

Dear Prudence: the WAPF Shadow State Budget 2009-10

Executive Summary

- There is now a developing hole in the WA State finances despite the Barnett government's sensible cuts to flagship projects as recommended by WAPF last year. Revenues from taxes to the State Government have fallen faster than expected whilst State government expenditures have continued to increase.
- More budget cuts are therefore required to avoid an unacceptable level of State debt. Expenditure on nurses and teachers provides a larger employment multiplier than on roads and flagship projects that may not now be needed for a decade or more. The time to take an axe to the roadbuilding programme in WA is *now*.
- Now quite evidently is not the time to cut taxes – possible negative bracket creep is one reason - but equally obviously they should not be raised except in very specific cases.
- Royalties for Regions is a good idea in principle but has become a pork barrel in practice. It needs looking at carefully when every cent spent needs to be spent well.
- The Government should still adopt a five-year target for the introduction of market pricing of electricity, and then water, but with targeted rebates for those who need them eg pensioners and single parents. A range of environmental incentives through grants (and where not practicable, on taxes) should be introduced.
- On the bright side, existing medium term revenue projections are for a range of reasons probably too pessimistic. Even in these tough times, combining judicious tax rises with targeted expenditure can achieve the goal of maintaining WA's AAA rating whilst simultaneously addressing many urgent public needs.
- But this can *only* be achieved if some more sacred cows of development are sacrificed. Crossing your fingers and hoping that the turnaround will happen soon is not a prudent – or, in the long term, even a tender – way to run the State's finances.
- Complete transparency is required for trust to be maintained between the people of Western Australia and its government. At this time failure to release important documents such as the results of the Audit Committee and the State Infrastructure Strategy are to say the least unhelpful.

This second WAPF Shadow Budget¹ is accompanied by a WAPF summary projection of how the State finances could look over the next four years if WAPF's projections are accurate and its budget recommendations were accepted.
www.wapolicyforum.org.au

¹ This Shadow Budget has been put together by a group led by Julian Roche

Introduction

The sands in the hourglass have now run out, and rather faster than expected. According to the WA Department of Treasury and Finance (DTF), projected economic growth in WA is now 3.5% in 2008/9². Economic growth is expected to slow further in 2009-10 – 3.25%. Even this looks remarkably optimistic, considering that Australia's economy as a whole shrank by 0.5% in the last quarter of 2008 and can be expected to have shrunk again by a similar, or larger, amount in the first quarter of 2009. If this trend were to continue until the end of 2010, the total fall in output and potentially revenue would be in the region of 5%. It is entirely reasonable to forecast flat output during 2008/9 and even a fall in the succeeding financial year. It is widely known that DTF forecasts are being trimmed regularly and the Budget can expect to contain the most pessimistic forecasts for the WA economy for a decade.

Already the State is running a deficit. According to the latest (January) data from the DTF, revenues for the first seven months of FY 2008/9 were up 7.2% (including the period of high commodity prices that has evidently now ended) whilst expenses were up 12.5%. The operating surplus fell to \$750 million, \$432 million lower than the \$1,182 million surplus recorded for the same period in 2007-08. The picture for the full twelve months, WAPF expects, will be grimmer still by comparison to previous years. WAPF thinks the eventual net operating balance for 2008/9 will be around \$1.2bn, more or less where the MYR of December 2008 said it would be and half the previous year. And already there is an alarming Treasurer's advance of \$1.2bn, without which apparently the WA Government would have struggled to pay wages³.

This is despite the fact that the Liberal-National Government has done exactly what WAPF recommended should be done last year: taken the building of a new football stadium off the agenda for two years, scrapped the Carpenter government's East Perth museum plan and rejected Labor's plans for the Perth foreshore in favour of a more modest redevelopment with greater private sector involvement and investment and hence less State government expenditure required now⁴. It is an awful trajectory.

Yesterday's Remedies

The WA Chamber of Commerce and Industry appears to believe that the key to successful control over public sector expenditure includes the introduction of performance agreements with agency heads; meaningful and measurable key performance indicators for them and their agencies which should be agreed and published annually; and the development of a clear strategic direction, and key performance measures, for service areas. This would all be expensive to implement, hard to agree, and subject to rapid change over the next few years. Evidence from the UK suggests that frequently such KPIs can wreak havoc with the flexibility the public

² Compared to 5.5% at the time of the Pre-Election Financial Statement

³ <http://www.abc.net.au/news/stories/2009/04/06/2536407.htm>

⁴ <http://www.abc.net.au/news/stories/2009/04/02/2533108.htm>

sector requires to do a good job (eg a single-minded focus on reducing hospital waiting times can lead to inadequate resource distribution in the health sector) and moreover there is little evidence to suggest that WA's public services are inefficient in the first place. The further suggestion that the Government should consider options for contracting out services to the private sector, privatisation of agencies is another of yesterday's remedies: as the sorry saga of Public-Private Partnerships indicates, when the going gets tough, the banks get bailouts and contractors plead for renegotiated contracts to stave off bankruptcy, so the very purpose of contracting out is completely negated. Now, when credit is scarce, is surely not the time to launch an ambitious program of privatization.

