

Inside Canberra

Rob Chalmers - bringing you the latest business intelligence from inside Federal Government

From the Gallery

January 14th, 2011

• What will happen in Afghanistan this year? We know the US President will begin the draw down of troops, while Julia Gillard adopts a more aggressive approach. She insists Australia is in Afghanistan "for the long haul".

• Yes, but for what? The Australian public has never been given a clear idea of just why we have a token force in Afghanistan. Is it to bring western style democracy to the Afghans, or simply to drive out the Taliban? If so, neither of these outcomes are remotely possible.

• Malcolm Fraser says in some ways, the US-led coalition was in a dangerously similar position to the Soviets in Afghanistan. "You can make military gains in an area but then the Taliban fade away – they move somewhere else." Fraser – as most Liberals believe – has morphed from a cold war warrior PM, to soft pinko, environmentalist and charity head. He is not welcome in the Coalition lobby. That doesn't mean he is wrong.

• *Inside Canberra* wonders how we can be certain that the Afghans being trained for the Afghan army will take over security duty from the western troops. They could easily go over to the Taliban. Once the western forces leave, the Taliban will still be there. They live in Afghanistan. The old story will be repeated: in the long run the invaders are defeated by the combination of local resistance and time.

Rob Chalmers, Editor
Parliament House, Canberra
Tel: +61 (0)410 441 407
R.D.Chalmers7@bigpond.com

Govt highest priority is return to budget surplus

Long before the Queensland floods, the government last year was anxious to assure voters that the Budget would return to surplus by 2012/13 – it is "non-negotiable" the Prime Minister says. And she is still insisting this is so, even though the circumstances of the Budget have changed considerably. The Queensland flood disaster will hurt the bottom line. Reserve Bank board member, Professor Warwick McKibbin, told *The Age* that the Queensland floods could impact the economy by up to one per cent of GDP, or \$13 billion. And that was before the Brisbane flood. McKibbin said that the government's determination to bring the Budget back into surplus by 2012/13 was "dangerous". "Look at the size of the Queensland economy relative to Australia – at the moment a fair chunk of it has just stopped," he warned.

Coal industry hit hard in Qld

Trade figures released on Tuesday saw coal exports down five per cent in November as the rain tumbled down. ANZ economist, Katie Dean, says things will get worse before they get better with about 75 per cent of Queensland coal production already stopped. "Our initial estimate is the floods could drive a 25 per cent fall in coking coal export volumes and around a 9 per cent fall in thermal coal export volumes in January. This could see exports alone strip 0.5 percentage points from GDP in the quarter," she said.

Departmental budgets hard to cut

If Gillard is determined to meet the target date for a budget surplus, she will have to explain what areas of expenditure will be cut to cover the cost of assistance to Queensland. The Department of Foreign Affairs & Trade (DFAT) believes it will be hit hard in the coming May Budget – partly, some claim, because of icy relations between Treasurer Wayne Swan and Foreign Minister Kevin Rudd. DFAT expects a chop of up to \$45 million according to *The Age*. This is on top of the \$124 million cut to DFAT during Rudd's time as PM. Other departments may suffer, but not anywhere severely enough to make up for the cost of the Queensland floods to the Budget. In any case, Gillard would have a revolt on her hands from ministers if there are heavy across the board cuts to departmental budgets.

Taxpayers not pressing for surplus budget

The urgency of achieving a surplus by 2012/13 is lost on taxpayers, and the government knows this. For some reason, the government believes the promise must be kept to please 'the market'. Just why the market would be concerned about Australia is a puzzle to *Inside Canberra*. We have one of the strongest economies of the OECD, mainly due to our good fortune in export resources on a booming market that shows no signs of running out of steam. So important is the surplus budget that the government has rejected funding a world-class national research centre for climate and weather risk management, including floods, storms, cyclones and heatwaves. The Cooperative Research Centre for Climate and Weather Risk Tech-

Pig research favoured over new climate study

Abbott damned on dams

Experts dump on Abbott's scheme

Coalition in economy tangle

Gillard and Baillieu in agreement

nologies failed in its bid to gain \$37 million in federal funding, despite the backing of more than 50 local councils, the world's biggest re-insurance broker, Australia's biggest general insurance company, top universities and meteorology institutes in Australia, Britain and the United States.

Rosslyn Beeby, *The Canberra Times'* environment reporter, wrote that according to documents outlining the research centre's benefits, it had the potential to deliver "at least a \$1.68 billion return" over 10 years by reducing the impact of floods, tropical cyclones, heatwaves, storm surges and hail. Yet the Government could find \$20m to re-fund research into pork production. No doubt, pig production is worthwhile, but the future of the planet would surely outrank it. There are certain to be more embarrassing outcomes of the government's non-negotiable return to budget surplus.

