



Centre of Full Employment and Equity

Analysis of the 2010-11 South Australian Budget

Report prepared for the Public Service Association of South Australia

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Executive Summary

- The South Australia Government fiscal strategy includes: a) a target of achieving a net operating surplus each year; and, b) ensuring that the net financial liabilities to revenue ratio converges to the value of other triple-A rated states.
- This report analyses the 2010-11 South Australian Budget. The Budget contained: new operating initiatives of \$2 billion; \$1.5 billion of savings; half a billion dollars of new revenue measures; and \$10.7 billion of capital investment over four years.
- As a result of the deterioration of the Budget position following the onset of the GFC, the South Australian Government established the Sustainable Budget Commission to advise on strategies to improve budget outcomes. The Commission recommended a 'menu' of savings initiatives for the Government to choose from. The Government is implementing these recommendations through the savings measures announced in the 2010-11 Budget.
- New expenditure measures deliver on election commitments and will provide increased resources in Health, Families and Communities and Education.
- Investment expenditures comprise both Commonwealth funding from the economic stimulus packages and State Government investment in line with the South Australian Infrastructure Plan.
- The Budget announced large reductions in public sector employment of 2673 FTEs (a further 1070 FTEs have been announced previously) and staffing increases of 1981 FTEs over the forward estimates period. The staff reductions are in addition to substantial reductions in recent years.
- The Government's intention to target back room administrative cuts so that service delivery disruptions are minimised will be difficult to achieve since there is no clear delineation between administrative and front-line service delivery positions. Currently the majority of public servants are either primarily engaged in service delivery or perform a range of duties that span administration and service delivery.
- Targeted Voluntary Separation Packages (TVSPs) will be available for staff whose positions are identified as redundant. The value of the TVSPs will be reduced if redeployed staff do not accept the package within six months. The Government will also reconsider its commitment of no forced redundancies if the required number of TVSPs is not reached.
- Large public sector staffing cuts are likely to have a number of adverse impacts. They will have a dampening effect on economic activity. Remaining staff are likely to have higher workloads and higher stress levels. The standard of service delivery is likely to decline with longer waiting times for clients and reduced client satisfaction.
- Cuts to public sector employment conditions include the scrapping of the leave loading for recreation leave and a reduction in annual accruals of long service leave after 15 years service; from 15 days per year to 9 days.
- Government Budget results vary over the economic cycle as a result of economic decisions by business firms and individuals. Governments have an important role to play in stimulating economic activity and maintaining high levels of employment to overcome inadequate demand in the private sector.

- The Budget forecasts a net operating deficit of \$389 million for 2010-11 after a surplus of \$167 million in 2009-10. The net operating deficit in 2010-11 is due to the fact that a large proportion of Commonwealth stimulus expenditure was received by the States in 2009-10 but much of the expenditure will occur in 2010-11. In subsequent years operating surpluses are forecast as increased economic activity restores revenues toward the trend level.
- We estimated the impact of the recent economic downturn on the South Australian Budget in order to extract cyclical variations in revenues and expenses and determine the Structural Balance. While this is not an exact science, it is clear that when cyclical influences are excluded the structural net operating balance increases substantially. It is evident that the structural net operating balance remains in surplus and these surpluses increase over the forward estimates period.
- The Government's fiscal policy of achieving a net operating balance every year may prove to be counter-productive. The Government has attempted to improve the budget outcome with discretionary spending cuts and taxation increases because of fears the budget balance is excessive. In these circumstances, the imposition of austerity may then cause State Product to contract and the automatic stabilisers (principally, tax revenue at the State level) to push the budget further into deficit. It also follows that a growth strategy underpinned by discretionary stimulus spending and/or tax cuts can drive reductions in the budget deficit outcome as the level of economic activity increases and tax revenues recover.
- Governments also contribute to economic and social development through a range of services including education, health, housing, transport and community services. The severity of the spending and staffing cuts implemented in the Budget place these objectives at risk.

1 Introduction

The onset of the GFC caused budget outcomes to deteriorate in South Australia. The South Australian Government has responded by reviewing fiscal policy and taking decisive measures to reduce deficits and place South Australian budget outcomes on what it considers to be a sustainable path. In particular the government has attempted to offset new spending initiatives and capital investment by introducing large expenditure savings and large public sector staffing reductions.

To achieve these cuts the Government established the Sustainable Budget Commission in 2009 to provide advice on specific savings measures of \$750 million (with \$150 million to be achieved in 2010-11, \$250 million in 2011-12 and \$350 million in 2012-13). In the period following the establishment of the Commission the economic situation improved significantly as Australia's economic performance outstripped that of other advanced countries.

