Briefing Paper:

Budget Analysis 2021-22: Heroic Assumptions and Half Measures

May 2021

The Commonwealth government has tabled its budget for the 2021-22 financial year. The budget will guide Australia's fiscal and social policies as the national economy (hopefully) continues to recover from the unprecedented hardship of the COVID-19 pandemic and recession. In delivering the budget, the Treasurer indicated the government's willingness to maintain or even increase program spending in some areas (while cutting spending deeply in others). He also committed the government to expanding fiscal support for certain human and caring services: including aged care, child care, and mental health. While an abrupt turn to austerity was avoided in this budget, overall program spending is nevertheless declining substantially: falling $60 billion this year (or around 3% of Australia's GDP) as COVID support programs are eliminated. And the new investments announced in some programs neither offset the contractionary impact of overall spending cuts, nor come close to meeting the real need for expanded services in any of these areas.

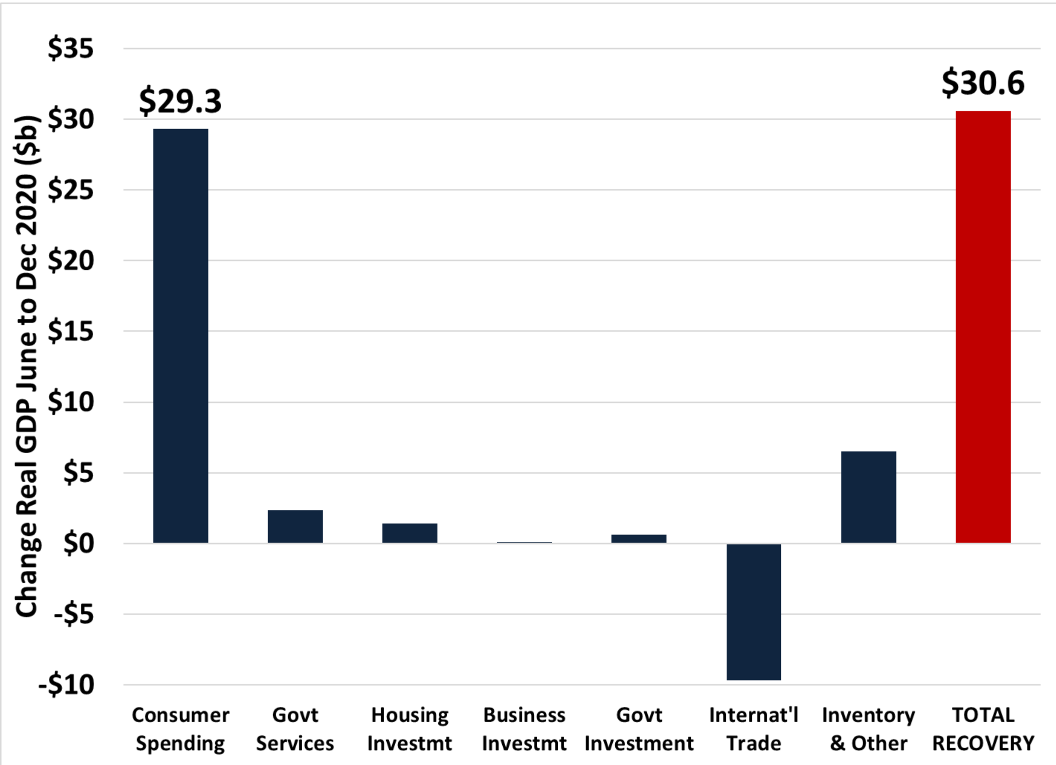
This briefing paper reviews the main features of the budget from the perspective of workers and labour markets. In particular, we consider in detail a major flaw in the overall macroeconomic logic underpinning the budget. The government is counting on a vigorous and sustained burst of consumer spending by Australian households to drive the post-COVID recovery. Yet the budget concedes that the main sources of income to finance expanded consumer spending (namely, wages and income supports) will remain weak or even contract. These two dimensions of the budget are fundamentally incompatible: the government cannot passively tolerate the grim reality of stagnant wages (and falling real wages), alongside major cuts in income supports, while still hoping that vibrant consumer spending can still lead the whole economy to recovery. Without active measures to stimulate stable jobs and higher wages, the assumed recovery underpinning this budget cannot be sustained. That casts doubt on its optimistic fiscal forecasts – and risks great damage to the well-being of Australians.

Counting on Consumers

The 2021-22 budget is based on a very rosy short-term economic forecast. It expects real GDP to roar forward by 4.25% in the next financial year – on top of the rebound that has already occurred since COVID-19 restrictions were largely lifted in mid-2020. Nominal spending (and hence government tax revenues) are boosted further by an expected acceleration of consumer price inflation. Those two optimistic assumptions both depend on the budget's expectation of a very strong expansion of consumer spending. It anticipates real consumer spending to accelerate by 5.5% in 2021-22. Again, this is *on top of* the rebound in consumer spending that has already been logged (in the latter months of the 2020-21 financial year) since the lockdowns were lifted.

Consumer spending has been at the heart of the encouraging but narrowly-based economic recovery that Australia has enjoyed since the worst of the pandemic last winter. Consumer spending rebounded vibrantly in the last half of calendar 2020. Australians were encouraged by our national success in largely controlling the spread of COVID. With retail and hospitality establishments open again, and pent-up demand strong, this burst of consumer spending was the main force behind new spending, job-creation, and recovering tax revenues for government.

