CHAPTER 1

Introduction

1.1 On 5 February 2009, the Senate referred the provisions of the following bills to the Finance and Public Administration Committee for inquiry and report by 10 February 2009:

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

1.2 On the same day, the Senate also referred the provisions of the Appropriation (Nation Building and Jobs) Bill (No.2) 2008–2009 relating to the social housing program to the Community Affairs Committee.

Conduct of the Inquiry

1.3 Details of the inquiry, the bills, and associated documents were placed on the Committee's website. As of Monday, 9 February 2009, the Committee had received 29 submissions which are listed in Appendix 1. Appendix 1 also lists additional information received by the Committee. Submissions were placed on the Committee's website for ease of access by the public.

1.4 In referring the provisions of the bills to the Committee, the Senate directed the Committee to hold hearings on 5 February, 6 February and 9 February 2009 respectively. A list of witnesses who appeared at the hearings is at Appendix 2.

1.5 The Committee thanks those departments, organisations and individuals who gave evidence at the hearings at very short notice for their cooperation and willingness to do so. The Committee is also grateful to those organisations and individuals who made submissions within the tight timeframe.

1.6 The Committee would also like to thank the Department of Parliamentary Services for producing the proof Hansard Transcripts in a very short time.

Context of the Inquiry

1.7 Australia faces an unprecedented global financial crisis as the majority of countries go into recession. The massive collapse of the United States subprime mortgage market has plunged the global economy into crisis. There is a major downturn in world trade which has led to a slump in consumer and business confidence. Australia is not immune to the crisis. The Government must act decisively to protect the national interest by strengthening the economy in order to protect the financial security of Australian families and businesses.

1.8 The International Monetary Fund's (IMF) October 2008 *World Economic Outlook* described the world economy thus:

> The world economy is entering a major downturn in the face of the most dangerous financial shock in mature financial markets since the 1930s…The situation is exceptionally uncertain and subject to considerable downside risks. The immediate policy challenge is to stabilize financial conditions, while nursing economies through a period of slow activity and keeping inflation under control.[1]

1.9 Dr Ken Henry, Secretary of the Treasury gave his assessment:

> 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.[2]

1.10 Mr Klaus Schmitt-Hebbel, Chief Economist of the Organisation for Economic Coordination and Development, stated that 'in normal times, monetary rather than fiscal policy would be the instrument of choice for macroeconomic stabilisation. But these are not normal times' and that central banks should also cut rates further.[3]

1.11 Mr Greg Evans, Australian Chamber of Commerce and Industry (ACCI), also commented:

> ACCI strongly supports the government's stimulus package and its attempt to lift aggregate demand across the economy. Such is the scope of our current economic difficulties that this package, combined with monetary easing, is absolutely essential. The size of the package at two per cent of GDP in 2009 is appropriate and in line with our own estimate of what is required.[4]

1.12 Anglicare Australia, Catholic Social Services Australia, The Salvation Army and UnitingCare Australia, in an issues paper on the impact of the global financial crisis on social services in Australia, noted that:

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1 International Monetary Fund, *World Economic Outlook*, October 2008, p.xv, http://www.imf.org/external/pubs/ft/weo/2008/02/pdf/text.pdf (Accessed 7.02.09).

2 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.13.

3 Mr Klaus Schmitt-Hebbel, Chief Economist of the Organisation for Economic Coordination and Development, 'A Long Recession: Managing the global financial crisis and economic downturn', *OECD* Observer, no 270-271, Dec 2008-Jan2009.

4 Mr Greg Evans, ACCI, *Committee Hansard*, 9.2.09, p.4.

> Some sectors in the financial markets have shut down altogether and others are simply dysfunctional. The capital markets, where financial intermediaries and companies borrow money to fund their investments and, increasingly, their day-to-day running costs, are most notably affected. Risk premiums demanded by lenders have jumped and even creditworthy borrowers are having trouble obtaining sufficient funds. All companies and households are affected.[5]

1.13 The Mid Year Economic and Fiscal Outlook 2008-09 (MYEFO) released by the Treasurer and the Minister for Finance and Deregulation on 5 November 2008 commented that the global financial crisis had 'entered a new and dangerous phase'. While Australia was better placed than most other countries to withstand the fallout, it 'was not immune from the effects of the global financial crisis and the global downturn'.[6]