Difficult choices

The real choice in practice now is between greater borrowing, raising taxes, cutting expenditure or a combination of all three⁵. WAPF recommends a combination aimed at preserving the welfare of the less well-off in WA whilst continuing to invest in the future of the State in partnership with the private sector where possible. Now is not the time to be running a record capital works program⁶. It is a time to be prudent⁷.

Yet what is completely missing from the State Government's approach is a realization that the recession is likely to affect the poor and underprivileged in WA completely disproportionately. WAPF argues that any cuts in State expenditure should be subjected to a social as well as an environmental impact assessment to minimize the impact on the less wealthy in WA. There therefore remain huge areas of State expenditure which either cannot or should not be cut. Likewise tax raises should be concentrated on those best able to bear them: the rich. And any additional borrowing needs to be carefully scrutinized in order to ensure that it can be incorporated within cyclical planning that will not jeopardize the State's hard-won AAA credit rating and place at risk the welfare of future generations.

WAPF Shadow Budget - overall

WAPF assumes that 2008/9 is a matter of forecasting Government decisions already taken; our projected Budgetary decisions are now made for subsequent years. We believe however that the DTF has exaggerated necessary spending from 2009/2010. WAPF continues to believe that inflation will be greater than the DTF allows for in its projections. WAPF also believes that the effect of the beginning of economic recovery will start to feed through into State government revenues from the end of 2010.

⁵ No doubt this is what the Treasurer's Audit Committee told him, if only we could see the report.

⁶ According to the state authority, Western Australia has \$7.7b worth of capital works already underway, an increase of \$1.7b on 2007.

⁷ Several economics consultancies have taken a sharply different view. Lateral Economics, for example, has taken the view that cost savings should come from recurrent expenditure rather than infrastructure investment.

The WAPF Shadow Budget therefore involves more drastic spending cuts in aggregate than does the DTF, but this combined with revenue revival has the effect of *retaining* the State’s AAA credit rating throughout the period of the downturn. This can be done: but it requires a fairly drastic reassessment of what WA will look like in four or five years’ time – a return, in fact, to the vision of WA that was popular a decade ago, and not the exaggerated expectations of growth in every direction that came to characterize both popular and government thinking over the last decade, especially the last few years.

Revenues

WAPF is *much* more optimistic about revenues in the medium term than is the DTF, which has a history of guarded pessimism about the State’s economic growth.

	250 7/8	223 1/9	1	182 8/11	167 7/12	154 10/13
M Y R 07/08	18516	19315	19991	20179	N o t forecast	N o t forecast
WAPF 08	18513	19867	21447	23178	25445	N o t forecast
M Y R 08/09	19345	20039	20297	20461	21001	N o t forecast
WAPF 09	19345	20079	21605	23262	25440	27900

Why?

Going forward, the State Government believes that GST grants will fall as WA becomes a victim of its own success⁸. Commonwealth GST grants are only one half of the picture, moreover. The Commonwealth provides a host of other grants. Estimates of GST grants have declined by \$682m from pre-election forecasts. In the 2008/9 MYR, DTF assumed that “Western Australia’s share of national GST revenue is projected to decline from 9.4% in 2007-08 to 5.7% by 2011-12, well below the State’s population share of over 10%. This represents ‘lost’ revenue of around \$6.0 billion over the forward estimates period compared to if Western Australia received its population share of the GST pool”. WAPF believes that this is politically infeasible. WAPF projects that COAG will take measures to prevent such an imbalance occurring to this extent, and also that the forecast itself is suspect – previous DTF estimates of GST revenue have been consistently lower than outturns. WAPF has suggested that

⁸ In fairness it should be pointed out that Commonwealth expenditure on WA’s infrastructure rose also....

GST grants remain approximately constant throughout the Shadow Budget period at around \$3.5bn annually.