Figure 1. Sources of Real Economic Growth, Second Half of 2020

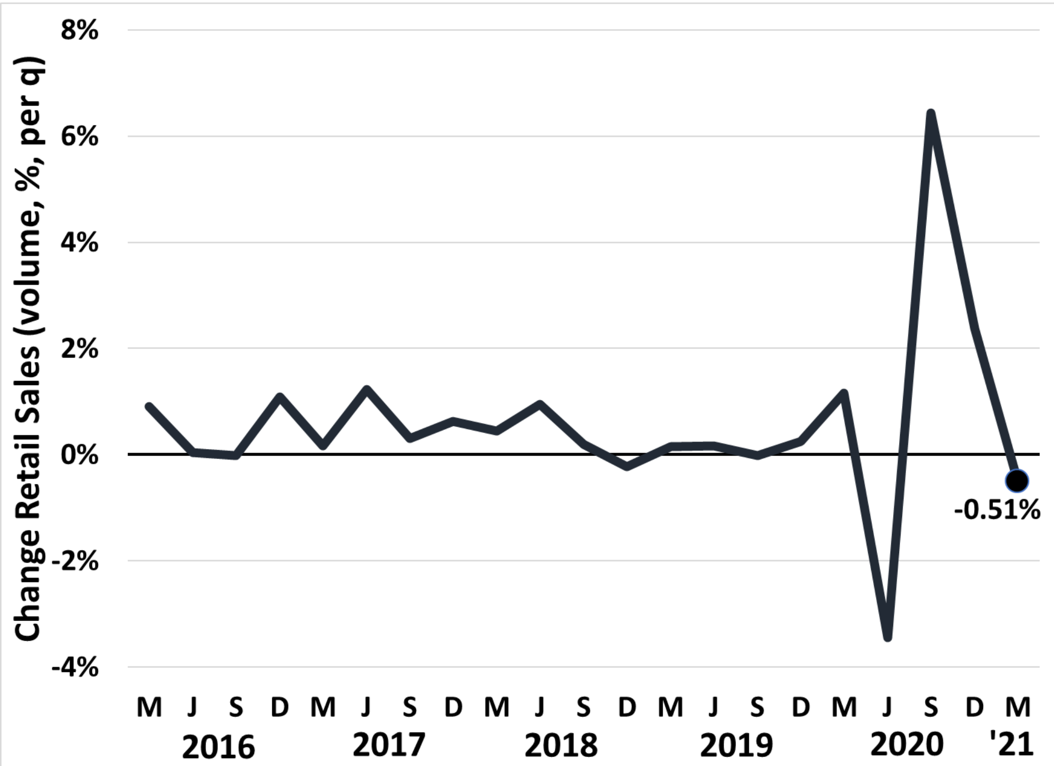


Source: Centre for Future Work from ABS National Accounts, Table 2.

As illustrated in Figure 1, real quarterly GDP grew by $30 billion during the second half of 2020, after hitting the trough of the recession in the June quarter. That welcome recovery, however, was almost completely dependent on strong consumer spending. In total, consumer spending accounted for 96% of the total rebound in real GDP in the first two quarters after the trough. To call this a consumer-led recovery is a massive understatement: there literally was almost nothing else growing. Other sources of expenditure and job-creation remained largely stagnant. Net exports actually contracted (in real terms). There was very little recovery in business investment, and even government infrastructure spending was weak – despite frequent ribbon-cutting ceremonies by government ministers announcing (or re-announcing) big projects.

Already there are signs that the strong rebound in consumer spending has reached its limit, and may even be poised for partial reversal. In fact, as shown in Figure 2, just days before the federal budget was released, the ABS reported that real retail sales in Australia declined in the first (March) quarter of 2021 – down 0.5% in that three-month period. The initial sharp decline in consumer spending during the lockdowns was followed by a record-breaking rebound in the September and December quarters. The fact that personal savings in Australia (in aggregate, but not for all individuals) increased during the pandemic (reflecting both the initial decline in consumer spending, and the success of major government assistance programs in offsetting the effects of job losses) boosted the recovery in consumer spending. So did a rebound in general consumer confidence, supported by Australia's relative success in controlling community transmission of COVID-19.

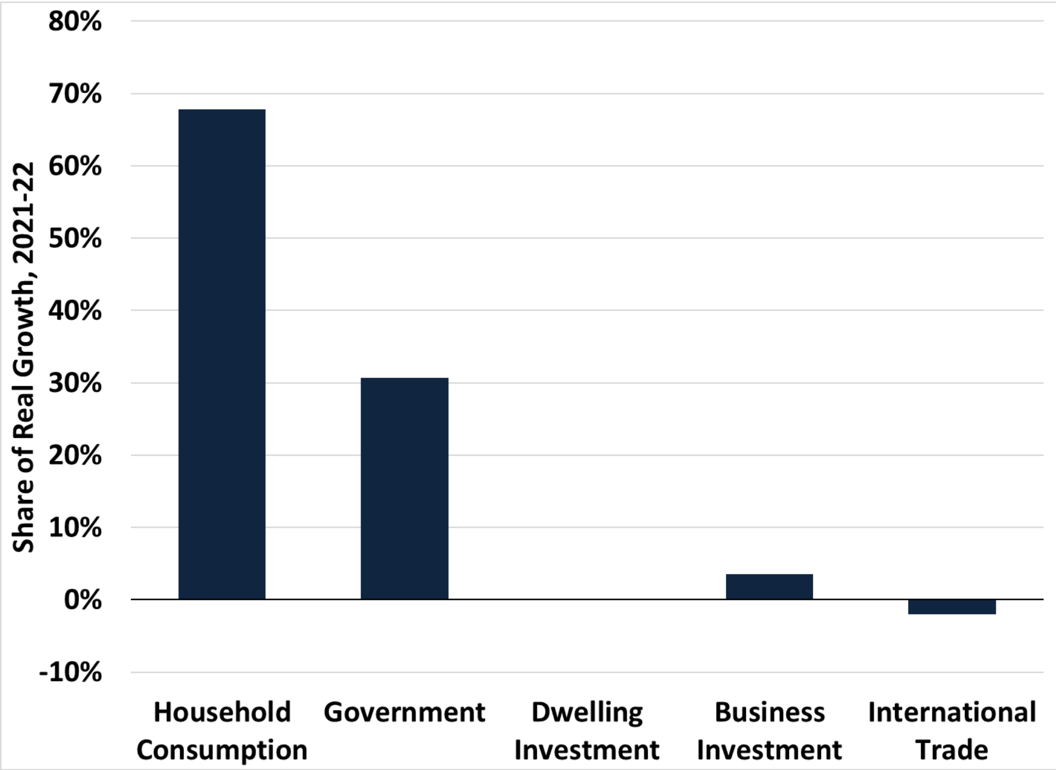
Figure 2. Quarterly Growth in Retail Turnover (Volume Terms)



Source: Centre for Future Work from ABS Retail Trade data.

However, that initial and exuberant rebound in consumer spending seems to be nearing an end. Consumers have 'caught up' to deferred demand, put on hold during the worst months of the lockdowns. They have drawn down savings that some were able to accumulate. (Not all Australians padded their savings during the pandemic: millions experienced negative savings as a result of job losses and, in many cases, exclusion from programs like JobKeeper or JobSeeker.) Yet the government expects real consumer spending to roar ahead by another 5.5% in real terms *next* financial year. Real consumer spending has not grown that quickly on a financial-year basis since 1998.

Figure 3. Assumed Sources of Real Economic Growth, 2021-22



Source: Centre for Future Work calculations from Commonwealth budget projections, Budget Paper #1, p. 37.

