some element of risk associated with our forecast as there always is. It is probably the case that right at the moment the risks are greater than usual. There has to be some imprecision in the forecasts that we make.

Senator FIELDING—I need some clarification on the same issue. The question was relating to bigger or smaller packages, and it comes to the modelling. What were the inputs and outputs in the modelling? You have mentioned confidence, you have mentioned GDP growth, in whichever way you want to measure, and you have mentioned the jobs supported, protected or saved. Are they the three outputs of the model? I want to clarify the point on the optimum mix. Economists are marvels at taking complex issues and modelling them. They are not accurate, but it is interesting to know how you would evaluate different sizes of the package. They are the three things that you measured against or was it just one of them?

Dr Henry—No, no.

Senator FIELDING—I will go a bit further. Obviously you could design a package to protect more jobs and less growth maybe or more confidence and fewer jobs. What were the inputs and outputs in the model?

Dr Henry—Sure. There are a lot of inputs and a lot of outputs in our forecasting exercises. Table 3.2 on page 33 is a summary version of the outputs of our forecasting process, and that is only a small subset of the things that you could regard as outputs of our forecasting process. This is the standard set that we publish—we publish in budgets, we publish in MYEFOS, PEFOS and now in UEFOs. It has the principal components of aggregate demand that we have spent some time discussing this evening. That is at the top of the table. That gets you down to gross domestic product. We do, as you can see, both non-farm and farm. We forecast the

current account balance and certain labour market outcomes—the unemployment rate; we have spent a lot of time—

Senator FIELDING—I can see the components there. If you spend \$50 billion or \$30 billion, how would those figures change? In a model, I know you can start with the components and say, ‘Look, I want to build hospitals, health’, and they may have different impacts.

Dr Henry—Of course.

Senator FIELDING—Generally speaking, did you start with the components first?

Dr Henry—Yes.

Senator FIELDING—So you selected some components?

Dr Henry—Yes, it is a component exercise.

Senator FIELDING—So a member of the government maybe went to Rudd and said, ‘We want more hospitals. Build more hospitals because that gets construction going or extensions to hospitals because they would not take much planning, as the hospitals are already there, and it has the same effect on jobs.’ That may have been in there and may have been part of the model?

Dr Henry—It might have the same impact on jobs. It would affect these components of aggregate demand differently, obviously. So, for example, the payments to households would in this table have biggest impact on household consumption activity. That will translate into an impact on gross domestic product. As I was explaining earlier tonight, the same number of dollars spent on a road program would not appear here in household consumption—it would appear in a component of aggregate demand—and would have an even bigger impact on gross domestic product in the year. So you have to go through this component by component exercise. Then, having assessed the impact on gross domestic product, we would then make a judgement on the impact on employment and the unemployment rate. It is the sort of exercise we go through.

Senator XENOPHON—I have a technical question following on from that. What model closure rule did Treasury use when it explored the effects of the proposal? As I understand it, normally you would get the model to adjust the economy to do what is necessary to achieve full employment, and often, as I understand it, the way it does this is to reduce real wages. So if you used a full employment model closure rule, what was the resulting change in real wages under this package?

Dr Henry—No, I do not think that is right. We are not in a position of full employment. As I was explaining earlier, this is not a situation in which we are having a fiscal expansion with an economy already at full employment. If we were, your question about long run closure rules would be quite a significant question. But the exercise we are undertaking here is one in which we have emerging a gap between actual output and potential output. We have growth in unemployment emerging—so clearly not an economy in full employment which is then hit with a fiscal stimulus; rather, an economy which is going into a period of deficient demand that is hit with a fiscal stimulus.

Senator XENOPHON—There would not be a baseline at all?

Dr Henry—We have to get back to the baseline. We first have to get back to the baseline of full employment before your question becomes meaningful, unless I have missed something.

Senator COONAN—I wanted to return to the cash handouts as a stimulatory mechanism. We know that there was a payment amounting to about one per cent of GDP in the December quarter and a bit over one and a bit per cent of GDP in the March quarter. What do you see happening from here? Is this going to go on? Are you expecting that there will be further stimulatory packages of a handout nature?

Dr Henry—I cannot comment on that. Obviously those are matters for government decision. Although obviously we will be continuing to provide policy advice to government, it is entirely up to the government to decide whether there are further fiscal stimulus packages and if so what size and when. Those are matters on which I could not possibly comment.

Senator COONAN—The government is seeking an increase in the borrowing cap from \$75 billion to \$200 billion. Does this mean that it is envisaged that there will be significant further stimulus packages?

Mr Ray—The additional \$125 billion that the government is seeking would finance the deficits that are projected in this document.

Senator COONAN—That is why the extra—

Senator JOYCE—So we are not fully hocked up?

Senator RYAN—Will there be much change out of the \$200 billion?

Senator COONAN—None.

Senator RYAN—Are you saying that extra borrowing will be required to actually finance all these deficits or there would be change left over?

Mr Ray—The cumulative deficits I think are \$118 billion, or something around that. There are additional financing requirements, including, for example, to inject equity into the special purpose vehicle for commercial property. There are a number of other, if you like, below the line financing transactions that are around.

Senator RYAN—But, in shorthand, you see the loan facility of \$200 billion that is being sought from the parliament, raising the requirement, being fully utilised by the announcements in this package and other announcements that have been made to this point—or almost fully utilised; maybe not to the exact ultimate?

Mr Ray—The way that the arithmetic works is that the cumulative deficits are about \$118 billion. There are other gross financing needs that the government has, because of various things it has announced. As things stand, the additional \$125 billion would fund all of those needs.

Senator RYAN—And we have how much outstanding at the moment?

Mr Ray—We have \$58½ billion of Commonwealth government securities on issue now—roughly.

Senator RYAN—So, give or take, there would probably be about \$15 billion to \$20 billion left in the cap of \$200 billion?

Mr Ray—There are a range of other financing needs.

Senator RYAN—One quick yes or no. Senator Coonan asked whether you envisaged any other stimulus packages. Are you working at the moment on any other stimulus packages?