Looking further ahead, the Treasury itself has suggested that each US1c fall in the value of the Australian dollar adds \$30m to the revenue of the State Government, and that the A\$ will average about US\$95c over the forecast period. The continuing strength of the Australian dollar, when combined with falling commodity prices, is the cause of the especial problems of today: but

Payroll tax

The WA Chamber of Commerce and Industry's view is that taxes should be cut further. Their specific target is payroll tax. No one likes paying taxes, especially business. But the State's finances are sufficiently precarious already that cutting taxes in the current economic environment would not be sensible economics. In their 2008/9 Budget Submission, the CCI suggested a 0.5% cut in payroll tax. This would have translated, in the absence of compensating expenditure cuts, into a reduction in the critical debt/revenue ratio. This would have been irresponsible.

There is another reason why tax cuts during this particularly deep recession would be irresponsible – negative bracket creep. The CCI argued that whereas in 2003, the small business exemption would mean that a typical business could employ 15 staff before it had to start paying payroll tax, this had fallen to 11 by 2008 when average wages reached \$67,000. If average wages fall, however, then this number rises again. It would therefore make sense for both reasons to wait another six months at least before taking any action at all on payroll tax. WAPF's projections assume no further cuts in payroll tax.

Property taxes

The housing market, the Treasury says, has been 'weaker than expected'. It is important to remember what this means in terms of State revenues: that the volume of transactions declined faster than expected and therefore Stamp Duty revenue was less than forecast. It is clear enough where the problem lies: the correlation between property value decline and transaction volumes has not been properly understood.

The State Government continues to raise a proportion of its revenues from taxes on land. Land tax assessments have increased at the same time as the property market has slumped, which has infuriated many landowners. Whilst it is doubtful they would have raised a similar objection when taxes lagged increased land values – indeed they did not – there remains a strong case as the CCI has suggested for land tax to be conducted on a five-year rolling valuation basis rather than on a single year in arrears. This might help to smooth revenues as well as reduce antagonism to the tax.

Vehicle duties

The Treasurer observed last year that distorting the tax system for policy purposes was on the whole an unsatisfactory policy route. Better, he argued, to use a grant system. Most economists would agree with this as a general rule: but in the case of motor taxes, for instance, to introduce afresh a grant system for 'green' motorists would be expensive and unnecessary. It would be simpler to incentivise motorists through a revision to the motor tax system. This has already been done elsewhere⁹. Part of the objective of the State taxation system must be to ensure that whatever taxes are removed from individuals and corporations' incomes, the effect on their subsequent expenditure patterns is as far as possible not to detract from their spending in Western Australia itself, but to reduce expenditure on overseas goods and services. Environmental levies on flying would also fall into this category, insofar as the State is able to interfere with this. WAPF has presumed that motor vehicle duties rise at a modest 5% over the forecast period.

Expenditure

It is certainly hard to disagree with prudence. But what are the prudent decisions that the State Government should be taking? Traditionally it has always been argued by Keynesians that government expenditure should rise in a recession, providing counter-cyclical employment and injecting demand into the economy, and be cut in a boom, enabling a catch-up on debt repayment to take place and preventing any 'crowding out' of private sector expenditure. There are several reasons why the State Government in Western Australia should be cautious in accepting this analysis wholesale.

(a) As argued below, forecasts of expenditure and revenue may be in error. Over-enthusiastic spending in a recession, when the state's credit rating is at stake, may be ill-advised. The CCI says that 'the forecast deterioration in the state's financial position over the forward estimates reinforces the need for the Government to be prudent in its investment decisions to ensure net debt levels do not threaten this key financial target'¹⁰.

(b) The expenditures themselves, especially at a time when social priorities are changing rapidly, may not be a cost-effective allocation of scarce resources. There is little doubt that falling employment is one of the key economic problems WA now confronts. Several steps have been taken at Commonwealth level to try to mitigate job losses, ranging from the stimulus package itself to a curb on 457 visas. The State should be considering how its expenditures best sustain employment.

(c) Infrastructure expenditure in particular is very long-term. Projects launched now may end up costing the most at precisely the wrong time.

⁹ Any Australian examples yet? If not use UK

¹⁰ ¹⁰ Chamber of Commerce and Industry, *2009-10 Pre-Budget Submission to the WA Government*, p5

The background is scarcely encouraging. Salaries have increased by 75 per cent (or almost \$3 billion) since the beginning of the decade, amounting to \$6.9 billion in 2007-08. The percentage of the State budget allocated to salaries has also increased steadily, reaching 41% in 2007-08. The Treasurer's response to this has been to say that public servants whose employment agreements expire after July 1st will only be eligible for pay increases of between 8.2 and 9.3 per cent over three years¹¹. This is a scattergun approach which runs the risk of alienating large parts of the workforce.