The government's prediction of rapid growth in consumer spending shows it expects the post-COVID recovery to continue to be dominated by Australians' willingness to open their wallets. In contrast, the government is downright pessimistic about other sources of growth in the coming fiscal year. It expects no change in residential investment, and an anemic 1.5% rebound in business investment (which hit a record low in 2020 as a share of GDP, despite the government's very expensive tax concessions).[1] The international trade sector is expected to again detract from growth next year (with imports, fueled by consumer spending, growing faster than Australia's exports). An increase in public sector consumption and investment (including by state and local governments) is expected to add to the recovery. But as illustrated in Figure 3, the government is assuming that almost 70% of real GDP growth in 2021-22 will come from one source: still more consumer spending.

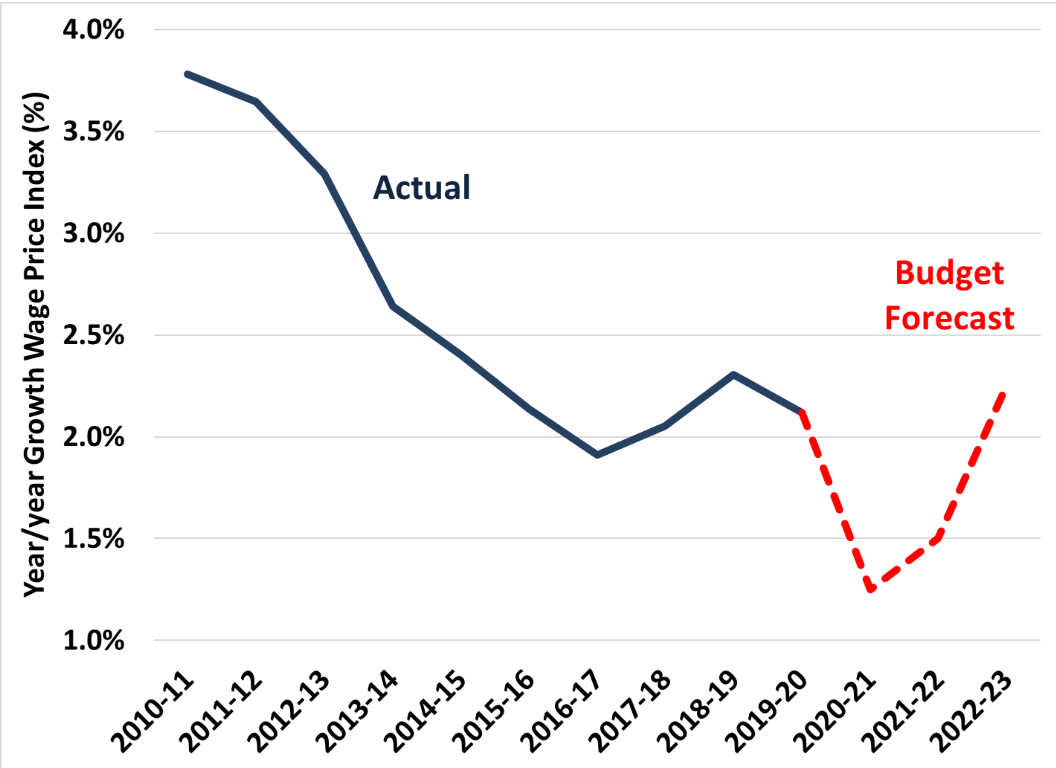
[1] The instant asset write-off policy, which allows businesses to expense 100% of the cost of a capital investment in the year it is made, was expected to cost $27 billion when it was first announced. It was then extended in the 2021-22 budget, with additional expense of $17.9 billion.

Where will that additional consumer spending come from?

Not from Wages

By far the most important source of personal income in Australia is wages and salaries. And there is absolutely no indication from the labour market that Australia's record-breaking string of weak wage growth is going to suddenly reverse itself. To the contrary, the 2021-22 budget seems to throw in the towel on the problem of weak wages. It expects year-average growth in nominal wages of just 1.25% by the time financial year 2020-21 comes to a close. That would set a new record for weakest annual wage growth in Australia's postwar history – coming on the heels of several years of record-weak wage growth already logged over the past painful decade. Then the budget expects only a very modest and gradual rebound starting next year: to 1.5% in 2021-22, and 2.25% (matching its historically weak pre-pandemic level) in 2022-23.

Figure 4. Budget Forecast of Wage Growth



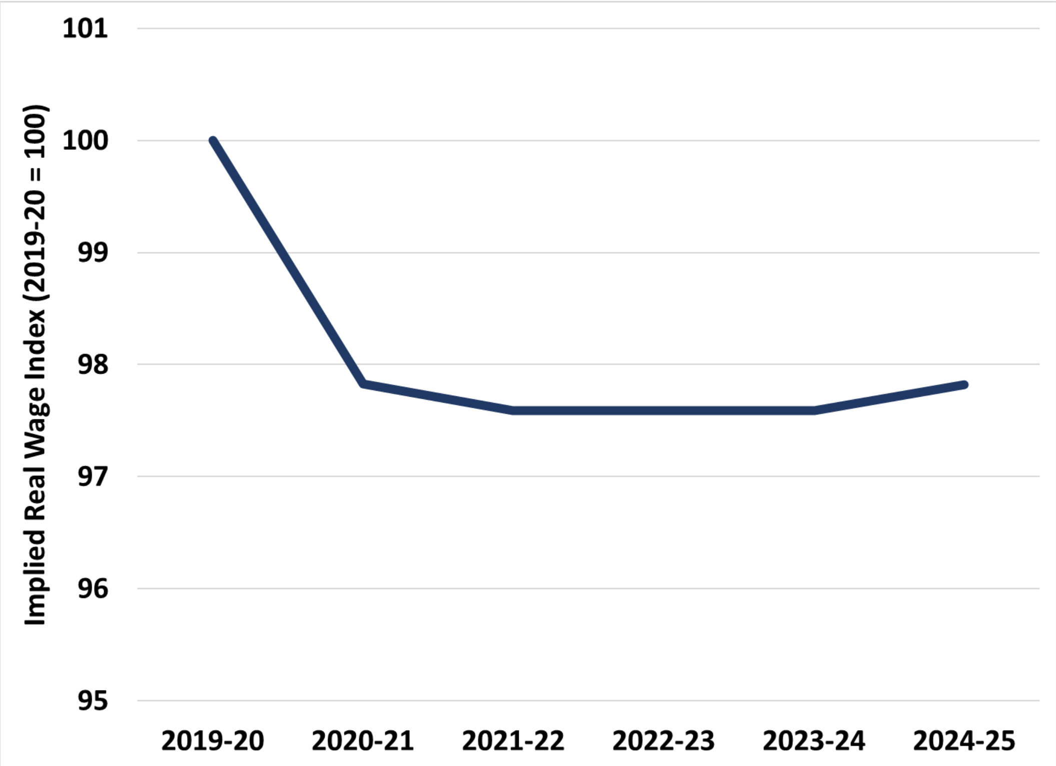
Source: Commonwealth Budget Paper #1, p. 37.