Dr Henry—We cannot answer that question, since it goes to advice that we may be tendering to government.

Senator COONAN—Wouldn't it be more an operational matter of what the government is undertaking.

Senator RYAN—We are not asking the content.

Senator ABETZ—We are not asking the detail of it.

Senator RYAN—I just noticed earlier on that there was obviously a close period of time between the last package and when discussion about work on this started, and I was seeking to maybe avoid that next time we come here.

Dr Henry—Oh, you were trying to be helpful, Senator!

Senator RYAN—I am new here, Dr Henry, so I am.

Senator ABETZ—Can we have an answer?

Senator FIFIELD—Could you answer Senator Ryan's question, Dr Henry?

Dr Henry—I really do not think I can answer the question, Senator. Your question is: is the Treasury at this moment working on the development of other policy options of a stimulatory nature at the request of the government? That goes precisely to the matter of policy advice that might be provided to government.

Senator FIELDING—If I could put it in a different way without asking that question, what could the government spend in the next stimulatory package to stay within the \$200 billion and not ask for more—given that you know the numbers of what is currently taken care of? What could the maximum amount of the next stimulatory package be whilst staying within the \$200 billion? How much is spare?

Mr Ray—This is across the forward estimates?

Senator FIELDING—Yes.

Mr Ray—I think my answer earlier suggested that there would not be that much gross headroom left above these deficits.

Senator FIELDING—But how much is left in the \$200 billion?

Mr Ray—I guess I am asking, at what time?

Senator FIELDING—You give me a time over the forward estimates.

Mr Ray—I would need to take that on notice because it is not a straightforward calculation. I cannot do it in my head.

Senator FIELDING—But what—

CHAIR—Mr Ray has said he will take it on notice. He will come back to us.

Senator FIELDING—What is the rationale for \$200 billion? Can you go through—exactly—Treasury's understanding of why it is \$200 billion?

Mr Ray—The rationale for the additional \$125 billion is that, given the gross borrowing needed to fund these deficits and the other funding needs of the government, including refinancing of existing borrowing lines et cetera, that \$125 billion is what would do it.

Senator FIELDING—But I am asking what the \$200 billion is based on. You must have asked the question, 'Why do you want \$200 billion?'

Dr Henry—The point is there is already an amount of \$75 billion.

Senator JOYCE—You have talked about the aggregate capacity of the economy and said that the reason why we have got pink batts and boom gates and the other detritus that floats through this package is that it really does not matter where the consumer spends it as long as they spend it. So it really would not matter if it was pink batts or ice creams. There is \$1.7 billion from 2008-09. Why, if that is the case, do we not just reduce taxes and let the consumer spend it where they will?

Dr Henry—Presumably you mean reduce taxes on a permanent basis?

Senator JOYCE—Yes, bring forward the taxes so they can spend their \$1.7 billion. If it really does not matter if they put it into pink batts or boom gates if it is all irrelevant—

Senator COONAN—Or save it.

Senator JOYCE—Or save it. Why don't we just reduce—

Senator ABETZ—As I understand it, with the income tax—

CHAIR—Senator Abetz, I am sorry but Senator Joyce put a question that has not been answered. If we could just have one question at a time, it would be most helpful.

Dr Henry—So we are talking about a bring-forward of a tax cut that is already legislated?

Senator ABETZ—Yes, that is what we are talking about.

Senator JOYCE—Yes, of course, because the other tax cuts are going to happen anyhow, so we know they are in the budget.

Dr Henry—I think I would assess that, in macroeconomic terms, as much the same as a one-off tax cut; that is, a tax cut that is provided for whatever that period of time is, whatever the bring-forward, and then withdrawn. That is, in concept it is similar to a one-off cash transfer to households in terms of its macroeconomic impact. The question therefore goes to the distribution of the tax cut bring-forward versus the distribution of the cash payments made to households. Would the brought-forward tax cut direct the transfer from the budget to households who are more or less likely to spend it? That is how we would analyse it.

Senator JOYCE—So did you formally model this to come up with a conclusive answer?

Dr Henry—Formally model it—

Senator JOYCE—You almost said no there.

Dr Henry—We didn't.

Senator JOYCE—You didn't formally model it.

Dr Henry—We did not formally model it.

Senator JOYCE—In fact, did you formally model any of this package?

Dr Henry—Yes, we formally modelled the entire package.

Senator JOYCE—So we formally modelled the impact of boom gates and Bradford batts and other such programs?

Dr Henry—As I said, we formally modelled the entire package.

Senator JOYCE—So any tax cut would have the same effect as Bradford batts and all these other issues?

Dr Henry—No. It would certainly have a smaller effect. I am sorry if this is getting a bit technical, and I would like to use plain English, but, provided the margin of propensity to save is greater than zero, it would certainly have a smaller impact tax cut than the Pink Batts costing the same amount. We have been through this on many occasions this evening and the reasons for that.

Senator COONAN—Because you have to make assumptions as to what impact that would have on a transfer to a household, wouldn't you? It is the difference between a one-off cash payment and a tax cut.

Dr Henry—This is the second point.

Senator COONAN—That is what I understood you to say earlier.

Dr Henry—The first point is that a dollar spent on Pink Batts by the government adds a dollar to aggregate demand. A dollar of transfer to households will add less than a dollar to aggregate demand, for the reasons that Dr Gruen indicated earlier, in the first instance. Just how much it adds to aggregate demand depends upon the propensity to spend of the people who get that transfer from the government. So if it is a tax cut that goes to households that have a high propensity to save, then obviously it would have a smaller impact on household consumption than if it were a tax cut that went to households that had a smaller propensity to save and a bigger propensity to consume.

Senator COONAN—So are there assumptions made about that? How does that work?

Dr Gruen—Qualitatively, I think it is reasonably well established that people on lower incomes tend to spend a higher share of these transfers to them. There is quite a lot of evidence of that. So to the extent that the package gave a higher proportion of the transfers to low-income people, you will get a larger effect on aggregate demand than if you gave a higher proportion of it to high-income people.