Similarly, the Liberal-National Government claims to have placed a ceiling on the size of the public sector at around 99,000 full-time equivalent posts. But the problems relate to the size of public pay awards – attempts to catch up with burgeoning private sector pay-packets awarded during the boom – and payments to consultants. Placing a constraint on the absolute number of public sector posts can often lead to expensive outsourcing and consultancy contracts. There is nothing intrinsically wrong with increases in public sector employment, nor in public sector pay. But it depends on who they are. Virtually everyone agrees that frontline services such as nursing and teaching need ever greater numbers of staff as the population grows (and ages). What is more difficult to understand is why the number of administrators in Departments needs to grow at a similar rate.

In this context, how does the Treasurer's across-the-board 3% cut in Departmental expenditures sit? Firstly, this is an astonishingly crude measure. It does not distinguish between crucial and inessential projects, and focuses savings on current, rather than capital, expenditure. Secondly, it does even seem that it is working. Scarcely a day seems to go by without announcements that expenditure by the State Government is increasing rapidly and apparently without any control, despite the fact that the Treasurer has insisted on across the board cuts of 3%. For example and most notably, DG Peter Flett disclosed in March that the budget of WA's Health Department was 'expected to blow out by up to \$230 million this financial year'¹²

Are they sure?

The WA Chamber of Commerce and Industry has suggested 'a spending growth target which aims to ensure that growth in general government spending does not exceed the rate necessary to match growth in prices and population'¹³ but this begs the question: the State Government does not know what future price and population growth will be, yet it must take spending decisions for years to come – and moreover on the basis of forecasts which have often proved off the mark.

A Comparison of the mid-year General Government Sector Expenses Forecasts with the WAPF 2007/8 Shadow Budgets

¹¹ <http://www.abc.net.au/news/stories/2009/04/01/2531860.htm>

¹² <http://www.abc.net.au/news/stories/2009/03/18/2519934.htm>

¹³ Chamber of Commerce and Industry, *ibid*, p12

	250 7/8	223 1/9	1	182 8/11	167 7/12	154 10/13
MYR 07/08	16685	17449	18189	18925	No forecast	No forecast
WAPF 08	16628	18118	19659	21341	23181	No forecast
MYR 08/09	16837	18853	19574	20356	21362	No forecast
WAPF 09	16837	18874	19660	20480	21341	22243

What this shows in the first line is what DTF was forecasting in the mid-year review of 2007/8 – which was issued in December 2007 – compared with in the second line WAPF’s forecast for 2007/8 and Budgets for the next four years four months later. Notice how although DTF was able to predict the 2007/8 outturn quite closely, their forecasts changed dramatically in December 2008 to accord much more closely with WAPF’s forecast and Budgets made in April 2008. By April 2008, therefore, WAPF was able to project expenditure which accorded relatively closely in aggregate, at least for the 2008/9 and 2009/10, with forecasts of actual proposed expenditure made by the DTF at the end of the year. *Why was this?*

It was mainly that the future was becoming a lot clearer to predict. By April 2008 it had become clear that the DTF’s previous forecast for 2008/9 had failed to take into account blowouts in Government health and other sector expenditure. WAPF saw at least some of this coming back in April 2008. As for 2009/10, the knock-on effects of these blowouts, even with the projected 3% “efficiency” gains (read cuts) was always likely to push expenditure higher than the DTF’s original projections, even with the different expenditure priorities that WAPF envisaged. On the other hand, last year WAPF budgeted for greater expenditure from 2010-11 onwards, and this year that projected expenditure has been retracted in the light of the global recession.

Infrastructure Planning

The severe problem therefore with the superficially appealing idea from the CCI of a medium term infrastructure plan, ‘to provide a greater degree of certainty as to the likely future infrastructure projects that will be undertaken in the State and assist in depoliticising the prioritization process’¹⁴ is that whilst the apparent bipartisanship is to be welcomed the combination of rapid demographic and technological change combined with wide oscillations in the State’s budget position, partly as a result of lack of State control over its revenue base, could easily cause such a plan to be undermined.

What might be possible though, and would certainly be desirable, is an interactive online forward infrastructure structure, with the latest cost-benefit analyses visible for the WA electorate and the rest of the population to see, and comment on.

¹⁴ Chamber of Commerce and Industry, 2009-10 Pre-Budget Submission to the WA Government, p5

Representative democracy would not permit direct voting on infrastructural investment priorities, but distortions to the democratic will could be minimized this way as indicative State-wide and even local voting would be possible. WA could become the first Australian State to *show* its future infrastructure on line: roads, ports, railways, even broadband – and how much it will cost to achieve these goals. This presentation would also serve to assist inward investment, as investors would be able to see where WA will be going over the forthcoming decades. Over time snapshots of the view of the future could be compared with the reality, which may help to achieve the CCI's goal of depoliticisation as State Governments became increasingly reluctant to abandon such visible goals and targets. A good start would be the release of the State Infrastructure Strategy document that the Barnett Government has but is refusing to release. In whose possible interests can it be for such debate to be secret?