1.14 In response, the Australian Government took action to strengthen the economy and support Australians including the $10.4 billion Economic Security Strategy (ESS), a $300 million program to build local community infrastructure, a $15.2 billion Council of Australian Governments (COAG) funding package and the Nation Building Package announced in December 2008.[7]

1.15 On 3 February 2009, the Updated Economic and Fiscal Outlook (UEFO) was released. The UEFO noted that the outlook for the global economy had deteriorated sharply since the MYEFO, with the IMF cutting its forecast for global growth and now forecasting a deep global recession.[8]

1.16 In relation to the Australian economy, it was stated that 'the weight of the global recession is now bearing down on the Australian economy. Growth is expected to be significantly weaker than previously anticipated and unemployment will be higher.'[9] In addition, the sharp fall in global commodity prices is compounding the impact on Australia.[10]

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5 Anglicare Australia, Catholic Social Services Australia, The Salvation Army and UnitingCare Australia, *Submission 5*, p.6.

6 The Hon. Wayne Swan, MP, Treasurer and the Hon Lindsay Tanner, MP, Minister for Finance and Deregulation, *Mid Year Economic and Fiscal Outlook 2008-09*, 2008, p.1. http://www.budget.gov.au/2008-09/content/myefo/html/index.htm (Accesed 7.02.09)

7 The Hon. Kevin Rudd, Prime Minister of Australia, *$42 billion nation building and jobs plan*, Media release, 3 February 2009, p.2.

8 The Hon. Wayne Swan, MP, Treasurer and the Hon Lindsay Tanner, MP, Minister for Finance and Deregulation, *Updated Economic and Fiscal Outlook 2008-09*, 2009, p.1. http://www.budget.gov.au/2008-09/content/uefo/html/index.htm

9 UEFO, p.1.

10 UEFO, p.12.

1.17 On 3 February 2009, the Australian Government announced a $42 billion Nation Building and Jobs Plan (the plan) over 4 years to provide immediate support for jobs and growth. In the UEFO it was stated that:

> Without this significant and timely policy stimulus, Australia would face a more severe slowdown than forecast. With the Nation Building and Jobs Plan, economic growth is only expected to slow to 1 per cent in 2008-09 and ¾ of a per cent in 2009-10. With slower growth, the unemployment rate is forecast to rise to 7 per cent by June 2010.
>
> The Nation Building and Jobs Plan has been crafted to strike the right balance between supporting growth and jobs now, and delivering the lasting investments needed to strengthen the economy for the future.[11]

And:

> Doing nothing is not an option. It is becoming increasingly apparent that, while still important, monetary policy action alone will not be sufficient to restore growth in demand within a reasonable time period. The Government's swift action ensures that fiscal policy, along with monetary policy, is clearly targeted at supporting economic growth and jobs.[12]

1.18 Key measures of the plan highlighted by the Government include:

- free ceiling insulation for around 2.7 million Australian homes;
- build or upgrade a building in every one of Australia's 9,540 schools;
- build more than 20,000 new social and defence homes;
- $950 one-off cash payments to eligible families, single workers, students, drought affected farmers and others;
- a temporary business investment tax break for small and general businesses buying eligible assets; and
- significant increase in funding for local community infrastructure and local road projects.[13]

1.19 The following day, the six bills were introduced in the House of Representatives to implement the plan, the objective of which is to 'support jobs and invest in future long term economic growth':

> By investing in jobs and long term economic growth the Plan strikes the right balance between immediate support for jobs now, and delivering the long term investments needed to strengthen future economic growth.[14]

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11 UEFO, p.1.

12 UEFO, p.9.

13 The Hon. Kevin Rudd, Prime Minister of Australia, *$42 billion nation building and jobs plan*, Media release, 3 February 2009, p.1.

Key Issues

1.20 A number of concerns and questions were raised during the course of the inquiry in relation to the Nation Building and Jobs Plan bills including:

- Australia's position in the current financial crisis;
- the size of the plan and the choice of measures;
- the multiplier effect of the plan's measures;
- the implementation lag;
- the employment effects;
- the proposed increase in the borrowing limit governing the issue of Commonwealth Government Securities; and
- the effectiveness of cash payments as opposed to tax cuts.

1.21 The proposed increase in the borrowing limit governing the issue of Commonwealth Government Securities and the effectiveness of cash payments as opposed to tax cuts are discussed in Chapters 4 and 5 respectively.