Senator JOYCE—What makes you make the decision that my propensity—or whatever you want to use—or my desire to put in ceiling insulation, if offered to me, is going to be greater than my desire to spend my tax cut if I receive it?

Dr Henry—We have not made that assumption, because if you do not elect to have the insulation installed then of course there is no increase in government spending.

Senator JOYCE—Then it would have to be less than a tax cut if I received a tax cut.

Dr Henry—We are talking about per dollar of government spending. If you do not elect to have the insulation installed, then in your case there is no dollar of government spending.

Senator JOYCE—Then that means the fiscal multiplier effect of me not doing it is less than what it would be if I received a tax cut and had a multiplicity of ideas, rather than just sticking it in the ceiling with the rats and the mice.

Dr Henry—The cost to the budget in those two cases would be very different. In the first case there is no cost to the budget. In the second case there is a cost to the budget.

Senator JOYCE—But one where we are actually saving money and stimulating the economy. It seems like a win-win situation to have a tax cut.

Senator CAMERON—That is not the assessment.

Senator JOYCE—That is not your assessment.

CHAIR—Is there a question?

Senator JOYCE—That was the question.

CHAIR—After this question has been answered, we are going to go to Senator Milne.

Senator JOYCE—I know the Labor Party are putting their faith in ceiling insulation. We have that clearly on record.

CHAIR—Senator Joyce, we are not here to debate amongst ourselves; we are here to put questions to the panel in front of us. The more time we spend debating amongst ourselves the less time everyone has to put their questions. There is a question before Dr Henry. When he has responded, we will be moving to Senator Milne.

Dr Henry—Do you want me to repeat the answer?

Senator JOYCE—No. I am happy with the answer. The answer is that if people spend money there is going to be a greater fiscal multiplier than if they do not decide to take up ceiling insulation.

Dr Henry—No. That was not the answer.

CHAIR—Perhaps you should just answer it again to make sure that everyone is clear.

Dr Henry—Suppose every household in Australia elected not to have insulation installed, then there would be no cost to the budget of that particular measure. So you would not be comparing like with like in any sense.

Senator JOYCE—There is no stimulant effect to the budget if they do not use it, is there?

Dr Henry—Right—

Senator JOYCE—How do we get a stimulant effect to a household that has installation?

CHAIR—Let him answer.

Dr Henry—What the costings in this package reflect is our judgment about the number of households that would elect to have the insulation installed. We have not assumed that every household in Australia will.

Senator JOYCE—What are you going to do—send around people to look in people's roofs?

Dr Watt—It is not hard to work out. There are some estimates of how many homes have ceiling insulation and how many do not. That information is known. That forms the basis of the assessment.

Senator ABETZ—But you do not know how many will take it up.

Dr Watt—Given the attractiveness of the options, which would cover a very large slice, if not all, of the cost of the insulation, it is hard to believe that many households would not take it up.

Senator ABETZ—We will see.

Senator MILNE—Like a lot of other people around the world, I had hoped that the response to the financial crisis would be an opportunity to also address the climate crisis and peak oil. I hoped that we would take the opportunity to restructure the economy for the long term and insulate low-income earners as much as possible from the coming increase in energy prices because of the carbon price and so on. So, whilst I appreciate the need to get money into the economy straightaway through a cash injection and then an infrastructure spend which will kick in after that, can you explain to me why it might not have been better to target your \$12.7 billion cash payments to direct consumer spending? You could expand the energy efficiency and the water efficiency program, for example, so that you have the money to buy things—everything from relatively cheap items like water efficient shower heads through to more expensive items like dual flush toilets through to water tanks, as well as ceiling and wall installation, going through to curtains, blinds and awnings. That would cover a whole range of small businesses across the country. It would target consumer spending to those businesses and would avoid the problem of: what if people do not spend the \$12.7 billion and save it instead? If you had directed it to a range of things that it is to be spent on, would you not have achieved a better outcome in terms of more targeted consumer spending, more likelihood that it would be spent and a better energy and water sustainability outcome at the same time?

Dr Henry—This is a question that really should be directed to the government because you are asking the government why it chose to do certain things rather than others. I would point out that the government has in this package directed a substantial amount towards energy-efficient homes—the ceiling insulation and the solar hot water system initiatives—and I think your question is, 'Well, why, in the configuration of the package, did the government not go further in that same direction?' And really that is a question that is more appropriately put to the government than to the government's advisers.

Senator MILNE—Can I put it another way: did the government seek advice from Treasury as to whether you would get greater certainty about a spend in the \$12.7 billion as opposed to an indiscriminate cash payout and a hope that, because people are lower income earners, they are more likely to spend it? Did they ask for advice as to whether you would get a greater spend from a more directed cash injection than just an indiscriminate cash injection, which this is? I am talking about the \$12.7 billion.

Dr Henry—I think I indicated earlier—you may not have been here, Senator—that we had, in our advice to government, indicated that direct government spending on goods and services will have a larger immediate impact on aggregate demand than a transferred payment or a tax cut provided to households, some of which would inevitably be saved. The structure of this package I think reflects that. The difficulty that I was explaining earlier with a package that relies solely on direct government expenditure on goods and services—

Senator MILNE—Is the time lag; I understand that.

Dr Henry—is the timing.

Senator MILNE—I understand that. That is why I am suggesting that, with a range of things like I am talking about, there is no time lag—you can actually go and buy a lot of those things.

Dr Henry—You have got to set up the programs, and people have to be able to apply, and then of course you have to have people who can answer their queries, and so on. It does take a while to set these programs up from scratch, and the time lag involved in doing so is reflected, at least in part, in the costings that we have provided, or Finance has provided, for the energy-efficient homes initiative, for example. There is an inevitable time lag.

Senator MILNE—What about this issue: did Treasury give any advice regarding trying to link the infrastructure spend with ongoing consumer spending? For example, if you had funded the Sydney Harbour link project for cycling, you would be talking about \$25 million or something as an infrastructure project, but once that was built that would drive considerable consumer spending as you would have an expansion in people buying not only bikes and helmets but clothes and a whole range of things, and you would also have a significant long-term impact on congestion, health and a whole range of issues. So was Treasury asked about looking at the infrastructure spend as a way in which, in coordination, you could then stimulate ongoing consumer spending?