Tony Abbott has made a bad start to the New Year, getting himself into a tangle over an area of policy he knows nothing about: management of rivers. Abbott insists Australia has to start building more dams and has set up a Coalition committee to implement this policy chaired by Andrew Robb, who also has no knowledge of river management. Apparently, Abbott has been inspired by Barnaby Joyce's beliefs in more dams, ignited by the flood threat to his home town of St George. Abbott remarked, "I just think it's a bit odd in a country with as many water issues that we've got that there have been virtually no dams built in the last two decades." It did not occur to him that the reason for the halt in dam building was because it no longer made sense to build them. Abbott's advocacy of dams has been immediately squashed by those whose business it is to know a lot about the subject.

For example, Willem Vervoort, professor of hydrology and catchment management at Sydney Uni, described the Abbott scheme as, "A misunderstanding of the natural system in Australia which goes from big droughts to big floods." Chief Executive of the Australian Water Association, Tom Mollenkopf, said he wouldn't be "rushing out with plans to build dams ... it just isn't going to be easy." Professor Richard Kingsford, Director of the Australian Wetlands and Rivers Centre at the Uni of NSW, pointed to the Murray-Darling system as evidence that building dams and taking water from river systems could have environmentally disastrous impacts. Jamie Pittock, a researcher at the Australian National University, says Abbott's idea is not smart. "You can either build a dam to store water for use, but if the dam is full of stored water it cannot catch a flood," he said. "If you want to build a dam to catch a flood, you have to keep that dam empty and then that doesn't store water. You can't have it both ways." Pittock says Australia has limited options for dams, and all the suitable sites have already been used.

Inside Canberra observes that as Abbott is opposed to government borrowing, he would obviously have to fund dams from current revenue. So here is the Abbott policy: reduce government debt to zero; always have budgetary surpluses; cut taxes (the principle source of revenue) and pay for dams from revenue. This will take some selling. On top of that the Coalition Leader is in disagreement over water with the Victorian Liberal Premier, Ted Baillieu. Abbott involved himself in the argument over the future of the Murray-Darling when Julia Gillard rejected calls from National Farmers Federation president, Jock Laurie, for more time to be taken over the Murray-Darling basin's rescue plan in the wake of the recent floods. Laurie said six months of strong flows into the river system "buys the government time to sit back and make sure they can get this right."

Gillard didn't accept this advice saying, "I think we've got to keep on time and we've got to deal with the water reforms we need for the Murray-Darling." She said that, although there were floods around the country now, the nation also regularly experienced drought. "So rather than just wait till the next drought hits the Murray-Darling, now is the time to get it right for the future, so

we will continue in 2011 to pursue our reforms through the Murray-Darling Basin Authority," she said. Abbott immediately declared the NFF was "absolutely right" to call for a pause. "Our general policy is that we support good policy, we oppose bad policy – and the current plan is not a good plan," he said. When Abbott's view was put to Baillieu, he disagreed, saying the floods were no reason to delay the Murray-Darling process. The Premier said there was still a long way to go in the COAG process on the issue, but the floods should not get in the way. "I don't think we should be diverted in a sense, by obviously what's a disaster in Queensland," he said.

Floods sweep away free market

Both major parties believe in the market economy, except that is, with the arrival of floods or droughts. Then there is a rush to look after farmers who own a commercial business, the success or failure of which is due to management. It is time for a national debate on disaster relief, or to put it another way, out of the ordinary weather patterns. Every farmer must surely have taken account of the prospect of bad seasonal conditions when buying their business. Why then is the taxpayer asked to bail them out? On a visit to the flood-hit Gascoyne region in WA, the Prime Minister found herself the target of abuse from some business owners who believed the government was not using taxpayers' money as freely in helping them as businesses hit by floods in Queensland. "Well, we need help just as much as Queensland," mango and banana plantation owner Jan De Boni said.

What about aid for Bondi?

It is apparent that many in the bush believe they have a right to be bailed out by the taxpayer to compensate for losses inflicted by the weather. We are not being flint hearted, but there are plenty of Australians in difficult circumstances who would welcome the offer of an interest free loan of thousands of dollars. The mango and banana plantation owner is no more justified in demanding help than the owner of a fast food takeaway in Bondi suffering because wet holidays are keeping people off the beach. The takeaway also caters for foreign tourists, so the proprietor is in the export business, yet the takeaway proprietor seeking weather related assistance would be spurned. Farmers can insure against floods and storms, as can householders and small businesses. Will the taxpayer therefore give only to those who have not insured and if so, why?

Assisting risk takers

If people made a decision to take a risk, that is their business. Moss Cass was Environment Minister in the Whitlam Government and, when a huge flood rolled down the Darling, he was asked what assistance would be given to farmers. Cass was castigated by the former Country Party when he observed, "Flood plains are for floods." As well as having to dole out millions to farmers, the taxpayer faces a massive bill just to restore public infrastructure in flooded areas, particularly roads. We believe there should be a review – perhaps not as grand as a Royal Commission – into dealing with natural disasters which are certain to become more frequent, the scientists say, as global warming advances. Perhaps a national disaster fund jointly financed by the Commonwealth and states could be established so that money is immediately on hand.