Australia's position in the current financial crisis

1.22 Dr Ken Henry provided the Committee with an overview of the prospects for the global economy:

> 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…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.[15]

1.23 Dr Henry also commented on the Australian economy:

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14 The Hon. Kevin Rudd, Prime Minister of Australia, *$42 billion nation building and jobs plan*, Media release, 3 February 2009, p.1. http://www.pm.gov.au/media/Release/2009/media_release_0784.cfm, (Accessed 7.2.09)

15 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.7.

> 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.[16]

1.24 Dr Henry went on to comment that Australia's performance is due to very careful management of the Australian economy over a long period of time with respect to both macroeconomic policy and microeconomic reform; effective regulation of the financial system; and the benefits which have flowed from the run-up in commodity prices that accelerated at the end of 2003. Dr Henry concluded:

> 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.[17]

1.25 UEFO provided a forecast of gross domestic product (GDP) of one percentage point in 2008-9 as compared to real GDP growth in 2007-08 of 3¾ percentage points. The forecast for 2008-09 takes 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' and 'is well below trend growth for the Australian economy and which explains fully why, in our forecasts, we have the unemployment rate increasing'. Dr Henry noted that in 2009-10, the forecast is for 'even weaker gross domestic product growth of only three-quarters of one percentage point'.[18]

1.26 Dr Henry continued:

> 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.[19]

1.27 Dr Henry concluded that 'these are highly unusual circumstances and we have advised government…that there is a need for fiscal policy action and that it is quite urgent'.[20]

16 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.7.

17 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.7.

18 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.7.

19 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.8.

20 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.15.

Size of the Nation Building and Jobs Plan

1.28 Given the size of the package, concerns were raised during the inquiry that the plan was too substantial or should have been staggered over a longer period of time.[21]

1.29 The UEFO stated that:

> The Nation Building and Jobs Plan is intentionally large — it reflects the seriousness of the challenges being faced and the need to build a strong economy for the future. By avoiding measures that lock in long-term spending, the Government is well-positioned to take action to begin to return the budget to surplus as soon as the economy starts to recover.[22]

1.30 The Australia Institute put the plan's size into the international context:

> While in absolute terms the $42 billion package (over 2.3 years) is very large, it is less than two per cent of GDP in 2009 and 2010. It is important to view projected government deficits in relation to both the size of the Australian economy (the total deficit is 2.8 per cent of Australia's $1.2 trillion GDP in 2009–10) and the size of the fiscal deficits in the US (eight per cent) and the UK (8.5 per cent). Most EU member countries will also have deficits well in excess of three per cent of GDP due to the adoption of stimulus packages and the average for advanced economies in 2009 is seven per cent.[23]

1.31 Similarly, Mr Greg Evans of the Australian Chamber of Commerce and Industry noted:

> In looking at this issue, we reviewed what was happening internationally and the size of various fiscal packages. We looked at the UK and the USA, which are partly analogous, although the depth of their economic decline has certainly been a lot greater than ours. Indeed, their fiscal stimuli has been greater than ours. So we thought, on balance, around two per cent of GDP was appropriate and, in 2009, that is basically what this package delivers.[24]

1.32 The Committee heard evidence from a number of economists who provided a range of views to the Committee.

1.33 In response to questions as to why the package was substantial when Australia is in a much better financial position in comparison to other countries Mr David Tune, Department of the Prime Minister and Cabinet, stated that:

> I guess it is a matter of trying to think forward. The objective of the package is to get in ahead of the game, in a sense. Looking at the

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21 See for example D. Tones, *Submission 7*, p.1.

22 UEFO, p.17.

23 The Australia Institute, *Submission 6*, p.1.

24 Mr G Evans, Australian Chamber of Commerce and Industry, *Committee Hansard*, 9.2.09, p.8.

> projections that the Treasury had produced on where they thought the Australian economy was going, the view was taken that it would be sensible to get in ahead rather than wait and see what actually happens. Those forecasts may or may not turn out to be correct; we will see. But, based on the best information that was available to us in the department, that was the basis of the advice that we were giving to the government around that time in conjunction with the other central agencies. Really, it is a question of whether you wait and see or whether you get in ahead of the game. On this occasion, the government obviously decided to get in ahead of the game.
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> The size of the fiscal stimulus and the period of time over which it occurs are also very important here. If you take into account what the government did in December last year in the ESS, the economic stimulus package, and what is being done in the current package, you are probably looking at up around three per cent of GDP. It is in line with the sorts of averages there in other countries that you have been talking about. I think it is really a matter of trying to act in advance of need. It is preventative to a large extent.[25]