Every major infrastructure project undertaken by the State therefore needs a proper cost-benefit analysis, independent of political considerations, to justify it. The \$334m over the forward estimates and \$1.07bn over the next eight years for a new major stadium at Kitchener Park, in Subiaco, projected last year by the Carpenter Government should already be showing as savings. A West Australian poll showed that 70% of respondents were in favour of shelving the stadium anyway.

Perth foreshore development.

Grandiose, ugly, a potential environmental and planning disaster, poorly thought out and of entirely questionable net economic benefit to the State, in practice this dreadful plan will have to be postponed indefinitely anyway. Last year the Carpenter Government proposed spending of \$319million on the Perth Waterfront project (\$50.571million within the forward estimates). All that can be saved going forward. The Government can, and should, ensure that whatever waterfront development is eventually agreed is funded by the private sector, and viewed by the Government as an object of scrutiny and regulation, as well as an eventual source of taxation revenue – not an investment by the State Government. Just at the moment, it would probably be helpful if the Government were prepared to say now that the entire idea will be kicked into touch for the foreseeable future. A massive new development at a time of recession when occupancy rates are falling is hardly what Perth needs.

Health

The WA Health Department seems unable to make the cuts demanded of it and will apparently be running some \$250million over budget. There is of course a real need for a new childrens' hospital. Last year the Carpenter Government's last budget promised \$502million in 2008-09 on health infrastructure - an 84% increase on the year before. This amount must be reduced in the coming few years and a growth of such magnitude cannot be afforded. Yet expenditure on prevention and health promotion services as a proportion of total recurrent health expenditure has fallen progressively since 2003-04. As Professor Mooney has argued, these are very false economies.

Both the AMA and the Nursing Federation have already made clear that the standard of public health services will be affected by the proposed 3% cut. The Commissioner for Children and Young People has told a public hearing that WA's health service is short of 94 vital maternal nurses¹⁵ The message is clear: the current Government's plans involve a cut in healthcare provision which will have real adverse effects on the health of the population of our State. This ought not to happen in a State that has, despite the recession, such a high GDP per capita. It is not necessary. A 4% rise in health expenditure annually over the next four years will be sufficient to honour existing pay agreements, but it will be necessary to curb administration expenses which have risen alarmingly over the last five years.

Education

The Education Department has already revealed its budget is likely to blow out by \$50 million as thousands of additional students enrol in schools across the state. An increased use of mobile classrooms also testifies to additional need for space. WAPF's Shadow Budget assumes that education expenditure is held to a 2% rise for the next few years to reach \$5bn by 2012/13. This will be the hardest part of the State Government's expenditure to keep in check, as teachers' salaries rise as part of agreed deals. But input costs will be falling as a partial counterbalance.

Parents may have to be asked – temporarily – to make contributions, albeit on the basis of ability to pay. This approach may be necessary to maintain standards, and it will also serve to reduce the unhealthy gap that is rapidly developing between public and private schooling in the State.

Housing

As WACOSS has argued, the number of public rental dwellings in WA has now fallen to 1993 levels, despite an 18% increase in WA's population over the last 15 years. As a result, the current shortfall relative to the 6% social housing target is no less than 15,900 dwellings. At a steady increase of 2,380 dwellings per year, it would cost an impossible-to-afford average of \$758m per year for the next 15 years to reach 6% of all stock¹⁶. By contrast, the State Government has committed to building just 1000 public houses across the State – last year's budget commitment was \$212m. Is there any way to bridge this apparently impossible gap?

WAPF recommends that expenditure on public housing should not be reduced, but unfortunately there does seem little scope for radical expansion of the State's public housing budget beyond about 8% annually. It must therefore be spent cost-effectively.

¹⁵ <http://www.abc.net.au/news/stories/2009/03/18/2519934.htm>

¹⁶ *Putting the Pieces Together*, WACOSS Pre-Budget Consultation Report on the WA State Budget 2009-2010, p15

One point is that this commitment is going to be carried out at a time when housing demand is actually falling and when bank repossessions are increasing dramatically. Given that it is beyond the financial capability of the State to prevent repossessions, more sensible perhaps would have been to allocate these scarce resources to buying houses auctioned after repossession, which would help stabilize the Perth property market as well as represent better value for money and even in some cases provide a route for homeowners in desperate straits to convert from ownership to renting.