Despite improvements in economic conditions and budget outcomes the savings targets were not revised. The Commission urged ongoing fiscal restraint and recommended large cuts to expenditure, asset sales and reviews of existing programs and policies. The report in August 2010 provided the Government with a 'menu' of savings initiatives totalling \$1.8 billion to 2013-14 (Sustainable Budget Commission, 2010).

The 2010-11 Budget announced new savings measures that would reduce expenditure by \$1.5 billion over the forward estimates period. New reductions in public sector staffing of 2673 FTEs were added to the 1070 FTEs that were previously announced but are yet to be realised. These reductions will be offset by additional staff resources of 1981 to 2013-14 associated with new expenditure initiatives.

The Centre of Full Employment and Equity (CofFEE) was commissioned by the Public Service Association of South Australia to analyse the South Australian Budget in the context of current economic conditions and assess the impact of the Budget on the economy and community of South Australia. The report will:

- Present an overview of the South Australian economy and labour market;
- Analyse the expenditure, saving and investment initiatives in 2010-11 South Australian budget and budget outcomes; and
- Consider the impact of the Budget on the South Australian economy and public sector service delivery.

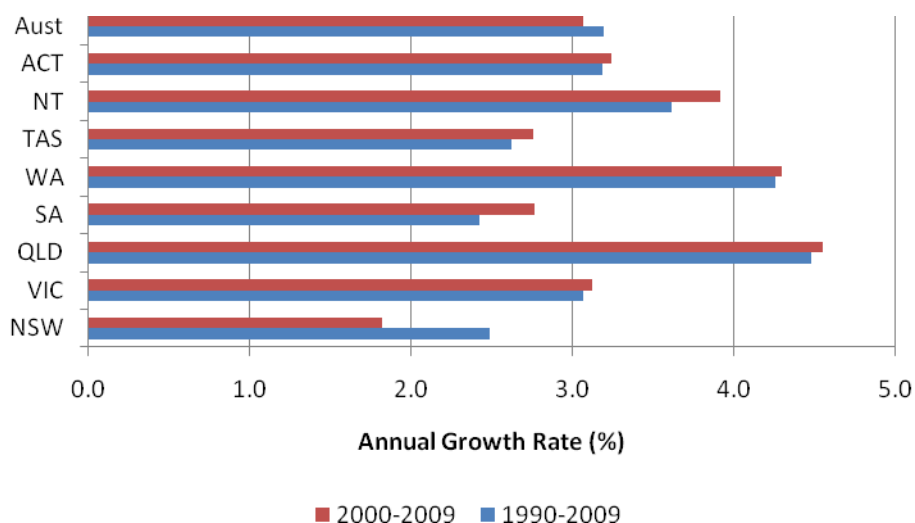
The report is structured as follows. Section 2 provides an overview of the South Australian economy and labour market, including details on public sector employment. Section 3 contextualises the Budget by outlining previous fiscal policies and outcomes. Section 4 provides an analysis of the 2010-11 Budget and details the major new expenditure, savings and investment initiatives. Section 5 discusses potential impacts of the large public sector staffing cuts announced in the Budget. Section 6 provides an analysis of the structural budget position that reveals that, when cyclical influences are removed, the South Australian Government has a considerable degree of fiscal flexibility. Concluding comments are in Section 7.

2 The South Australian economy

2.1 Economic performance

Since the onset of the GFC the Australian economy has outperformed other major economies. In 2009-10 the economy grew by 1.4 per cent compared to a contraction of 3.2 per cent in advanced economies. In contrast to declining employment in other developed economies, employment increased by 225,000 in Australia (Australian Government, 2010). Unemployment is set to fall to 4.75 per cent by 2011-12.

Figure 1 Annual growth rate of GDP



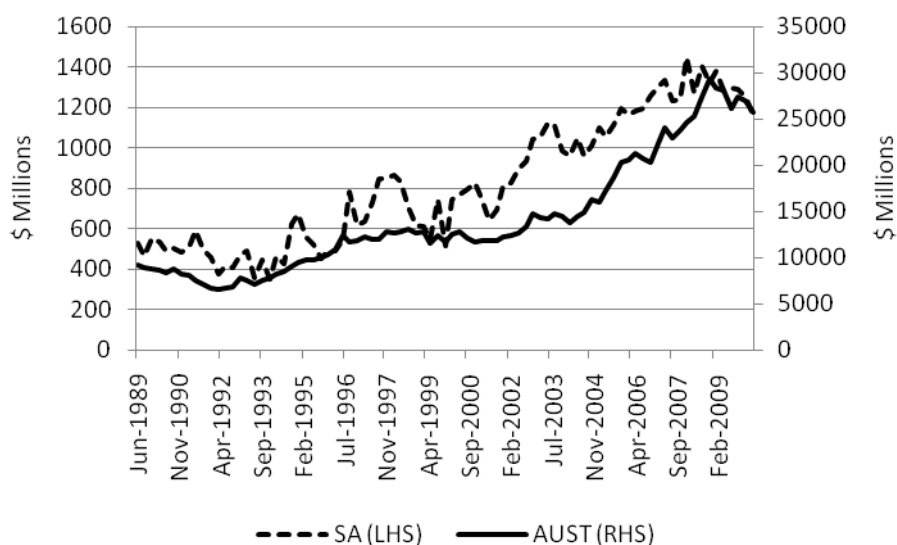
Source: (ABS, 2009a), Cat no. 5220.0 Australian National Accounts: State Accounts, Table 1 Gross State Product, Chain volume measures and current prices