1.34 Mr Tune also noted that most advanced countries are doing 'fairly substantial fiscal stimulus programs at the moment'. The IMF recommendation or view is that fiscal stimulus should be at least two per cent in calendar year 2009, which is around the figure of Australia's package.[26]

1.35 Officials were questioned as to whether a smaller package, $12 billion or $21 billion, would not have achieved the same outcome. In response, Treasury Secretary, Dr Ken Henry stated that the proposed $42 billion plan would result in GDP growth whereas a smaller plan may well leave GDP contracting in 2009–10:

> … we estimate that as a result of this package…GDP growth will be around half a per cent higher in 2008-09 and around ¾ 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.[27]

1.36 On the other hand, doubling the package amount would not necessarily result in a doubling of the impact on GDP. Dr Henry also commented that 'one would have to start worrying about the capacity issues':

> 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,

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25 Mr D Tune, Department of the Prime Minister and Cabinet, *Committee Hansard*, 6.2.09, p.26.

26 Mr D Tune, Department of the Prime Minister and Cabinet, *Committee Hansard*, 6.2.09.

27 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.090, p.28.

> 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.[28]

Government's Balance Sheet

1.37 A number of senators raised questions about the impact of borrowing on the Government's balance sheet. The Government will need to borrow to fund the Nation Building and Jobs Plan to support the economy and jobs. However, the Government's balance sheet remains in sound shape, particularly when compared to other comparable economies.

1.38 As economist Mr Saul Eslake, stated 'the levels of public debt projected in the Updated Economic and Fiscal Outlook are not excessive or alarming by either Australian historical or international standard'.[29]

1.39 The UEFO forecasts that general government net debt will rise to 5.2 per cent of GDP in 2011-12. This is around the average net debt levels that have prevailed over the past three decades and compares to an average net debt across OECD member countries of more than 45 per cent of GDP.

Composition of the package

1.40 The UEFO provided a chart showing the projected impact of the package on aggregate demand as well as the relative contributions of earlier stimulus measures.[30]

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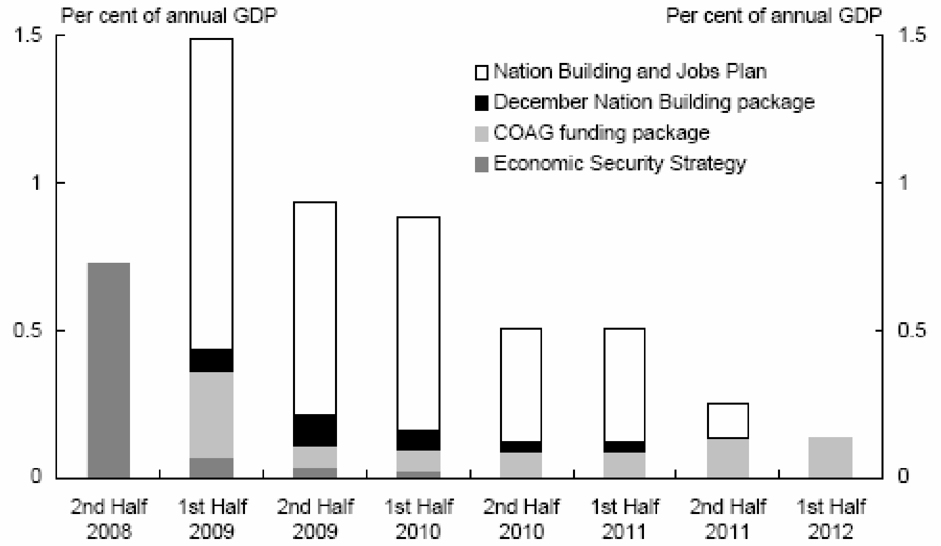
28 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.29.

29 Mr Saul Eslake, *Committee Hansard*, 9.2.09, p.37.

30 UEFO, p.11.

Chart 2.1 shows the fiscal stimulus package provided by the Australian Government.

Chart 2.1: Fiscal stimulus packages delivered by the Australian Government[(a)]



(a) Impact on underlying cash balance as a per cent of annual nominal GDP.
Source: Treasury.

1.41 The UEFO stated that as a result of the plan, GDP growth will be around half per cent higher in 2008-9 and around three-quarters to one per cent higher in 2009-10.[31]

1.42 There was considerable discussion during the inquiry concerning the composition of the package. This went to the use of a tax bonus instead of tax cuts (this is discussed in chapter 5) and the balance between the various elements of the plan, including the timing of the impact.