Dr Henry—Probably not in precisely the way that you have put it—that is, in drawing a link between the infrastructure investment expenditure and what it might do for sustaining household consumption expenditure. I do not remember us having that exchange with the government. I do remember a lot of discussion about the ability to bring forward infrastructure projects, and of course that discussion is ongoing and it plays into, in part, the government's consideration of the recommendations from Infrastructure Australia.

Senator CAMERON—A point of order, Chair: I am trying to listen to these responses, and there are a couple of meetings going on between other committee members. I just need some quiet if you do not mind.

CHAIR—I take the point of order. I remind committee members that, if you want to have a conversation, it is polite to leave the room. That is a reminder to everyone.

Dr Henry—I was just saying that there is an ongoing consideration of infrastructure issues, in part because the government is awaiting the final report of Infrastructure Australia and so on. To the specific question you raised about bringing forward infrastructure projects that are strongly complimentary with consumption, I do not remember us being asked for advice on that issue.

Dr Watt—I think it is best to say, following up on Dr Henry's point, that when you look at infrastructure projects and those, for example, which Invest Australia has under consideration now, the ability to spend significant amounts of money in the first two or three years is zero. You just cannot get them up and going quickly enough in almost every case.

Senator MILNE—Just as a comment on that, I know that there are a number of cycling infrastructure projects which are already planned and approved by the local authorities and so on that are just waiting for the cash to actually proceed. Obviously there is a lead time if you are starting from scratch, but a number of the projects that I am referring to are already done and dusted; they are just waiting for cash. That is the point I was making.

Dr Watt—When we talk about Invest Australia infrastructure projects, they are very large-scale projects.

Senator MILNE—Yes, but I am talking about a different set of circumstances: you want to get a cash injection out now and you want infrastructure to kick in after that. Surely you would want that infrastructure to try to drive some consumer spending complimentary to it so that you get some of those flow-on effects to take the pressure off, assuming that this is going to go on for a couple of years. Those small \$25 million dollar projects that I am talking about are not big, complicated projects, so they are not going to take that much time to install.

Dr Watt—While I do not know about the nature of those particular projects, on page 22 you will see a program called Community Infrastructure which is designed to deal with relatively small-scale community projects which are relatively up and ready. They are the sorts of projects that may well be considered under that package.

Senator MILNE—The final question I have goes to capacity constraints. I am totally supportive of the injection in infrastructure in education; it is long overdue. I want to see it greened up, but I am nevertheless

very pleased to see that in every primary school there is the capacity to have the buildings that are long overdue. Dr Henry, my concern is that, whilst I heard you say that your advice to the government was that in aggregate there is the capacity across Australia to deliver this infrastructure, that would not be an even capacity, and yet the allocation of funding is meant to be an even allocation—for example, for every primary school, regardless. When you go to a state like Tasmania, for example, it is very difficult already to be able to get tradesmen to do things in a relatively short period of time. Could you give us some insight into what your findings were in terms of those capacity constraints around the country, if you have those. The second thing is: was any consideration given to match the capacity constraints with training packages? You might have short-term, three-month TAFE courses or something to help upgrade the skills of plumbers to be able to roll out solar hot water or those kinds of issues. In the case of school libraries, we will have libraries built and no trained librarians to go in them. Was there any discussion of the complementarity of the people and the skills base that is needed (a) to deliver the infrastructure and (b) to actually maximise its benefits?

Dr Henry—I am not sure that I can answer the second part of the question, because I just do not know. In general terms I think I can address it, at least in part. With respect to the first part of the question, there was a fair amount of consultation with people in state governments about the capacity of the states to absorb the programs that are identified here. In the development of the package, judgements have been made about those capacity issues. That is the first point.

The second point is that, as all senators would be aware, the Prime Minister and the Treasurer met with the premiers, the chief ministers and their treasurers this morning to, among other things, discuss this very point. All the premiers and chief ministers and the Prime Minister obviously recognise that, in order for these programs to be implemented in the way that is set out in this document, there will need to be strong coordination between governments. They agreed this morning on a set of quite formal implementation and monitoring arrangements to ensure that, where there are difficulties of implementation, those difficulties are identified very early and responses are developed to address those implementation difficulties.

Senator Cameron interjecting—

Dr Henry—Yes, it does.

Senator MILNE—Would that include training?

Dr Henry—That is the second part of your question, which, I am sorry, I cannot answer. I am not sure. I do not think so, but I will take that on notice.

CHAIR—Before I call the next senator, Mr Ray was going to report back to Senator Abetz on an important issue he raised in relation to when the document went to the printers. You were going to correct a statement that you made earlier, Mr Ray.

Mr Ray—As I said before dinner, I want to correct my earlier answer. The document went to the printer on Monday morning.

Senator ABETZ—At 6 am?

Mr Ray—It went to be put into digital proof at around 6 am.

Senator ABETZ—If it is digital proof you would know exactly, wouldn't you? Look, a few minutes here or there will not make any difference and I will not delay the committee, but the exact time would be on the document.

Mr Ray—It has to be collected first.

CHAIR—I propose to go back to the opposition at this time and then divide the last 15 minutes between Senator Xenophon and Senator Fielding.

Senator COONAN—I wanted to come to some of the specific measures in this package. We might go to the 20,000 social housing homes. Where are these going to be built?

Dr Watt—That will depend upon where the state housing authorities and community housing bodies choose to build them. In the first instance, there are a number of homes—somewhere in the order of 2,000—

Senator COONAN—The document says 2,300.

Dr Watt—The states have identified those as houses that can be relatively quickly brought on stream. They would be part of housing and land developments they already have or have identified for location. The remainder of the homes to be built under social housing will be subject to two tender processes. One of the things which will be taken into account in terms of evaluation is location. Obviously access to, for example,

transport will be something that the people evaluating those tenders will consider, remembering that that is a bit of a two-edged sword. It is better to have good access to transport, but usually if you are buying the land as well as the house it costs a bit more for it, so there is a bit of a trade off there.