An important implication of this pessimistic official wage forecast is that the government anticipates a significant and sustained decline in real wages for Australian workers. Indeed, the government's wage forecast lags behind its expectation of consumer price inflation for both of the next two years (see Table 1).

Table 1 Budget Forecast of Wages and Prices		
	Wage Price Index (% per yr.)	Consumer Price Index (% per yr.)
2020-21	1.25	3.5
2021-22	1.5	1.75
2022-23	2.25	2.25
2023-24	2.5	2.5
2024-25	2.75	2.5
Source: Budget Paper #1, p.9.		

With nominal wages expected to lag consumer prices for two consecutive years, and then barely match it after that, the result is an implied decline in real wages. Real wages fall by a cumulative total of about 2.5% in the first two years of the forecast, and then stay well below their 2019-20 level throughout the forecast period (Figure 5).[2]

Figure 5. Implied Real Wage Index



Source: Centre for Future Work from Budget Paper #1, p. 37.

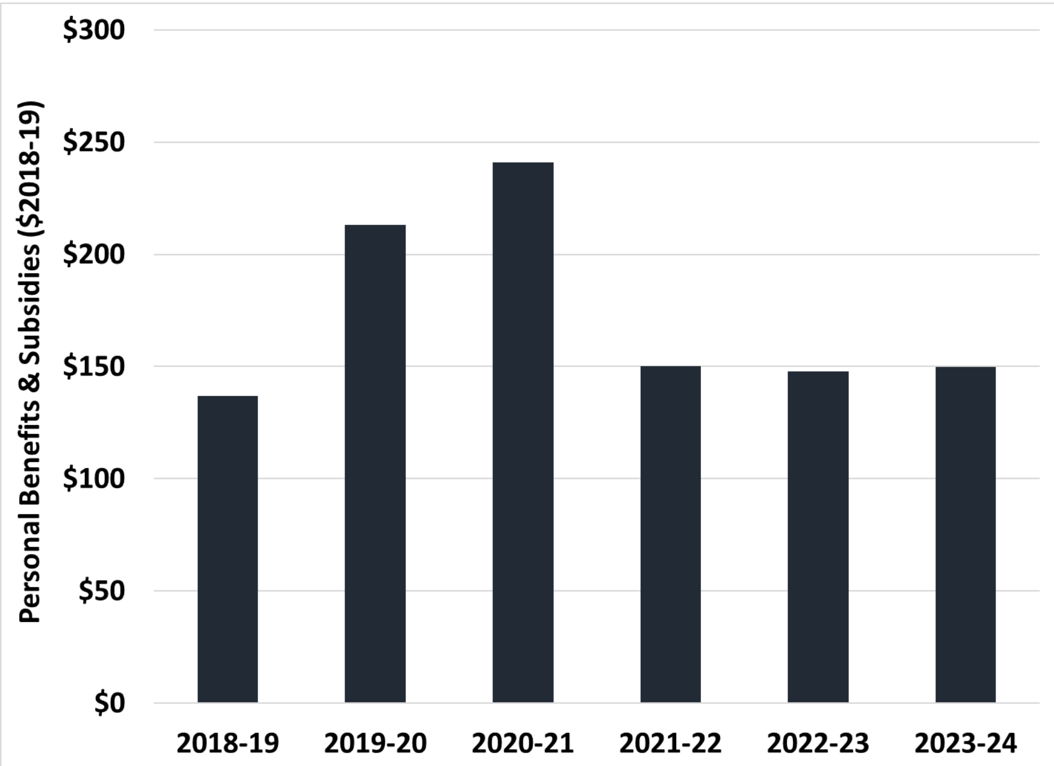
[2] That expected decline in real wages more than offsets the increase in real wages experienced during 2019-20, the result of a decline in average consumer prices for the year; hence real wages remain lower than pre-pandemic levels throughout the full forecast.

It is hard to imagine how Australian households could pay for the strongest expansion in personal consumer spending in a generation, out of real wage packets that fall and then stay low. The budget does not explicitly address the constraint on consumer spending from record-weak wage growth – nor does it pledge to do anything about it. To the contrary, the government has pro-actively helped to *suppress* wage growth: with counter-productive measures like its new public sector wage policy (which restrains wage growth in the federal public service to match private sector growth, setting up a race-to-the-bottom in wages between the government and non-government sectors) and its recent changes to the *Fair Work Act* (which cement the right of employers to use lower-wage casual labour in virtually any position they deem desirable).

Not from Income Supports, Either

The other sign of deep cognitive dissonance in this budget is the contradiction between the hoped-for burst of consumer spending, and the rapid retrenchment of special income supports that were provided during the pandemic – and then yanked away by government as soon as the economy started to recover. Government supports for personal income and wages (through transfers to individuals like JobSeeker, and subsidies to business like JobKeeper) were vital to the maintenance of employment and personal incomes through the pandemic.

Figure 6. Commonwealth Income Transfers



Source: Centre for Future Work from Budget Paper #1, p. 309, and Final Budget Outcome for 2018-19 and 2019-20.

Those transfers were expanded when the pandemic hit, reaching almost $250 billion during the 2020-21 financial year. The government then cut back on these programs early in the economic recovery – unduly anxious to roll back extraordinary expenses, and influenced by employer complaints that relatively generous income supports were somehow undermining Australians' 'incentive to work.'[3] Many sectors of the Australian economy are still operating well below pre-pandemic levels of activity: including airlines, universities, arts and recreation, and hospitality. These sectors, and the people who work there, need continued support for wages to rebuild employment. And all unemployed Australians need enough income support to at least reach the poverty line.

Instead, the elimination of JobKeeper, JobSeeker, and other income supports will reduce personal incomes dramatically in the coming financial year. As illustrated in Figure 6, the combined total of personal benefit payments and subsidies (the latter of which consisted largely of JobKeeper payments) will fall by $100 billion in the coming financial year, and then stay stagnant (in real terms) thereafter. Going forward, these payments will remain only slightly above pre-pandemic levels – reflecting the modest ongoing increase in JobSeeker benefits (lifted by just $50 per fortnight, a small fraction of what was needed).