South Australia's economy has shared in this strong performance. GDP growth is increasing and will reach 2.75 per cent in 2010 and 3.5 per cent in 2011-12 (Foley, 2010a). Figure 1 shows the average annual growth rate for GDP since 1990. Over the entire period the annual GDP growth rate in South Australia has been relatively low at 2.4 per cent compared to the Australian average of 3.2 per cent. However, the average annual growth rate of GDP improved considerably in recent years and reached 2.8 per cent for the period 2000-2009. It has surpassed NSW (1.8 per cent) and is much closer to the national average of 3.1 per cent per annum.

In 2008 state final demand represented 6.6 per cent of the national total and GDP was 6.5 per cent. GDP per capita in South Australia in 2008 was \$44,696 which was below the national figure of \$51,253.

Figure 2 displays private new capital expenditure for South Australia and Australia between 1989 and 2010. The trajectory of investment expenditure in South Australia mirrors the experience for Australia as a whole. From 2004 to 2008 private sector investment expenditure increased in South Australia but then declined after the onset of the GFC. Investment reached \$6527 million in 2007-08 and then declined rapidly to \$5389 million in 2008-09. In 2009-10 investment fell even further to \$5004 million.

Figure 2 Private capital investment, 1989-2010



Source: (ABS, 2010a), Cat no. 5625.0 Private New Capital Expenditure and Expected Expenditure, Australia, Table 4B: Actual Expenditure, Current Prices: Seasonally Adjusted

The three industries with the highest contribution to sales and service income in 2007-08 were Manufacturing, Wholesale Trade and Retail Trade. These industries accounted for almost 53 per cent of income in South Australia compared to 48 per cent nationally. Agriculture is more important to the South Australian economy than it is to any other state or territory. Agriculture contributes 4.7 per cent of sales and service income compared to 2.7 per cent nationally. South Australia produces 11.8 per cent of the gross value of agricultural products in Australia, 19.5 per cent of aquaculture and fisheries production and 45.3 per cent of the wine grape crush (ABS, 2009b).

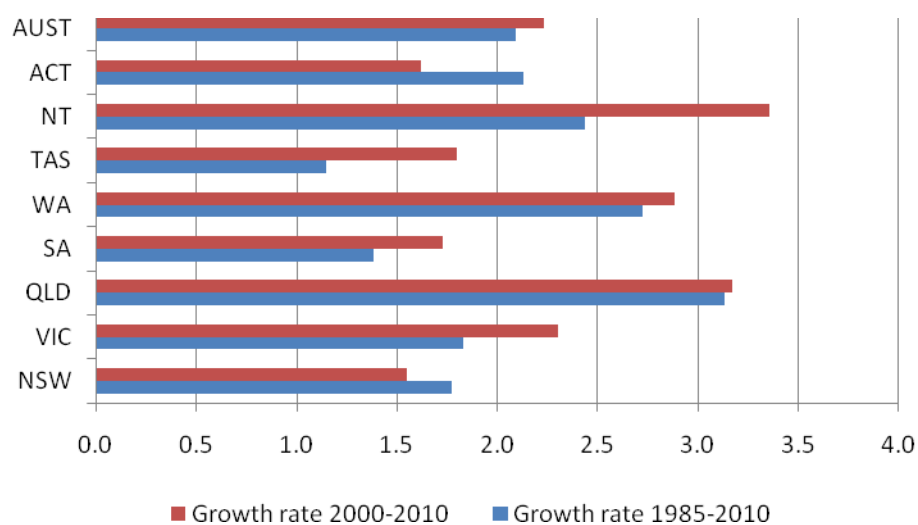
2.2 Labour Market

In July 2010, the labour force participation rate in South Australia was 63.2 per cent compared to the national participation rate of 65.3 per cent (ABS, 2010b). Unemployment was 5.3 per cent, slightly above the national rate of 5.2 per cent. Employment increased by 1.5 per cent in South Australia in the year to July 2010 compared to the national figure of 2.7 per cent.

