Here are some alternative facts — not fake news, but quite bad

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Many think “alternative facts” are synonymous with fake news. But bringing to light alternative facts that are true can help balance a story. Such is the case with the recent federal budget. Several alternative facts about Australia’s fiscal position that to date have been largely ignored suggest a less sanguine view than that conveyed in the budget papers and commentary on them.

Consider the budget deficit measure — the shortfall between government revenue and expenditure — a macroeconomic variable of interest as it represents the government’s borrowing requirement.

All advanced economies, except Germany, Iceland and South Korea, are still running sizeable budget deficits after the global financial crisis. Collectively these deficits have exhausted a huge pool of private saving that could have been used to fund private investment. With this in mind, the private investment drought in Australia and other advanced economies is hardly a mystery.

Yet the fiscal drain on private saving stemming from annual budget deficits is just part of the story. The drain is significantly larger because budget deficits only convey the government borrowing requirement for the financial year in question, not the total government borrowing requirement in that year arising from maturing short-term debt because of previous budget deficits.

An interesting alternative fact is that Australia’s total budgetary financing need in recent years, inclusive of short-term debt falling due for repayment, has significantly exceeded actual budget deficits. You would be hard pressed to find this data in the budget papers but it’s readily accessible from the International Monetary Fund’s biannual Fiscal Monitor publication.

Whereas Australia’s budget deficit in 2017 on a calendar year basis was 2.4 per cent of gross domestic product, IMF estimates show the total government financing need, including maturing debt, was 3.2 per cent. A 3.6 per cent of GDP financing need is predicted for next year, almost three times higher than the budget deficit as a proportion of GDP.

In other words, the focus on the budget deficit alone as the indicator of the government’s call on domestic and foreign saving misses a major element. That the Australian government will continue to borrow significantly more than posted budget deficits in the near future because of past deficits implies a bigger negative for the economy.

That said, Australia’s total budgetary financing need in coming years is better than many other advanced economies, thanks to having a very low public debt position at the time of the GFC.

What stands out from IMF data is that the most moribund European economies tend to have budgetary financing needs that are much higher than their ongoing budget deficits. This is because those countries already had public debt overhangs going into the financial crisis that were compounded by recession and damaging fiscal stimulus. These include France, Greece, Italy, Portugal and Spain.

The standout advanced economy, however, is Japan, whose total government financing need in 2017 is estimated at more than 40 per cent of its GDP. Oddly, few economists ever draw the link between Japan's decades-long economic torpor and its public debt mountain. What it means is that Japan's high private saving is forever being recycled into low-yielding government bonds rather than directed to growth-enhancing private investment.

Meanwhile, what governments finance with borrowing is important. So it was a welcome development that this year's federal budget papers give greater prominence to the net operating balance measure, a "new" official alternative fact, publication of which is in line with budgeting practices adopted by Canada, New Zealand and the Australian states.

The net operating balance measure distinguishes between recurrent and capital spending and a deficit on this measure worsens the government's balance sheet as it reduces net assets.

A string of deficits by this measure has cumulatively totalled $354bn since the financial crisis, worsening the government's balance sheet accordingly, to the tune of negative 25 per cent of GDP — another unpleasant and much neglected alternative fact. Only future sizeable budget surpluses, not yet in prospect, can rectify this balance sheet problem as Julian Pearce and I show in "Fiscal Consolidation and Australia's Public Debt", published in the Australian Journal of Public Administration.

The published net operating deficits also confirm how delinquent successive ill-advised governments of both persuasions have been to borrow so heavily for unproductive purposes.

In addition, this year's budget stressed that government spending was on track to fall to 25 per cent of GDP by decade's end. Focusing on federal government spending in this way, however, ignores spending by other tiers of government in Australia and draws attention away from another alternative fact: that total government spending in Australia, at 37 per cent, is about 2 per cent higher as a proportion of GDP than it was before the crisis.

Though the share of government spending in Australia is close to the G20 advanced economy average — itself heavily weighted by debt-burdened European economies — it remains well above the average of about 20 per cent for the most competitive economies in the region: Hong Kong, Singapore and South Korea.

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