Roads

The idea that road construction ‘will see WA through the economic crisis’ is preposterous and repulsive. WA Governments, of whatever political hue, do still seem to think that more roads are part of the answer to the recession: \$810 million was budgeted in 2008-09 alone for roads. It says its investment in road construction include the major projects at Bunbury to improve port access and safety, improved freight access in the Perth metropolitan area, particularly between the Canning Vale industrial area and Fremantle Port and a \$20million allocation to finalise planning and start construction of the Roe Highway extension from Kwinana Freeway to Stock Road¹⁷. All of these should be seriously considered for the axe. More candidates for postponement are all the projects identified by the CCI: the Bunbury Outer Ring Road, the Port Access Road a flyover at the Eelup Roundabout – duplication of the Mandurah Entrance Road and construction of the Pinjarra Bypass as Peel priorities - all good ideas to postpone. At the absolute least, the many companies that will benefit from the WA Government’s proposed investments should be asked to make special contributions to public funds in proportion to their potential economic benefits from such environmental desecrations.

Of course it is good news that the Perth-Bunbury highway may well have come in at slightly less than the originally budgeted \$705m, but this should perhaps be compared with whether it succeeds in the equally original aim of cutting 30 minutes off the trip between Perth and Bunbury without yet more expenditure on feeder roads. Roads breed traffic. And it may be an exception – taking the Mt Barker northern bypass as an example, at one stage it was commented that whereas its original projected cost was \$9 million this had now risen to more than \$13 million.

There are therefore several reasons why roadbuilding is the right target for immediate and substantial budget cuts.

1. *Slowing traffic growth suggests caution.* Demand projections based on economic growth expectations constructed before the recession will almost certainly now be exaggerations. For this reason alone many roadbuilding schemes should now be at least postponed.
2. *Spending on public transport is a better bet.* Alternative technologies and better use of resources, including public transport, may also be able to steal some thunder from roads over the coming decade. Environmental awareness -

¹⁷ <http://www.roadconstruct.com.au/Article/Road-construction-will-see-WA-through-economic-crisis-WA-Gov/472580.aspx>

and expectations of eventual fuel cost rises - are also now increasing to the point where individuals and companies no longer take unnecessary journeys¹⁸. Extrapolations of road use growth from the previous decade may prove inaccurate for these reasons also.

3. *Slow speeds and fixing Black Spots save lives.* The safety argument can be better achieved by the fixing Black Spots where possible and the imposition of dramatic speed restrictions on remaining Black Spots. And whilst a reduction of a few km/hr would not make much difference, slowing traffic down to 20-30 km/hr will cut deaths and serious injuries probably just as significantly than millions of dollars of expenditure.
4. *Shareholders do not need supporting.* Road expenditure, unlike for example direct spending on the WA health sector, involves a transfer of resources, in the form of profit, to the companies that construct roads. This profit is then in turn transferred to the shareholders of such companies. In a recession when financial resources are tight, it must be seriously questioned whether such a resource transfer is either necessary or desirable.

On the other hand it is deeply regrettable that the WA Government believes WA should be kept toll-free. On the contrary, this recession represents an opportunity for bold and decisive action to introduce tolls and congestion charges as ways of both raising revenue and encouraging the use of public transport. There is also a safety argument. The RAC called last year for \$50 million to be spent fixing black spots across the State, \$35 million for the continuation of the safer roads program, \$25 million for a program of safer intersection upgrades in the metropolitan area and \$75 million for upgrading dangerous country highways. That's \$185m in all, over say five years. Money well spent, especially if it could be raised by tolls at the very places where lives have been lost. This would combine speed reductions with revenue raising at precisely the points where both are needed.

Rail transport

WAPF presumes that the Government will keep its commitment to the extension of the northern suburbs rail line to Butler, but construct it on an extended timescale from that currently projected. WACOSS wants the State Government to commit to light rail, at a projected cost of \$10m per kilometer: the first phase of a scheme – connecting major transport nodes between the Fremantle and Armadale rail lines and the Midland and Joondalup train lines would cost approximately \$450m. In the current financial environment, a commitment of this kind may be hard to afford, although WAPF is projected expenditure of over \$1bn each year for the next four years and it might well be possible to include additional light rail within that quite considerable capital budget.

Police

¹⁸ And of course if WA is to retain and enhance its tourist and quality of life appeal, covering it with roads is not the way to go either.

Commissioner Karl O'Callaghan told the WA Parliamentary inquiry into budget savings that WA Police is required to find \$12.5 million in savings this financial year, but will fall about \$8 million short¹⁹. Most of the police budget is tied up in salary costs but he expects to make up the shortfall in future years by outsourcing some services. WAPF has presumed that police expenditure can be maintained at a growth rate of 6% over the next four years, but this is to admit that all the efficiencies WA Police are planning will just suffice to maintain existing levels of service. Ideally, expenditure should be increased and numbers raised, but it is hard to envisage that the budget will be available for this for several years yet.