All of this casts enormous doubt on the budget's hope that a sustained increase in consumer spending can lead Australia's continued economic and employment recovery after COVID-19. Nominal wage growth remains historically weak, and government is making matters worse – rather than intervening to lift wage growth. Real wages are expected to fall, and to remain below pre-pandemic levels. Income supplements will decline dramatically; that will further reduce personal incomes and spending power. For those Australians who did manage to accumulate savings and pent-up demand during the pandemic, economic evidence suggests the short-lived rebound in spending may already be ending. And for millions of Australians who lost work, income, and personal savings during the pandemic, the government's withdrawal of income supports only deepens the economic challenges they face.

The glaring contradiction between the government's reliance on consumers to spend us out of recession, and the government's blunt refusal to support household incomes with higher wages and sustained income supports, means the budget's economic foundation is simply unbelievable. Unless urgent measures are taken to broaden the recovery (with powerful policies to stimulate public and private investment, expand high-value industries, and create secure jobs), and rebuild wage growth to normal and healthy levels (at least 3.5% per year[4]), then the budget's economic and fiscal targets are simply not credible.

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[3] Low-wage employers who offer short or irregular hours complained that some of their employees could make more money through income supplements than through working. However, that is the result of their own inadequate wages and rosters, not 'overly generous' income supports. And incomes – whatever their source – are largely spent on consumption, which in turn supports private business.

[4] Reserve Bank of Australia Governor Philip Lowe has noted repeatedly that nominal wage growth of 3.5% is necessary to support the Bank's 2.5% inflation target, complemented by 1% annual trend productivity growth.

Half Measures that Fail to Meet the Needs of Australians

Apart from this contradictory and unbelievable macroeconomic logic, the budget's specific spending and taxation announcements also fail to meet the challenge of leading a balanced, inclusive, and sustainable post-COVID recovery. Obvious needs for expanded public and human services have been identified in a wide range of areas. The government's spin-doctors claim the budget is responding to those needs. But the resources committed to priority areas (like aged care, childcare, vocational education, and others) is far from adequate to meet the requirements of Australians, especially in the wake of the unprecedented challenges of the pandemic. And despite verbally eschewing austerity, the budget will nevertheless oversee a dramatic retrenchment of the total federal fiscal footprint at a time when (as shown above) the post-COVID recovery remains precariously unbalanced. This briefing will now review several important areas of the budget in more detail.

Aged Care: Research by the Centre for Future Work[5] has shown that implementing the urgent recommendations of the Royal Commission into Aged Care Quality and Safety would require increased federal spending of at least $10 billion per year. That research also identified several options for financing that spending – including canceling expensive Stage Three tax cuts for high-income households, reforming company and capital income taxation, and modest adjustments to income tax rates. The 2021-22 budget announced a cumulative total of $17.7 billion for aged care programs over 5 years, roughly equally divided between residential care and home care initiatives. That represents just one-third of what is reasonably required to fully implement the Royal Commission recommendations – and to do right by Australia's seniors, many of whom have experienced sub-standard care, neglect, and even abuse.

While some of the announced measures are headed in the right direction, the timing, resources, and quality standards included in those announcements are still inadequate. The government announced a plan to require 200 minutes of care per day for seniors in residential care by late 2023. That represents an important reversal of the Commonwealth government's previous hands-off approach to aged care staffing standards (implemented under Howard-era deregulation policies), but does not meet the Royal Commission's recommended benchmark (220 minutes). Nor does it include other measures to enhance the quality and stability of jobs in the sector (including registration, better training, higher wages, and stronger regulation and oversight of the practices of private care providers).

In aged care, like other human services, the quality of care cannot be separated from the quality of work. Unless and until the government allocates more resources, and imposes much stronger quality conditions and safeguards, the vision of high-quality universal aged care advanced by the Royal Commission will remain a far-off hope.

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[5] See David Richardson and Jim Stanford, *Funding High Quality Aged Care Services* (Canberra: Centre for Future Work), https://d3n8a8pro7vhmx.cloudfront.net/theausinstitute/pages/3481/attachments/original/1620071887/Funding_Aged_Services_FINAL.pdf?1620071887.

Gender Inequality: It is well known that women bore a disproportionate share of the overall economic costs of the COVID-19 pandemic and recession.[6] The government faced serious criticism of its last budget (in 2020-21) for ignoring these gender dimensions of the recession. It faced more criticism for its callous and incomplete response to revelations of widespread sexual harassment and assault within Parliament. So it is not surprising that the government tried to impart a more 'sensitive' gender perspective with this latest budget. However, real commitments to gender equality in the budget fall far short of what Australian women need. As our Senior Economist Alison Pennington puts it,[7] the budget tries to address gender inequality with a token 'pink pill'. Australian women deserve much better.

The budget's spending on women consists of relatively small amounts of money divided across many different, often symbolic priorities. The largest item in this women's 'spending bucket' is childcare support: the budget commits $1.7 billion over four years to modestly increase subsidies. That's far less than what childcare advocates and economists alike have been saying is desperately needed to support women's labour force participation and accelerate post-COVID economic growth.

Much-needed domestic violence services funding will increase by $250 million per year – but then is cut by 99%, falling to just $2.3 million, in 2025-26. But the crisis in domestic violence, exacerbated by the pandemic, will certainly not be over then.

This modest new spending for women contrasts with permanent and much more expensive measures that will reinforce or widen gender inequality in Australia. For example, previously announced Stage Three income tax cuts will proceed, which have been shown to overwhelmingly benefit high-income households and men.[8] In fact, men will receive $12.1 billion of annual savings from those expensive tax cuts, more than twice as much as for women.

The Budget abolished the $450 earnings threshold for superannuation payments. This will see additional funds flowing into super accounts for 200,000 low-wage women currently excluded from super by this threshold. But with one in three women retiring with no super at all, and median super savings about half that for men, much more is needed to lift women's retirement incomes: including super payments while on parental leave, and top-ups to offset the persistent effects of career interruptions and lower wages.

An especially glaring absence from the budget is any discussion about women's wages and the continuing gender gap in Australia's labour market. As noted above, the budget

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[6] For a full discussion of the gendered impact of the crisis and how to address those effects, see Australian Council of Trade Unions, *Leaving Women Behind: The Real Cost of the Covid Recovery* (Melbourne: ACTU), December 2020, https://d3n8a8pro7vhmx.cloudfront.net/theausinstitute/pages/3405/attachments/original/1607584195/Women_and_COVID-_A_Gender-Inclusive_Recovery.pdf?1607584195.

[7] See Alison Pennington, "Why I won't swallow the 'pink' budget pill," The New Daily, 12 May 2021, https://thenewdaily.com.au/finance/news-federal-budget/2021/05/12/alison-pennington-federal-budget/.