Bruce Hawker's economics absurd

Over the hols, your editor belatedly read Bernard Lagan's *Loner* – the sad account of Labor's experiment with Mark Latham. There were no new and startling revelations, but we found particularly interesting the advice offered by Bruce Hawker to counter the key element of John Howard's 2004 election campaign: the lie that interest rates would always be lower under a Coalition government than under Labor. Hawker had two ideas. One was for Latham to promise to resign as PM if he "failed to take steps" to keep rates down. This was obviously absurd and the voter would see through it. But Hawker's second option was for the Labor leader to promise a law which "would require a Latham government to keep the budget in surplus, and cut Commonwealth debt and federal tax collections – all designed to keep interest rates down." Lagan wrote: Hawker, Tim Gartrell, then ALP National Secretary and his deputy Mike Kaiser "believed it would be highly effective because it was brazen and original."

Fiddling with cash rate

Latham correctly ignored the Hawker plan. It is disturbing that Hawker, who advises the Gillard Government and state Labor governments, would be so ignorant in the area of federal economic policy. Firstly, there is no direct connection between the cash rate set by the Reserve Bank and budget surpluses, the level of government debt and federal tax collections. Interest rates are broadly decided by the level of activity in the Australian economy, which in turn is decided by a wide range of varying factors, not all capable of being influenced by governments. Hawker's proposal would have also resulted in a savage electoral backlash as services – such as health – were cut to meet the promised Budget surpluses. Hawker's law would have prevented the Rudd Government from providing the \$43 billion stimulus to the economy in the face of the global financial crisis. Putting the Budget into deep deficit undoubtedly saved the economy from a serious recession.

The Bob Carr legacy

It is notable that during the GFC, while the budget was in deep deficit, interest rates reached near record lows, which is the opposite to the outcome Hawker's theory predicted. Hawker was for nine years chief-of-staff to Bob Carr, NSW's longest serving Premier; a record attributable more to the incompetence of the NSW Liberals than the brilliance of Carr. He succeeded in eliminating all government debt, no doubt with the support of Hawker. As a result, Sydney is left with a derelict public transport system because of a lack of necessary investment. Carr also handed over Sydney toll roads to Macquarie Bank and other private sector investors. In the process, the Carr Government agreed not to upgrade alternate government roads, which could compete with toll roads. In turn, this has led NSW Labor to the disaster which faces it at the coming March election. Despite all this, Hawker-Britton flourishes.

Tax summit

There will be a tax summit, but don't expect too much. The tax summit is a nuisance and it's there because of Julia Gillard's success in negotiating with the cross benches after the election. Recall: of the three former Nationals, she got two – Oakeshott and Windsor, and Abbott got Katter and opposition. Oakeshott and Windsor wanted a tax summit and Gillard agreed. Now Treasurer Wayne Swan and his new Treasury head, Mark Parkinson, are trying to work out who should be at the summit and what it will be about. The government will go into the summit on the basis of no change in its broad economic objective of getting the Budget back into surplus by 2012/13. It's to be hoped that the summit will not be devoted primarily to whinges about too much tax. We doubt whether for most taxpayers, it is a big issue. Does the average wage earner even know what tax is imposed on his or her earnings? We doubt it.

How low can they go?

Those most interested in so called tax reform (meaning lower tax) have incomes exceeding \$200,000. The debate about taxes is the wrong way round. The initial step should be to set out what we need to build in long term infrastructure, such as railways, hospitals, schools and roads, which then should be funded by long term government borrowing. Ignore the absurd Coalition policy of insisting on zero government debt. We again quote the example of the Sydney Harbour Bridge, built on borrowings, opened by Jack Lang in 1932, with the debt not being retired until 1988. It has been of inestimable value to the NSW economy, but if Lang had adopted the approach of Abbott and Barnaby Joyce, it would never have been built. Once the long term infrastructure borrowing is settled (and this would have to be done under COAG) then the summit could look at the outgoings compared to revenue and decide whether education, public health and defence for example, should be cut to lower taxes, or if taxes should be raised to improve the delivery of these services. It is a fallacy to believe the community can have low taxes (we are already well down the OECD list of high taxed countries) and decent community services.

'Inside Canberra' - bringing you the latest business intelligence from inside Federal Government - is published every Friday, and is available by email subscription for A\$375 (inc. GST) for 46 issues each year.

The Newsletter is published by Phantom Media Pty Ltd. Correspondence should be addressed to:
Rob Chalmers, Room S89, Press Gallery, Parliament House, Canberra ACT 2600. Tel: +61 (0)410 441 407/Fax +61 (0)2 6280 0007

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