1.43 Dr David Gruen, The Treasury, commented on the way in which the plan has been framed:

> 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.[32]

31 UEFO, p.17.

32 Dr D Gruen, The Treasury, *Committee Hansard,* 5.2.09, p.11.

1.44 Dr Henry reinforced the need for the plan to address immediate problems:

> The problem we are dealing with at the moment…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… 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.[33]

And:

> 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.[34]

1.45 This point was also noted by Mr David Tune, Department of the Prime Minister and Cabinet:

> The key focus was to try and get immediate stimulus. That is what it is about, and that is why there was a mix there of cash payments, including a tax offset, and infrastructure—mainly community infrastructure because it is very fast to get going. The whole intent of this package is to try and get stimulus during the course of 2009.[35]

1.46 Table 2.1 of the UEFO provides the key components of the plan and impact for the years 2008-09 to 2011-12. The impact of the capital projects lifts after 2009-10 while direct payments to families have an immediate impact. The implementation lag is shorter for direct transfer payments to households and longer for direct government spending.

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33 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, pp 18–19.

34 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.25.

35 Mr D Tune, Department of the Prime Minister and Cabinet, *Committee Hansard*, 6.2.09, p.31.

Table 2.1: Key components of the Nation Building and Jobs Plan

	Underlying cash balance impact				
	2008-09	2009-10	2010-11	2011-12	Total
Building prosperity for the future					
Building the Education Revolution	-987	-8,624	-5,109	0	**-14,720**
20,000 Social and Defence Homes	-260	-4,274	-1,794	-312	**-6,640**
Energy Efficient Homes	-39	-1,540	-1,544	-736	**-3,859**
Small Business and General Business Tax Break	0	-840	-1,350	-515	**-2,705**
Black Spots, Boom Gates and Community Infrastructure	-480	-410	0	0	**-890**
Sub-total	**-1,766**	**-15,687**	**-9,797**	**-1,563**	**-28,813**
Supporting jobs now					
Tax Bonus for Working Australians	-6,950	-1,201	0	0	**-8,151**
Single-income Family Bonus	-1,273	-147	0	0	**-1,420**
Farmer's Hardship Bonus	-20	0	0	0	**-20**
Back to School Bonus	-2,347	-271	0	0	**-2,618**
Training and Learning Bonus	-413	-98	0	0	**-511**
Sub-total	**-11,004**	**-1,717**	**0**	**0**	**-12,721**
Total Stimulus Package	**-12,770**	**-17,404**	**-9,797**	**-1,563**	**-41,534**

1.47 Dr Ian Watt, Secretary of the Department of Finance and Deregulation, commented on the table and stated that:

> 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.
>
> …
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> 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.[36]

1.48 Dr Henry also explained:

> 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.[37]

36 Dr I Watt, Department of Finance and Deregulation, *Committee Hansard*, 5.2.09, p.12; see also Dr K Henry, The Treasury, *Committee Hansard*, 5.2.06, p.19.

37 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p. 25.

1.49 In answer to questions on why there was a need to implement the plan in one stage, rather than some parts at a later time if required, Dr Henry commented:

> 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.[38]

1.50 A number of Senators raised the question of whether cash vouchers would be a more effective means of ensuring immediate cash flow into the economy as opposed to one-off cash bonuses.

1.51 In response, Dr Henry stated:

> I am just trying to illustrate why there is a difficulty with the voucher proposal—then surely a household that could only access the $950 through a voucher arrangement would simply spend that $950 and reduce spending by an equivalent amount elsewhere in their income. That is, if you thought that the whole $950 was going to be saved unless you had a voucher mechanism then surely what the household would do is take the voucher, spend all the money and save another $950 part of their income. To put it another way, money is fungible.[39]

1.52 Treasury officials were questioned on the choice of measures in the plan, particularly in relation to infrastructure projects including why infrastructure projects that would overcome bottlenecks for the export industry and spending on the Murray-Darling Basin were not included while spending has been directed to assembly halls and sports centres. In response, Dr Henry highlighted that such projects would not enable prompt infrastructure expenditure required to address the deficiency of aggregate demand which the plan was specifically designed to address.[40] He further noted that:

> 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

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38 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.25.

39 Dr K Henry, The Treasury, *Committee Hansard*, 9.2.09, p.53.

40 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.14.