Senator COONAN—Can we know with these 2,300 are? Is there a list or some document that you can point us to?

Dr Watt—I do not have a list with me, nor was Finance ever aware of the exact locations of those homes.

Senator JOYCE—So where did the information come from?

Dr Watt—The information was provided by the state governments to the Department of the Prime Minister and Cabinet, who provided it to us. What we did have, however, was a state-by-state breakdown.

Senator ABETZ—Could you table that?

Dr Watt—I do not have it with me, Senator.

Senator ABETZ—Not table it; supply it on notice.

Dr Watt—On notice I am happy to do that, but I believe FaHCSIA are coming in tomorrow.

Senator COONAN—Yes.

Dr Watt—I am sure they are listening to this with considerable interest. I might say to my FaHCSIA colleagues that they may wish to bring those numbers with them, because I am sure they will be asked.

Senator ABETZ—What makes you think they are listening?

Dr Watt—Human nature, Senator Abetz.

Senator JACINTA COLLINS—They haven't got anything better to do?

Dr Watt—I think they have, but I think they are still watching it.

Senator COONAN—The revised document says that these will be largely completed by December 2010. Without putting too fine a point upon it, Dr Watt, you and I are veterans of tenders and all of the planning and other processes that go into a measure this complex. How is the department actually going to administer this and get infrastructure that Dr Henry said has a very long lag time built and completed by the end of next year?

Dr Watt—There are a couple of points to make, and no doubt you will again wish to have a bit more of a chat in detail with FaHCSIA—and I am sure they will probably thank me for saying that! The two points are these. In relation to the first 2,000, we know that often the land is ready and they are ready to go. That is easy. In relation to the subsequent ones, there will be a high premium put on simple design and quick solutions. Part of the—

Senator COONAN—What does that mean?

Dr Watt—Perhaps I could come back to that. Houses are very simple to build. This is one of the things that are important to emphasise in this package. When you look at the construction activities that we are undertaking, they are all at the relatively simple end of the construction scale—relatively simple. I understand—and this is a very—

Senator COONAN—Is there some standard design that you have seen?

Dr Watt—I would have thought that, as part of the tender processes, FaHCSIA will be looking for standard designs wherever possible, looking for cookie cutter designs. It has been emphasised, for example, to move into the schools area, that there will be a limited number of designs used, so it is not possible to spend a long time designing the project rather than building it. There will be relatively simple—again, relatively simple, because a house is not a completely simple thing—designs used which will make it quicker and simpler. That will not be completely universal, but it will help. If I look at the average time to build a house, I think the numbers I have seen—and Dr Grimes I am sure will correct me if I am wrong—are that, from the time you start to the time you finish, it is in the order of six months. That is once you are ready to go. So, if you are ready to go, that is the kind of time. That is the kind of time that DHA, I think, suggest to us that they can build houses in, once they are ready to go. You are right; there are other things to do, but that is why it is important that the process the Prime Minister has described of high levels of coordination, extensive monitoring and rapid intervention to get things back on track if things look like they are not going on track is important.

Senator COONAN—I am afraid I have been occupied all day and I have not had a chance to look at the communique. What monitoring will go on with these contracts to monitor the fact that the states are not just

stopping their expenditure? There was the threat in the revised document here, the UEFO, that, if the states fail to meet its expenditure benchmarks, it will report its findings to COAG and consideration will be given to a big stick, reallocating the funding. Who would do all this?

Dr Watt—Sorry?

Senator COONAN—Who will be actually doing the monitoring?

Dr Watt—There will be a coordinator-general set up in the Department of the Prime Minister and Cabinet. It is an existing member of that department called Mike Mrdak, who, as the Prime Minister said today, is a highly regarded deputy secretary in that department and has had a long time in infrastructure. There will be coordinators-general—I assume they will be coordinators-general—set up for each state in the state premiers' departments. The reason for setting these things up—

Senator COONAN—How much will this cost administratively?

Dr Watt—Compared with the package, not much.

Senator COONAN—No, but for this—

Dr Watt—I can come to running costs in a minute. It might be better if I finish the story, then I will come to running costs—

Senator COONAN—Okay.

Dr Watt—so as not to interrupt you. There will state coordinators set up in each premier and cabinet department of the states. The idea of setting them up in premiers' departments is to really make sure things happen. Each line agency of the Commonwealth will have a responsible officer who will be responsible for that project. The Prime Minister has made clear that that line officer will have credibility on the line and will be fully accountable for achieving the deadlines as required.

Senator RYAN—Did you say that these offices will be set up in the respective departments of premier and cabinet or their equivalents?

Dr Watt—Yes.

Senator RYAN—Are they Commonwealth or—

Dr Watt—No, these will be state based.

Senator RYAN—State agencies will be reporting to the heads of departments of premier and cabinet?

Dr Watt—I would assume so. They may be the heads of the premiers' departments themselves.

Senator RYAN—Just following on from Senator Coonan, then, these coordinating departments that have been described in here, which are, for lack of a better way of putting it—we are pressed for time—to keep the states honest—

Dr Watt—And for the states to keep their own line agencies honest.

Senator RYAN—are actually reporting to the states and not to the Department of the Prime Minister and Cabinet?

Dr Watt—No, the state coordinators will report to the coordinator general in the Department of the Prime Minister and Cabinet in Canberra.

Senator RYAN—As well as to their own department?

Dr Watt—As well, I am sure, to their own governments.

Senator RYAN—Who employs them?

Dr Watt—Officials at the state level will be employed by the state.

Senator RYAN—And pay them?

Dr Watt—They will be paid by the state.

Senator RYAN—And govern their employment and contractual arrangements?

Dr Watt—Matters for the states.

Senator RYAN—So they have a dotted line, in effect, to Prime Minister and Cabinet.

Dr Watt—No, they will have a direct line to Prime Minister and Cabinet.

Senator JOYCE—Who actually owns the houses?