[8] See Matt Grudnoff, "Coalition's Tax Cuts Favour Men Over Women" (Canberra: Australia Institute), 8 October 2020, https://australiainstitute.org.au/post/coalitions-tax-cuts-favour-men-over-women/.

passively accepts that Australia's miserable wage growth, already mired for years at the weakest pace since the 1930s, is going to get even worse. And this wages crisis hits women hardest; a budget that ignores wages could never be called a 'women's budget.' Four million women (or 65% of all employed women) work in low- and middle-income services industries – like hospitality, retail, and healthcare and social services. Almost half (45.1%) of employed women are in part-time positions. Women fill 54% of all casual jobs. And since the post-COVID recovery in employment began last May, women's jobs are becoming even more insecure: casual jobs account for over 60% of new jobs since then, and women fill 62% of those casual roles.

Those structural features, especially women's concentration in part-time, insecure jobs, explain why the gender pay gap (measured across all jobs) is 31%. And the continuing growth of insecure work could make that worse.

In sum, this budget offers no real change to the policy settings that block women's ability to fully work and earn. Thus the budget will not make an appreciable difference to women's economic security, or address widening inequality. Pink-washing cannot hide the powerful disequalising forces that this government has set in motion.

Vocational Education and Skills: Ongoing cuts to the vocational education and training (VET) sector since 2013 have seen funding reach record lows. Indeed, VET has been a major and consistent loser in education expenditure throughout the 8 years of Coalition government.

Unions and VET advocates have called for the restoration of $3 billion of funding cuts to the vocational system since 2013, but the government's forward estimates paint a far different picture.[9] The 2021-22 Budget projects that expenses will decrease by a further 10.8% in real terms from 2020-21 to 2021-22, and then another 24.2% in real terms between 2021-22 and 2024-25.

The Australian Education Union (AEU) has called on all governments to urgently invest in TAFE, the public provider of high-quality vocational education, by guaranteeing that a minimum of 70% total government VET funds flow to TAFE, and providing capital funding for much-needed infrastructure. This would equate to an additional $750 million for the TAFE system per year, helping reverse the damaging market-driven system that has undermined quality VET in Australia over the past two decades. TAFE is the highest-quality, most stable provider of vocational training and education – yet the 2021-22 federal Budget (just like the one before it) literally made no mention of TAFE.

The budget's separate announcements about investing in apprenticeships and traineeships appear significant on the surface. But the government apparently sees no central role for the public system in delivering training and skills. Unsurprisingly, then, the government's preference for a competitive, market-oriented system would place the development of VET even more in the hands of private providers.

[9] See Budget Paper #1, pp. 169-170.

The 2021-22 Budget has extended the Boosting Apprenticeships Commencements scheme, providing $2.7 billion over four years (some of which is re-announced money), and purportedly supporting 170,000 apprenticeships and traineeships.[10] But the government's record of overseeing an unprecedented decline in participation in apprenticeships and traineeships in recent years does not inspire confidence in this projection. And even if it was realised, it would represent merely restoring apprenticeships to levels resembling those seen before the Abbott government's cuts to VET – not to mention the further steep reduction in commencements experienced during the pandemic.

The budget also announced an extension of the JobTrainer program to the end of 2022. This measure provides $500 million (which must be matched by state and territory governments) to support job opportunities for young workers. But in reality it amounts to little more than a repurposing of the failed JobMaker scheme, in both rhetoric and reality. JobMaker supported a mere 1,100 jobs for 16 to 35-year-olds, and utterly failed to counter the mass unemployment experienced by young workers during and after the pandemic.

Superannuation: The budget made no mention of the hot-button issue that has dominated discussions about superannuation over the last couple of years: the legislated increases in the superannuation guarantee (lifting it from 9.5% of wages to 12% over five years) that are scheduled to begin on 1 July this year. This seems to indicate that at least the first of those increases will go ahead – despite efforts by some members of the government to cancel them. Previous Centre for Future Work research has highlighted the importance of the superannuation guarantee in both supporting overall labour compensation and enhancing the security of retirement incomes for working Australians.[11]

This year's budget does make a number of incremental changes to the superannuation system: some positive, some less so. Most important is the removal of the $450 per month threshold for employer contributions under the superannuation guarantee. This will help low-income earners save for retirement. It is estimated to improve retirement savings for the 200,000 Australian women who make up most of the low-wage workers whose earnings currently fall below that threshold. This is an important but partial step toward reducing gender inequality in the superannuation system: next steps should include superannuation contributions during parental and other family leaves, top ups to address women's persistently inferior superannuation balances, and reforms to the system of tax preferences which currently disproportionately benefit high-income earners (most of whom are men).

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[10] See Budget Paper #2, p. 34.

[11] See Jim Stanford, *The Relationship Between Superannuation Contributions and Wages in Australia* (Canberra: Centre for Future Work), November 2019, https://d3n8a8pro7vhmx.cloudfront.net/theausinstitute/pages/3125/attachments/original/1574168220/Relationship_Between_Superannuation_Contributions_and_Wages_Formatted.pdf?1574168220.

Other changes announced in the budget include facilitating voluntary contributions of up to $300,000 for Australians over 60 who downsize their homes. The budget also removed requirements for older Australians to meet a work test before making voluntary superannuation contributions. Both these changes will disproportionately benefit higher-income Australians, who enjoy more capacity to make voluntary contributions to their savings.

Disappointingly, the budget was silent on the consequences of allowing 3.5 million Australians to withdraw $36 billion from their superannuation funds during the pandemic, under the government's misguided early release program. Facing unemployment or reduced hours, many low- and middle-income earners emptied their superannuation accounts to try to make ends meet through the pandemic. As a result, they now face a major disadvantage in saving for retirement.

Income Security: As noted above, the government's elimination of the JobKeeper and JobSeeker Coronavirus Supplement programs will rip close to $100 billion out of personal incomes in Australia this year. It also intensifies the insecurity still facing millions of Australian workers, whose employment prospects have not yet recovered to pre-pandemic levels. The $50 per fortnight increase in JobSeeker benefits leaves them far below the poverty line. Far from constituting an 'incentive to work', such an inadequate level of income support actually contributes to isolation from the labour market and lower participation.

The youth unemployment rate is currently 11.8%. There is further concern that with the end of JobKeeper, up to 250,000 people aged 24 and under may face unemployment as their wage subsidies are eliminated.[12]

Manufacturing: Continued deficiencies Australia's manufacturing capability were underlined most recently by our inability to effectively produce and deliver coronavirus vaccines. Despite many ambitious statements from federal government leaders during the pandemic about the need to rebuild Australia's manufacturing capacity, this budget fails miserably to elaborate a convincing and viable industry plan for manufacturing.