> 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.[41]

1.53 Dr Henry made similar comments in relation to other infrastructure projects raised in the evidence.[42] Dr Henry also addressed the notion that there is 'a very large volume of supply enhancing infrastructure projects out there on which government expenditure could be undertaken tomorrow'. He commented that 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'.[43]

The multiplier effect of the plan's measures

1.54 Questions were raised during the inquiry as to the rationale of the combination of measures proposed under the plan and the strength of the multiplier effect of such measures.[44] The Treasury indicated that the multiplier would be a half to one, but there was uncertainty about the magnitude.[45] Dr Gruen stated:

> …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.[46]

1.55 Dr Gruen continued:

> We can make a broad comment on that which is 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

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41 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.13.

42 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.18.

43 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.19.

44 For a discussion of multiplier effects see, *Nation Building and Jobs Plan – Interim Bills Digest*, Parliamentary Library, 6 February 2009, no 92, 2008-09.

45 Dr D Gruen, The Treasury, *Committee Hansard*, 5.2.09, p.11.

46 Dr D Gruen, The Treasury, *Committee Hansard*, 5.2.09, p.16.

> of that dollar. You probably get a larger multiplier for infrastructure spending.[47]

1.56 Dr Henry noted that leakages, such as to savings and spending on imports, occur and detract from the direct impact of the measure:

> 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.[48]

Employment effects

1.57 Treasury officials noted that when economic growth is forecast to be below trend, the unemployment rate is forecast to rise. The UEFO states that the plan will help 'support and sustain' up to 90,000 jobs over the next two years but 'notwithstanding the solid boost provided by the fiscal stimulus, the unemployment rate is forecast to reach 7 per cent by June 2010'.[49]

1.58 Treasury indicated that the figure of 90,000 was based on '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'.[50] Dr Henry commented:

> …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.[51]

1.59 Dr Henry concluded that the 'biggest risk to unemployment in Australia is the deficiency of aggregate demand emerging'.[52] The plan is aimed at increasing aggregate demand which will impact positively on employment. Mr Tune also commented that:

> This package does protect jobs; there are no two ways about it—it supports jobs. There are issues there about other people who will lose jobs. Yes, that is what happens in these sorts of situations. The existing income support system is there to assist those people. The Job Network is there to assist those people. Both those programs are demand driven, so there is no dollar constraints on whether people can gain access to those payments or gain

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47 Dr D Gruen, The Treasury, *Committee Hansard*, 5.2.09, p.41.

48 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p. 24.

49 UEFO, p.6; see also Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.22.

50 Dr D Gruen, The Treasury, *Committee Hansard*, 5.2.09, p.16.

51 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.22.

52 Dr K Henry, The Treasury, *Committee Hansard*, 5.2.09, p.23.

> access to the services of the Job Network. So all of those things are there. The Prime Minister said yesterday that in conjunction with the states he would like to work through what more can be done in those particular areas. So that is an issue under active consideration at the moment.[53]

1.60 In response to concerns raised about a rise in unemployment, Mr Grant Belchamber of the Australian Council of Trade Unions (ACTU) stated:

> The package as a whole is directed at supporting economic activity and avoiding the increase in unemployment that would otherwise occur. The cash payments are at the front end of the package, with the infrastructure spending to follow on from them. We think both parts are absolutely critical in assisting currently unemployed Australians to find work and in preventing job losses amongst currently employed Australians. On the whole, the package delivers substantially in the interests of unemployed Australians and those employed in firms that find the going tough over the coming year.[54]

1.61 Mr Frank Quinlan representing major Church providers noted of the plan:

> The Rudd Government's Nation Building and Jobs Plan is not designed as a rescue package for the community sector or for unemployed people. It is a rescue package for the nation as a whole which focuses on creating and maintaining jobs.[55]

1.62 Whilst Ms Hatfield Dodds of the Australian Council of Social Service (ACOSS) raised concerns about assistance to the unemployed, she stated that ACOSS supports the plan for seeking to 'prevent unemployment from rising even more rapidly'.[56]

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53 Mr D Tune, Department of the Prime Minister and Cabinet, *Committee Hansard*, 5.2.09, p.38.

54 Mr G Belchamber, ACTU, *Committee Hansard*, 9.2.09, p.15.

55 Mr F Quinlan, Major Church Providers of Social Services in Australia, *Opening Statement*, pp2–3, Tabled 9.2.09.

56 Ms L Hatfield Dodds, ACOSS, *Committee Hansard*, 9.2.09, p.21.