Dr Watt—The houses will be owned by state housing authorities and community housing authorities, as are houses currently built under Commonwealth social-housing programs.

Senator COONAN—So they will already own the land?

Dr Watt—In some cases they will and in some cases they will acquire it.

Senator COONAN—So just who will have the residual ownership?

Dr Watt—The state housing authorities, just as they do now in all housing built under the Commonwealth-State Housing Agreement.

Senator JOYCE—So the states get the houses and they can sell them at some stage in the future if they wish?

Dr Watt—That I cannot comment on. I do not know enough about state housing authorities' disposal proposals. I suggest you take it up with FaHCSIA.

Senator JOYCE—That is a nice little earner for the states, though, when they sell it, isn't it?

Dr Watt—I think you find there are maintenance of effort clauses in there that would make that difficult.

Senator RYAN—So when this was constructed, were you aware of the program in South Australia announced in March 2007 to sell their public housing?

Dr Watt—I am aware that the states do from time to time sell public housing. That does not stop and has not stopped the Commonwealth from supporting additional public housing with the states. We already have a large number of programs to do that.

Senator RYAN—But there is no restriction at this stage on that happening in the future with these houses being built with this money?

Dr Watt—There is at this stage no restriction. I am sure, however, that that is something that will be taken up in the detailed implementation.

Senator COONAN—What is the probability of an underspend or an overspend on this particular measure?

Dr Watt—When we do costings, we try to do them on a basis of even probabilities. We think we have got central-point costs. In this case, I think we have central-point costs. Now, there are risks around the costing. We could come in under; we could come in over. But, based on the look we have had at this, we are convinced that the time lines are reasonable.

Senator COONAN—You were going to tell me about departmental versus administered costs.

Dr Watt—Compared to running costs? As you will see in the package, we have not agreed running costs for any agency or entity. There will be some. These are substantial programs. That will be done over the next few days, except for the ATO, with whom we have agreed running costs. Why have we not agreed it? The answer is that, with the speed at which we had to move—it was a reasonable speed—it was thought better to look at the running costs over the next week or so.

Senator ABETZ—So we have not even got the running costs sorted for this program? That is indicative of the rush with which it has been cobbled together.

Dr Watt—No, it is not. It is quite common, as you would remember, for issues of running costs to take a little bit longer to resolve than issues other than running costs.

Senator ABETZ—How much longer to resolve?

Dr Watt—I think we will resolve it in the next week or so.

Senator ABETZ—But if this package was being worked on immediately after the last one, I would have thought you would have had plenty of time to sort these little matters out. I suspect this was cobbled together a bit quicker, Dr Watt.

Dr Watt—Running costs are little in size but rarely little in importance to the agencies involved.

Senator ABETZ—But you do not have a figure of the totality of the cost, which will be on top of.

Dr Watt—It is a small amount. It is a very small amount.

Senator ABETZ—It will be on top of.

Dr Watt—It will be on top of, yes, but it is a very small amount.

Senator ABETZ—So it is an even bigger debt we are incurring.

Dr Watt—I think you lose it in the rounding area of the package.

Senator JOYCE—These assets will then be represented on the books of the state government, will they not?

Dr Watt—That is correct.

Senator JOYCE—So it is really just a transfer straight to the states?

Dr Watt—Any existing Commonwealth program on social housing is a transfer to the states. It always has been.

Senator JOYCE—And the schools will be on the states' books too, will they not?

Dr Watt—That is correct, and states and independent school authorities.

Senator COONAN—How many jobs was this particular measure expected to create?

Dr Watt—I would defer to my Treasury colleagues on that.

Dr Gruen—On the nature of the 90,000 estimate, as I said earlier, we came up with that estimate using aggregates. So coming up with an estimate of how much GDP this spending would lead to, given those GDP estimates, what we thought was a reasonable estimate of how many jobs that implied.

Senator ABETZ—But it is not a reasonable estimate when you only give us the top figure up to 90,000. What is your reasonable estimate?

Senator RYAN—That number seems to imply a range. Does the model only spit out a number or does it give you a range? Do you have 95 per cent confidence of it being between, say, 50,000 and 110,000 jobs?

Senator ABETZ—What page?

Dr Gruen—Bottom of page 19.

Senator ABETZ—But that does not answer the 90,000.

Senator RYAN—That answers Senator Coonan's question, I suppose.

Senator COONAN—Clearly it was meant to stimulate the construction sector, so I had anticipated that there would have to be some estimate.

Senator RYAN—But does the model provide a range or does it provide a number of 90,000? That is a change in language and it says 'up to 90,000'.

Dr Gruen—We used the same language last time—'up to 75'.

Senator ABETZ—We have been through that, with great respect.

Dr Gruen—With great respect, Senator, we used the language 'up to 75' last time—we did.

Senator ABETZ—This is appalling. The change was—

Dr Gruen—The question I was asked was—

Senator COONAN—Yes, the change was—

CHAIR—Sorry, but it is awfully confusing to chair this hearing if people are going to interact. Dr Gruen had the call. We wait for his response.

Senator ABETZ—We were referring to—

CHAIR—Sorry, I was speaking and I gave the call back to the witness to continue his answer. Then could we have one question at a time please.

Senator JOYCE—And this is 90,000 jobs—

CHAIR—Senator Joyce, I have just given the call to the witness to respond to the question that is before us. It is very unhelpful to keep interjecting. I remind people that you are under standing orders. Dr Gruen, would you like to continue?

Dr Gruen—Would you please repeat the question?

Senator RYAN—We were talking about the second reading speech. You were making a point about the text of the document. One question I have, which I understand could be answered by Finance and Deregulation as well, is: could a different structure or profile of a package have supported more jobs for the same amount of money, \$42 billion? You have commented before on different timings and different sorts of government expenditure leading to different multipliers.

Dr Gruen—We can make a broad comment on that which is that we have already made the point that we think it is reasonable to expect that the multiplier on infrastructure spending is likely to be higher than the multiplier on one-off payments to individuals. The reason is that, if you spend a dollar, you have already put a dollar into the economy whereas, if you hand a dollar over to someone, they may save part of that dollar. You probably get a larger multiplier for infrastructure spending.

