

Back in the black with a touch of restraint

May 12, 2010

Peter Hartcher

Sydney Morning Herald

Rudd has sidestepped his two fears of being painted as a big spender and getting into debt.

The Rudd government has turned the time-honoured artform of the election-year budget on its head. Instead of buying votes with big spending, it is trying to win our trust by exercising restraint.

Telling us that it is giving us nothing and we should be grateful for it, the Rudd government is recalling the Greek historian Thucydides: "Of all manifestations of power, restraint impresses men most."

Kevin Rudd and his Treasurer, Wayne Swan, are motivated by fear, the fear that the opposition will succeed in portraying them as traditional Labor big spenders.

And as it happens, their political fear happens to align perfectly with the financial fear now stalking the global market - a newly awakened terror of government debt.

The two sets of fears have come together in happy coincidence to produce a budget for our time. It's a time that the chief investment officer of the world's biggest bond investment firm, Mohamed El-Erian of Pimco, calls "a significant regime shift in advanced economies with consequential and long-lasting effects".

Swan said last night that the credit crisis that has forced Greece to its knees "is a really stunning reminder" of the risks that lurk in the world economy. Impressing on us the restraint that the government has exercised, he said that it met "the highest standards of responsible economic management".

He unveiled a budget deficit for next year of \$40.8 billion, which is \$6 billion smaller than expected just six months ago. The culmination of smaller deficits ahead means that the government has promised to return the budget to surplus in three years, which is three years earlier than previously forecast.

The truth is that the natural recovery in the economy has done all the hard work for the Rudd government. Its attempts at cutting spending are embarrassingly feeble. From total outlays of more than one-third of a trillion dollars, it has cut spending by just \$1.4 billion.

The real hero of the budget is neither Rudd nor Swan but a very low-profile fellow named Mr Parameter Variations. This hard-working chap, whose father is a faster economic recovery and whose mother is fast-rising commodity prices, has done all the really hard work in the budget.

These so-called parameter variations have delivered a net increase of \$8.9 billion to the budget balance next year, according to the budget papers. In other words, it is an effortless improvement for the government.

Or, in football parlance, the goalposts have moved, allowing the government to claim a goal despite displaying no real game skills.

A former budget analyst with the federal government, Stephen Anthony of the consultancy **Macroeconomics.com.au**, last week published an estimate that the "parameter variations" would allow the government to declare that peak debt would be only \$91 billion in 2012-13, less than half the \$200 billion projected a year ago.

Swan last night announced that peak debt would be \$93.7 billion, very close to Anthony's calculation.

"Overall, this government's record on spending is very poor - it's addicted to spending," says Anthony. Yet while the government doesn't deserve credit for the rigour of its cuts to spending, it does deserve recognition for its restraint.

In the approach to an election, it's customary for governments to open the spending spigots and break the bank in the conviction that we'll be pathetically grateful for being given a larger lick of our own money.

John Howard was increasingly convinced of the effectiveness of this approach. In his last four years in power, the Treasury calculated that he handed out 94 per cent of the revenue windfall gains delivered by the commodity boom.

The limitations of Howard's approach were starkly demonstrated in 2007. As he announced ever-bigger handouts in the panicked approach to the election, he opened an opportunity for Rudd.

Rudd promised to spend less than Howard - "this reckless spending must stop!" - and was instantly hailed for his prudence.

It sealed his claim to be an "economic conservative".

But now, after last year's epic stimulus spending, Rudd is anxious to recover this title. Rudd plans two big themes for his re-election campaign this year - health and hospitals reform, and responsible economic management. Sure, the budget delivers what Swan describes as "modest relief" for "working families", that hallowed constituency to which the Prime Minister prays every night for re-election.

But by allowing the natural recovery in revenues to flow to the treasury and not out to the voters, Rudd is shoring up his claim to sound economic management. And, happily, this is strengthening Australia's position in the world.

In 2007, Australia had the ninth-strongest fiscal position among the 30 nations of the OECD. This budget should put Australia in fifth place. The world markets are these days impressed by restraint. Rudd prays that the Australian voter is too.