Manufacturing is a pivotal and strategic sector, with many linkages to other parts of the economy and strong export and innovation intensity. Previous research by the Centre for Future Work has demonstrated[13] that the sector could add 400,000 jobs and $50 billion of GDP, if it were rebuilt to a scale proportionate to our national needs for manufactured goods.

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[12] See Frank Chung, "Up to 250,000 Jobs Could be Lost as JobKeeper Ends," News.com.au, 5 March 2021, https://www.news.com.au/finance/economy/australian-economy/up-to-250000-jobs-could-be-lost-as-jobkeeper-ends/news-story/a311f47581af3542af00ffa369d46dd8.

[13] See Jim Stanford, *A Fair Share for Australian Manufacturing: Manufacturing Renewal for the Post-COVID Economy* (Canberra: Centre for Future Work), July 2020, https://d3n8a8pro7vhmx.cloudfront.net/theausinstitute/pages/3332/attachments/original/1595693276/A_Fair_Share_for_Australian_Manufacturing.pdf?1595693276.

This makes it all the more surprising and disappointing that the Treasurer's speech merely recycled last year's manufacturing Budget measure: a $1.5 billion manufacturing package, with most funds targeted at six priority areas. These include resources technology and critical minerals, food and beverages, medical products, recycling and clean energy, defence, and space.

And the government has still not committed to a durable, funded recovery in publicly-provided vocational education and training, aimed at equipping young and transitioning workers with the full range of skills required to participate in a reinvigorated manufacturing sector. Until the government addresses this shortcoming, any manufacturing-led recovery will be hamstrung.

The government also continues with its misleading and destructive attempt to package further subsidies for fossil fuel production as a 'manufacturing' policy. To subsidise further expansion of domestic gas production, this budget provides $58.6 million – in addition to the so-called 'Gas-Fired Recovery' measures announced last budget. This is despite the fact that most of Australia's current gas production is exported, and that LNG expansion has in fact damaged Australian manufacturing – not helped it. Indeed, research from the Australia Institute shows there is no relationship between gas production and the success of manufacturing.[14] Lower-cost renewable energy possibilities have been largely disregarded in the budget: a new battery project in the Northern Territory that receives targeted support from this budget is the exception proving the rule. Meanwhile, hydrogen production measures being claimed as 'clean' (because of the integration of still-unproven carbon capture and storage technologies) may not integrate renewable energy sources at all.[15]

The budget includes $76.9 million in already-announced subsidies for the Portland aluminium smelter's participation in demand-response measures that help stabilise the electricity grid when there is a shortfall of generation. This is an important and promising initiative, but it is disappointing not to see efforts to unlock other potential applications of demand management in the industrial sector, to complement the wholesale demand response market opening up in October 2021.[16] The government could improve competitiveness, improve reliability, and reduce coal use faster if it worked with AEMO to bring online more industrial demand response from major users – in sectors like metal mining and processing, sugar refining, cement, and even gas and coal mining and processing.

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[14] See Mark Ogge, *Wrong Way, Go Back* (Canberra: Australia Institute), April 2021, https://australiainstitute.org.au/report/wrong-way-go-back/.

[15] See Department of Industry, Science, Energy and Resources, "Jobs Boost from New Emissions Reduction Projects", 21 April 2021, https://www.minister.industry.gov.au/ministers/taylor/media-releases/jobs-boost-new-emissions-reduction-projects.

[16] See Australia Institute, "Demand Response Rule Change: Electricity Market Competition will Reduce Prices, Help with Summer Heatwaves (Canberra: Australia Institute), June 2020, https://australiainstitute.org.au/post/demand-response-rule-change-electricity-market-competition-will-reduce-prices-help-with-summer-heatwaves/.

Meanwhile, Australia's inability to produce modern vaccines – despite our strong medical research sector, and our past historical success in producing vaccines and medicines – is one of the most glaring consequences of the general erosion of our manufacturing prowess. The Victoria state government has recently provided important support to start rebuilding our capacities in this area. This federal budget also announced an unspecified amount of funding to support investment in Australian mRNA vaccine production capacity. This is a promising opportunity, but will need to be monitored to see if the government's real commitment of resources matches the ambition of its rhetoric.

Higher Education:

Higher education has been one of the hardest-hit sectors of Australia's entire economy throughout the pandemic. Higher education lost 35,000 jobs in the year ending November 2020 – reflecting the catastrophic failure of the Coalition government to include universities in the JobKeeper program, and the devastating loss of international students. At a moment when the need for Australians to gain new skills is probably more acute than at any other time in a generation, this avoidable crisis in Australian higher education reflects a terrible error of judgment on the government's part.

It is particularly perverse for the government to talk about investing in skills, even as it continues to neglect the higher education sector. Tens of thousands of our most qualified and highly skilled educators, researchers, and professional staff have lost their jobs. The tertiary education sector's exemption from the government's JobKeeper wage subsidy was arbitrary, ideological and cruel.

Incredibly, this budget will make matters worse. The budget confirms the cessation of special measures to preserve research capacity at universities as international student numbers (and fee receipts) dropped during the pandemic. This means that Commonwealth payments to universities will actually fall by 9.3% over the forward estimates, despite the continuing crisis in higher education. The only new spending for universities announced in the budget is $9.4 million to support online and offshore education models, and an extension to the FEE-HELP loan fee exemption by six months (costing only $300,000). Describing these measures as band-aids would be generous: for universities, the slogan 'we are all in this together' therefore rings especially hollow.

The damage to Australia's ongoing research and economic capacity that has occurred on this government's watch through its neglect of the university sector is incalculable. A genuine recovery for tertiary education will require durable and ongoing funding to make the university sector sustainable, and reduce its long-standing overreliance on international student fees. In turn, stabilising and strengthening higher education and research would have knock-on benefits for Australian productivity and innovation throughout the economy.

Commonwealth Government Employment and Wage Caps: The COVID-19 crisis represents an opportune time for governments at all levels to reinvest in their own operations and staff. For the Commonwealth, not only have long-term staffing and wage caps undermined the capacity, productivity, and morale of the Australian Public Service, but they are also macroeconomically damaging. Undermining federal public sector employment and wages (through staffing reductions, wage caps, and rampant overuse of consultants) undermines consumption spending, labour market conditions, and confidence.

In an economy beset with stagnation and underconsumption, artificially restraining wages in the Commonwealth public service – one of the biggest employers in the economy – is a grave mistake. Similarly, foreclosing possible good-faith outcomes from industrial bargaining between government agencies and workers by pre-limiting wage increases is self-defeating in both macroeconomic and human resources terms.