Royalties for regions

The principle underlying the Royalties for Regions scheme is laudable. Regional WA of course deserves its fair share of State Government expenditure, and there are many communities, notably Native Australian communities, that could certainly benefit from highly targeted expenditure. Royalties for regions might have been quite a good idea in principle, but the way the Government has gone about it is different from what might have been expected. As it stands, however, throwing A\$300m at what the Government itself has described as “minor capital works throughout the State” is unlikely to be a cost-effective way to that will generate jobs, let alone stimulate investment or substantially improve amenities in regional communities.

A good example is broadband. Certainly, businesses in the regions need access to some form of broadband. Whether in the next five years they will find a deep urge to use videoconferencing, for example²⁰ or any other use of superfast broadband is quite another matter. Yet to deny its absolutely essential quality has now become tantamount to heresy. It is in fact quite conceivable that the National Broadband Strategy will eat up scarce resources and become, eventually, yet another example of misplaced resources. Older people especially need healthcare, and young people, jobs – not necessarily ever faster broadband services.

Energy, Water & Public Corporations

The State Government has also made what the Premier described as ‘the difficult decision to increase electricity tariffs for residential customers’²¹ – by 10% in April and 15% in July - and for business customers. The Government says that these increases, while regrettable, are an effort to stem the unacceptable level of Verve Energy’s losses, which could total \$1 billion over the next five years – and Synergy too. It does make sense, both economically and environmentally, for electricity to be fairly priced, and a period when gas and coal prices are not likely to rise dramatically is a good time to start. What is important is to ensure that poorer customers are not

¹⁹ <http://www.abc.net.au/news/stories/2009/04/02/2533242.htm>

²⁰ Apart of course from the ubiquitous Skype which does not need land broadband to work

²¹ <http://www.mediastatements.wa.gov.au/Pages/Results.aspx?ItemId=131474>

unfairly disadvantaged by these measures – the Government must press Synergy on this in the months ahead. WAPF has however presumed no change in these policies.

The long-term aim should be for the public corporations to be able to pay for such infrastructure investment *themselves*, from revenue – not from the public purse. For too long WA residents have been shielded from the costs of investment in infrastructure. For example in the last budget \$1.1bn was allocated for water infrastructure, including the start of work on the Southern Seawater Desalination Plant. The cost of water will rise inexorably in years to come, and using taxpayers as a piggy-bank for the necessary expenditure is both unfair, as usage varies greatly between taxpayers - and ultimately resource-distorting. Consumers ought to be paying more for these investments, and Government's responsibility will ultimately be to ensure that the less well-off are not prevented from being able to have the water they need. This will mean less disposable income for WA's citizens in years to come than in the boom years: but that is another reality best faced sooner rather than later.

There remains the matter of infrastructure investment. Last year the Carpenter Government proposed investment of \$1.2billion, focusing on safety and reliability and meeting the needs of what it optimistically described as the State's fast growing economy, including commencement of a \$295million 300kV transmission between Pinjar and Moonyoonooka, near Geraldton²², and \$50 million over four years to enable Verve Energy to initiate renewable energy projects. It follows therefore that if the State economy is not growing anywhere near as rapidly, a greater focus on renewable energy and a scaling-back – at the very least a postponement – of such intensive investments is required.

Community

WACOSS has consistently demonstrated that there is a raft of relatively inexpensive projects that could not only replace infrastructure investments in the short term to generate more employment, but which will also improve the life of WA's less fortunate residents. WACOSS's total 2009-2010 wish list amounts to \$1.37bn, less than 10% of State Government spending, and includes such highly desirable expenditure items as crisis and supported accommodation, housing services for vulnerable groups, expanded energy efficiency programs, and a series of measures to benefit Native Australians. Training is another State Government function: we all need to face the reality that, in common with most other places in the world, WA no longer faces a general labour shortage. Moreover, those jobs that continue to be advertised are mostly lower-paid, unskilled, and even part-time. This should not mean that the WA Government uses the recession as an excuse to walk away from its responsibilities for training. However, the interplay between temporary working visas and training expenditure needs careful scrutiny. Moreover, a Government's

²² A fresh cost-benefit analysis may be required on the proposed renewable energy plants in the Mid-West and their timescale. If private sector investment were obtainable this might still be a good idea

responsibility to its people extends to skilling them to work not only now, and locally, but in the future, and globally.