The logic of the package as it is presented and as was explained by Dr Henry is that it takes some time after you have made the decision to actually spend money when you are talking about infrastructure spending. As Dr Henry also explained we think without this package the greatest period of weakness for the economy is the whole of 2009 and that there are benefits in spending some significant proportion of money earlier.

Senator FIFIELD—Would \$42 billion with a different profile have supported more than 90,000 or up to 90,000 people.

Honourable senators interjecting—

CHAIR—The witness has been trying to finish his answer. I have had three senators interjecting. Could we allow the witness to finish and then we will go back to Senator Ryan. You have four more minutes before you lose the call.

Dr Gruen—The problem with the question and the reason it is not straightforward to answer is that one is not interested in an outcome which generates a certain number of jobs, let us say for a week or two. That is not really something worth achieving. In other words if you were to spend a huge amount of money over a very short period of time, in principle, you could employ a very large number of people to do something for a week. My point is simply that the profile matters as well as the maximum number of jobs and therefore it makes sense to design a package which has a profile that both helps the economy in the near term and later on.

Senator FIFIELD—More long-term jobs. The \$42 billion with a different profile.

Dr Gruen—No. In the long run we are not talking about saving jobs.

CHAIR—Senator Ryan, have you finished?

Senator RYAN—I am happy to yield.

Senator FIFIELD—Just a very quick matter which I am sure you will be able to clear up. I was flipping through the document and if you could turn to page 17, table 2.1, the single income family bonus and the total dollar figure for that. Could you read that out to me either Dr Watt or Dr Gruen? I suppose it is Dr Watt, is it?

Dr Watt—I can read it: tax bonus for working Australians. Senator, I can read it out as easily as you can.

Senator FIFIELD—Sorry, the single income family bonus.

Dr Watt—The single income family bonus. Yes, I can read it out. The total is \$1.4 billion.

Senator FIFIELD—One point four billion dollars. Good. Now if you could just go to page 67. It looks to me like a discrepancy but it probably just means I cannot read these figures that well. At the bottom of page 67 it shows 2008-09 and 2009-10 and to me it looks like there is an extra \$97 million which does not seem to be taken into account in the total at table 2.1.

Dr Watt—You are quite right, Senator. I believe the answer was that this was a figure that crept in in error in the final stages of production. I think that is correct, Mr Ray? The error is regretted by both Treasury and ourselves.

CHAIR—Sorry, I did not hear that.

Dr Watt—The error is regretted by both Treasury and ourselves.

Senator FIFIELD—What is the correct figure?

Dr Watt—I would have to defer to Treasury seeing it is their issue. I do not know the answer, Senator, is what I am saying.

Senator ABETZ—Why did we have to discover this? You knew about it and were hoping we would not discover it.

Dr Henry—As I understand it, the figure of \$97 million in 2009-10 simply should not appear. It should be a dash, as in the subsequent years. I understand that is right. These are fiscal balance estimates, whereas the table on page 17 that you have referred to is not fiscal but underlying cash. It reflects the cash profile of the 1.42. The \$97 million is an error; it should be zero.

Senator ABETZ—So we can just put a cross through it.

Dr Henry—Yes.

Senator ABETZ—It would have helped if you had peer-reviewed this.

Dr Watt—In a sense, an erratum has been issued. The appropriation bills are correct.

Senator XENOPHON—I want to get some closure on the closure rule. As I understand it, all macroeconomic models have to have a closure rule to work. That is right, isn't it? Otherwise, there are too many complex interactions. You need to have a stopping point, don't you?

Dr Henry—Yes. All I was saying earlier was that, in this short-term period of less-than-full employment, a closure rule is not particularly meaningful.

Senator XENOPHON—Yes, but there would still have to be some closure rule for a macroeconomic model to work, wouldn't there?

Dr Gruen—It is certainly the case that, if you have a macro model, in order for it to run you have to make explicit assumptions about all of the exogenous assumptions you put into it. That is true.

Senator XENOPHON—There would need to be some closure point for the model to work, wouldn't there?

Dr Gruen—You have to describe the full universe of exogenous variables that you wish to put into the model.

Senator XENOPHON—So where was employment in the context of this modelling?

Dr Gruen—Employment is something that comes out of the modelling. In the long run, the unemployment rate will return to the NAIRU—

Senator XENOPHON—To the what? Sorry, there is a bit of background noise.

Dr Gruen—The unemployment rate will return to the model's rate at which inflation is neither rising nor falling, sometimes called the NAIRU. But that happens beyond the forward estimates—that is a way of thinking about this. In other words, the forecasts end in June 2010, and at that point unemployment is seven per cent and inflation is falling, so we have yet to get to an equilibrium. If you were to take those results as being the output of a model then the equilibrium would be further out in time.

Senator XENOPHON—I will shift to the marginal propensity to save; wouldn't that be the same between a modelled effect in terms of a lump sum as a tax cut?

Dr Gruen—It will depend on who you give the money to. As I said earlier, there is a lot of evidence that suggests that people with lower levels of wealth or lower levels of income tend to consume a higher share of any dollar that is given to them.

Senator XENOPHON—It seems to me that there is an assumption that people would be more inclined to save a tax cut rather than a lump sum. If that is the case, where is the evidence for that? Am I right to assume that what, in effect, Treasury is saying is that people are more inclined to save a tax cut than a lump sum? Isn't that one of the assumptions that have been made, or have I misunderstood that? No? Okay, if I have got that wrong—

Dr Gruen—It will depend on who the money is given to.

Senator XENOPHON—Yes, but was any modelling done to determine what the savings effect would be between getting a tax cut and getting a lump sum?

Dr Gruen—As Dr Henry said, we have modelled the government's package. In principle one could do a wide variety of experiments with a model like this. We did some and not others.

Senator XENOPHON—Sure. So the alternative of what the impact would be on either savings or expenditure in terms of whether it is a tax cut or a lump sum, is that something that was considered or modelled?