The Commonwealth's current public sector wages policy, under which public sector wages are capped in line with wage increases in the private sector,[17] is no comfort at a time of record-low private sector wages growth. Over the last financial year, the relevant private sector wage price index annual growth figure was a mere 1.7%. Instead, the government should use its status as a major employer to lead by example: lifting its own wage and employment practices. Replacing the previous 2% wages cap with an even more restrictive measure forfeits this important tool of macroeconomic policy.

Unfortunately, this Budget does not modify that restrictive approach to public sector wages. It does, however, acknowledge that public sector wage caps at the state government level are moderating overall wage growth[18] – a tacit acknowledgment that low wage growth at the Commonwealth level must be further contributing to that dynamic.

The budget's spending estimates confirm the absolute stagnation of total wages and salaries paid out to Commonwealth public servants over the forecast period. There is virtually no change expected in total wages and salaries from 2020-21 through 2024-25, held constant at around $22 billion per year. Even with the meagre wage increases allowed under the new wage policy, this implies a reduction in headcounts by about 8% over the four-year period. By 2024-25, total labour compensation for the federal government (including superannuation expenses) falls to just 5.2% of total revenues (down from 6.7% in 2020-21). At a time when Australia needs more stable, well-paying jobs, the government's ultra-austere approach to its own staffing practices (the 'savings' of which are largely squandered through over-use of outside consultants and contractors) sets a terrible example.

[17] See Department of the Prime Minister and Cabinet, "New wages policy for Commonwealth Public Servants and a review of performance bonus arrangements for senior executives," 13 November 2020, https://ministers.pmc.gov.au/morton/2020/new-wages-policy-commonwealth-public-servants-and-review-performance-bonus-arrangements-senior-executives.

[18] See Budget Paper #1, p. 62.

Tax Cuts: Not surprisingly given the economic and social catastrophe caused by the COVID-19 pandemic, this budget projects large deficits over the medium-term. This is appropriate and healthy, given the urgent needs of Australians: for health services (including a much more effective national vaccine roll-out), income security, and other human and public services. These deficits, while large, are actually significantly smaller than were anticipated in last year's budget. This reflects the faster-than-expected rebound in employment, aggregate demand, and GDP after the end of widespread lockdowns last winter.

Unfortunately, instead of seizing on this good news to strengthen its program commitments in the various crucial areas outlined above (such as aged care and childcare), the government has chosen to double down on its ideological commitment to tax cuts. As usual, the largest of these measures are targeted at large businesses and well-off households. These tax cuts undermine the revenue base for essential public services, and widen inequality in Australian society even further.

The largest tax cuts announced or reaffirmed in this budget include:

- The budget extends the instant asset write-off concession for businesses, which allows them to deduct the full cost of new capital spending in the year it occurs (rather than being amortised gradually over time). This scheme was initially announced in last year's budget, and was extended for one year with this budget. The cost of that extension alone is a staggering $17.9 billion – by far the largest single spending or revenue initiative contained in the entire budget (for example, costing more than all five years of new funding for aged care also announced in the budget). The purported pay-off from this lucrative measure, meant to stimulate new investment by business, is so far completely invisible: there has been virtually no rebound in business capital spending at all since the record lows of mid-2020, and even the government's own budget expects no significant recovery for several years.
- The budget also affirms previously-legislated Stage Three personal income tax cuts will begin in 2024-25. They are expected to cost federal revenues $17 billion per year once in place.[19] The savings from Stage Three measures are closely targeted on high-income taxpayers: 80% of the savings flow to the richest fifth of households, while none of the savings flow to the lowest-income 60% of Australians. Simply cancelling those Stage Three cuts would provide more than enough revenue to fully fund all of the recommendations proposed by the Royal Commission on Aged Care Quality and Safety.

Perhaps recognising that the concentration of so much largesse among a very narrow segment of Australian society might be politically unpopular, the government announced a sprinkling of other tax measures in this budget. The most important is a

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[19] See Shane Wright, "Pandemic Will Help Make Stage 3 Tax Cuts Cheaper," *Sydney Morning Herald*, 9 May 2021, https://www.smh.com.au/politics/federal/pandemic-will-help-make-stage-3-tax-cuts-cheaper-20210507-p57pzg.html.

one-year delay in the elimination of the Low and Middle Income Tax Offset, which will now stay in effect through the 2022-23 financial year. This is not so much a tax cut, as a deferral of a tax *increase*: the LMITO was always intended as a temporary measure, to assist with the political challenge posed by the fact the government's other tax cuts were so concentrated at the top end of the income spectrum. This one-year offset will deliver only token savings to some Australians (and no benefit at all to many). As our previous research has demonstrated,[20] marginal tweaks to personal tax rates cannot compensate for the long-run erosion of living standards in Australia that results from the combination of stagnant wages and inadequate public services.

Conclusion

Australians have traversed an unprecedented and frightening chapter in our economic and social history. The COVID-19 pandemic and recession imposed enormous costs and disruptions, that were not shared equally across society. The largest burden of the pandemic was borne by those who could least afford it: workers in insecure jobs (many of which disappeared almost instantly), women, young people, international and migrant workers. Australia's relative success in controlling contagion creates the opportunity for a faster, stronger recovery than many other countries could hope for. (Although our miserable progress at rolling out vaccines now threatens that success.) Initial rebounds in spending, employment, and confidence registered since last winter are encouraging. But they are fragile, and narrowly based.

This budget was an opportunity for the government to recognise that a sustained recovery needs a more balanced and inclusive economic and fiscal approach. The ability of Australian consumers to lead the recovery cannot be taken for granted: especially if their incomes are undermined by falling real wages and steep, unnecessary cuts in income supports. And in any event, no economy can function well with just one cylinder of its engine firing. Australia's economy needs a broader, more ambitious plan to support sustainable growth and decent growth for years to come: one that involves necessary investments in public and private capital, a permanent expansion in vital human and caring services, a genuine plan to nurture high-value industries in Australia, and a willingness to seize the opportunities associated with the accelerating energy and climate transitions.

Sadly, the budget fails to deliver on all these counts, and others. Its hope that exuberant consumers can single-handedly lead continued recovery is contradicted by its acceptance of stagnant wages as the 'new normal' of Australia's economy. And the half-measures announced to provide necessary support for vital services and infrastructure (including aged care, childcare, and vocational education, among many others) confirms the government has not truly accepted its responsibility to oversee a lasting and inclusive reconstruction after the terrible events of the last year.

[20] See Centre for Future Work, "Commonwealth Budget 2019-20: Refusing to Learn from Past Mistakes," 2 April 2019, https://d3n8a8pro7vhmx.cloudfront.net/theausinstitute/pages/2982/attachments/original/1554217579/Budget_Night_2019.pdf?1554217579.