WAPF estimates that within its proposed budgets, by no means all of WACOSS's proposed programs will be achievable. Some would be, though, assisted by the cutbacks on infrastructure: especially the smaller projects, such as \$10m to provide cycle networks throughout the Perth Metropolitan region, \$5m for English language support programs (in turn likely to benefit social cohesion and reduce crime), and \$1.9m of increased funding to child care in WA, where almost 3000 children are in care.

The credit rating of the State

The Federal Government has acted to compensate the States for putting them at a disadvantage by guaranteeing wholesale borrowing by the country's banks, effectively lending them Australia's AAA rating. For triple-A rated states such as WA, the fee for the existing stock is 15 basis points and for new issuance 30 basis points.²³ This will give the states access to credit so they can proceed with projects that generate jobs. This measure is temporary, though: it does not remove the need for sound budgeting by the States – nor should it. How is WA shaping up and what can be done?

At present, WA is moving steadily towards losing its AAA rating. Already DTF's last quarter figures also show a near 25% rise in net debt to \$4.7 billion. In the DTF's last Mid-Year Review, the net debt to revenue ratio was projected to exceed the 47% target limit in both 2010-11 and 2011-12. This would be sufficient for the State to lose its AAA-rating from Standard and Poors, at least, as failure to adhere to the 47% target limit would certainly translate into a failure to maintain the ratio of 0.9 between gross revenue and net financial liabilities which would be required to keep Triple-A. Current evidence would seem to vindicate the DTF's pessimism that WA is indeed on this track. For starting from an impressively conservative net debt/revenue ratio of 0.17 in 2006/7, WA has already deteriorated dramatically in 2007/8 to 0.27 and WAPF predicts that in 2008/9 this will further fall to 0.34.

But this assumption is based on expenditure forecasts which, despite the 3% 'efficiency gain', do not dispense with any major sacred cows. Revenue forecasts are based on the assumption that there is no significant change in taxation either in how it's raised or how much. WAPF's four subsequent Shadow Budgets by contrast allow a more modest growth in expenditure – and, to be fair, for a more rapid growth in revenues, more consistent with previous history than the DTF forecasts. The result is that WA *can* retain its AAA rating and keep control of its finances in the recession, rather than creating a fiscal position that will be *extremely* difficult to reverse, as the current State Government plans imply.

²³ <http://business.smh.com.au/business/canberra-to-guarantee-state-debt-20090325-99z5.html>

	286 4/7	250 7/8	223 1/9	200 9/10	182 8/11	167 7/12	154 10/13
WA Govt	0.17	0.27	0.29	0.42	0.5	0.61	??
WAPF	0.17	0.27	0.34	0.33	0.42	0.41	0.44

WAPF's relatively optimistic assertion in these Shadow Budgets, however, are certainly largely dependent on the success of the State in growing its revenue base after 2009/10 along the lines of the WAPF projections in Table Revenue. The expenditures budgeted above rest on the assumption that State revenues grow along the lines projected in Table Revenue. What should the State Government do if they actually grow along the more pessimistic lines suggested by the Mid-Year Review? Should these prove unfortunately unable to achieve, then it will be necessary to cut expenditure still further, and introduce some further elements of charging, to maintain a conservative fiscal balance. The only justification for net borrowing that threatens the State's credit rating is if in the long term the expenditure provided contributes more to a better credit rating than do the short term savings.

Conclusion

It is worth remembering that WA has legislation designed to ensure that the State Government manages the State finances in the way this Shadow Budget suggests it should²⁴. GFRA 2000, Section 6, sets out the principles on which the State finances should be conducted:

- (a) funding for current services is to be provided by the current generation;*
- (b) spending and taxing policies are to be formulated and applied so as to give rise to a reasonable degree of stability and predictability;*
- (c) financial risks are to be managed prudently;*
- (d) spending and taxing policies are to be formulated and applied with consideration to the effect of these policies on employment and the economic prosperity of the State.*

Any deviation from these principles is to be 'temporary' and applied only in 'special circumstances'. That we have the latter seems hardly worth arguing; what matters is whether the Budget that the State Government is currently contemplating is a 'temporary' deviation from these four cardinal principles or whether, in fact, it will burden a subsequent generation of West Australians with an unacceptable level of State debt and represents a failure to provide 'a reasonable degree of stability and predictability'.

WAPF believes that the combination of budget cuts, especially on flagship projects, relatively unchanged tax levels, charging for some services and seeking to maximise the social and environmental benefits of all expenditure is the best route through this

²⁴ The Government Financial Responsibility Act 2000 (GFRA 2000)

crisis. The alternative may be to burden future generations with expensive debt for
redundant infrastructure.