Dr Henry—Can I ask a point of clarification, Senator? Are you talking about a lump sum on the one hand versus a permanent tax cut on the other?

Senator XENOPHON—Yes.

Dr Henry—That is a different question.

Dr Gruen—A permanent tax cut has fiscal implications for a very long time. It is not just bringing forward a tax cut that is already there. That is different. Bringing forward a tax cut that is already legislated is like a lump sum.

Dr Henry—Yes. Except that it may go to different people.

Dr Gruen—It may go to different people.

Senator XENOPHON—Behavioural economists like Richard Taylor—I do not know whether you are familiar with his work—

Dr Gruen—I am.

Senator XENOPHON—They say that people put different windfalls in different mental accounts. Sometimes it depends on the extent of the lump sum. If it is \$500 compared to \$1,000 or \$2,000 or \$3,000, they behave differently. They also behave differently in terms of how much they save given what their fears are for the economy and their job. To what extent has any modelling being done or how has that very important behavioural work been taken into account? That is the key issue here, isn't it?

Dr Gruen—We are certainly aware of it.

Dr Henry—Perhaps I can say in general terms that coming to a judgement on the appropriate multipliers to apply to this package we did review quite an extensive literature, including the literature that you are referring to. So we did our best to take into account those effects, but at the end of the day where it comes down is that you have got to make a judgement about the appropriate size of the multiplier to apply to the lump sum or the direct government spending or whatever. But we did refer to that literature in making those judgements about the appropriate size of the multiplier.

Senator XENOPHON—Going back to the issue of whether people would be more inclined to save a tax cut, I put it to you that it would be a permanent tax cut. Would your view be different if it was a difference between a temporary tax cuts compared to a lump sum payment? I think that is something that Senator Joyce has been raising.

Dr Henry—Let me put it this way. If it was a temporary tax cut that was identical to the lump sum both with respect to its aggregate size and the people that it went to, we would not have drawn any distinction between the two things. We would have said these are the same.

Dr Watt—There is the timing question.

Dr Henry—Dr Watt reminds me of a rather important matter, which is that there is in concept the possibility of course that if people get a lump sum in one cheque they were treat it differently from a temporary tax cut that, instead of being provided in one cheque, is provided in a number of small payments, say, each fortnight for, let us say, six months.

Senator XENOPHON—They are more likely to spend that, aren't they.

Dr Henry—Which one?

Senator XENOPHON—The latter.

Dr Henry—No.

Dr Gruen—On one-off payments to people, there is evidence where they actually followed people who got one-off payments and other people who did not so that they have actually got detailed evidence on individuals rather than the total effect on the economy. The evidence is quite strong that something like two-thirds of a one-off payment gets spent within the first six months.

Senator XENOPHON—We have not seen it yet.

Dr Gruen—No, not for the Australian case, but there have been several American experiments of a series of different one-off payments, and the proportion spent is quite high.

Dr Henry—We have not had time to see that yet.

Senator FIELDING—Dr Henry, I want to pick up that point of up to 90,000, so the model must have said that is the upper limit. What is the lower limit? For you to say up to 90,000 jobs, what was the lower limit of the model? There must be one.

Dr Henry—I understand what you are saying. Conceptually there is a lower limit; obviously there is a lower limit of zero, but it would be absurd to think that there is an even distribution of possibilities between

90,000 and zero. Obviously we think that the distribution we are talking about is heavily weighted to the 90,000 end of probable outcomes. As for the sensible range to talk about, we did not calculate that.

Senator FIELDING—On page 19 of the UEFO you say:

The Commonwealth Social Housing ... will translate into about 15,000 jobs ...

You did not say ‘up to’ but ‘about’ 15,000 jobs. Before you said you had aggregate levels of GDP that translated into jobs, but now all of a sudden you have an individual component. Could you go through the components that you think will make up those 90,000 jobs? Could you also you take on notice my question about the range in these calculations?

Senator JOYCE—Where is the top of the bell curve?

Dr Henry—The top of the bell curve, if you want to put it in those terms—

Senator JACINTA COLLINS—Is it a bell curve?

Dr Henry—Probably not, but even if it were the top of it would be very close to 90,000.

Senator FIELDING—Could you take my question on notice about breaking up the jobs in the package into components? You have done it for one, so I am sure your model will be able to do it roughly for the others. If, say, by the end of Monday there is a view that there may be a better component, how long would it take to model that change? How long would it take to model each component if they changed? Did any of them change along the way, and how long would it take to recalculate the model for a component?

Dr Gruen—It depends how big it is. If it had a material impact on the forecasts then it would be a major exercise. If you are just talking about some small component then it would be a much smaller exercise.

Senator FIELDING—What was the latest change in the components that were estimated? Obviously the government has come up with some components and you have modelled them. I am particularly interested to know how long it would take you to model them if they changed. Would it take, say, a day if it were non-complex?

Dr Gruen—In principle, if we were asked to do modelling on a different set of components in the package we could do it in a couple of days.

Senator JOYCE—If 90,000 is the top of the bell curve then it should go up to a number far higher than 90,000.

Dr Henry—I did not say 90,000 was the top of the bell curve. I said the top of the bell curve would be very close to 90,000. If it is a bell curve we are talking about something with very small dispersion.

Senator JOYCE—How are we going to pay this money back? At the end of the day, when we are hocked up for \$200 billion—and I looked through your discussion of efficiency in the economy, which, I imagine, means putting people out of rather than into work—how are we actually going to pay this money back?

Dr Henry—The government has set out its fiscal strategy in the UEFO and has indicated that it remains committed to:

- achieving budget surpluses, on average, over the economic cycle ...

Having gone into deficit, that implies surpluses of some magnitude when the economy returns to a stronger period of growth. The government has also indicated that it remains committed to:

- improving the Government’s net financial worth over the medium term.

So the net debt would be repaid out of future budget surpluses.

CHAIR—Dr Henry, Dr Watt and your colleagues, thank you very much for appearing before us.

Committee adjourned at 10 pm