2.2.1 Employment

The South Australian economy has undergone significant change in the past 25 years. Employment has increased by 235,000, from 574,000 in 1985 to 809,000 in 2010 (ABS, 2010c).

Figure 3 Average annual employment growth, 1985-2010



Source: (ABS, 2010c) Cat no. 6291.0.55.003 Labour Force, Australia, Detailed Quarterly, Table 05 Employed persons by State and Industry

Figure 3 shows the average annual growth rate of employment between 1985 and 2010. For the entire period, South Australian employment growth (1.38 per cent per annum) was lower than all states with the exception of Tasmania and lagged the nation average of 2.09 per cent. As was the case with GSP, South Australia's average annual employment growth rate has improved over time. For the period 2000 to 2010 the average employment growth rate for South Australia was 1.73 per cent compared the national rate of 2.33 per cent.

Employment growth has been much higher than average for some industries. Between 2000 and 2009 the employment growth accelerated in the Mining, Construction and Health Care and Social Assistance industries that each recorded annual growth rates of 5.7 per cent. Employment in Arts and Recreation Services increased by 4.1 per cent per annum.

Between 1985 and 2010 part-time employment has increased from 20.4 per cent of total employment to 32.4 per cent and has increased in all industries. Part-time employment exceeds half of total employment for Accommodation and Food Services and Retail Trade (60 per cent and 53 per cent respectively). Part-time employment accounts for over 40 per cent of total employment in Administrative and Support Services, Health Care and Social Assistance, and Arts and Recreation Services (ABS 2010c).

In 1985 manufacturing was the largest industry in terms of employment with 16.9 per cent of total employment (Table 1). The importance of manufacturing has declined to just 9.9 per cent of total employment in 2010 and has fallen in absolute terms over this period, from 97,000 to 80,000. Similarly, the industry shares of employment for Wholesale Trade and Agriculture, Forestry and Fishing have declined. Industries recording an absolute decline in employment included: Agriculture, Forestry and Fishing; Manufacturing; Electricity, Gas, Water and Waste Services; and Information, media and Telecommunications.

Over this period Health Care and Social Assistance has increased from the third largest employer to the first, increasing its employment share from 9.6 per cent to 13.9 per cent of total employment. Retail trade retains the second highest share of employment and has increased from 10.7 per cent to 11.3 per cent of total employment. Increased employment

shares have been recorded by the Construction, Accommodation and Food Services, Public Administration and Administrative and Support Services industries.

Table 1 Industry share of employment, 1985 to 2010

	1985	1990	1995	2000	2005	2010
Agriculture, Forestry and Fishing	7.8	7.4	7.3	7.9	5.1	4.7
Mining	1.4	0.8	0.4	0.6	1.1	0.8
Manufacturing	16.9	16.1	14.8	14.1	12.5	9.9
Electricity, Gas, Water and Waste Services	1.8	1.3	1.1	1.0	1.2	1.1
Construction	6.8	5.8	5.5	6.2	6.6	8.6
Wholesale Trade	5.0	5.8	4.5	4.0	4.1	3.7
Retail Trade	10.7	10.5	10.6	11.1	11.0	11.3
Accommodation and Food Services	5.0	5.1	6.0	6.4	7.0	6.9
Transport, Postal and Warehousing	4.6	3.8	4.8	4.0	4.1	4.6
Information Media and Telecommunications	2.9	2.7	1.7	2.2	2.2	2.1
Financial and Insurance Services	3.5	3.8	2.8	2.9	2.9	3.0
Rental, Hiring and Real Estate Services	1.1	1.5	1.2	1.3	1.7	1.5
Professional, Scientific and Technical Services	3.6	4.3	5.1	5.4	5.1	5.2
Administrative and Support Services	1.6	2.2	3.2	4.4	3.9	3.2
Public Administration and Safety	4.8	5.3	4.7	5.9	6.2	6.6
Education and Training	7.3	6.7	7.8	7.1	7.5	7.9
Health Care and Social Assistance	9.6	10.4	11.6	10.0	12.6	13.9
Arts and Recreation Services	1.1	1.4	1.5	1.1	1.3	1.4
Other Services	4.3	5.0	5.1	4.2	4.1	3.6
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: (ABS, 2010c), Cat no. 6291.0.55.003 Labour Force, Australia, Detailed, Quarterly, Table 05 Employed persons by State and industry

2.2.2 Public Sector Employment

Table 2 details public sector employment in South Australia between 1991 and 2009. As in other jurisdiction public sector employment has contracted in the past two decades. During this period total employment fell from 101647 to 83885 full time equivalents (FTEs). Public sector employment contracted from 18.1 per cent of the South Australian workforce in 1991 to 12.7 per cent in 2009.

In June 2008:

- 65.5 per cent of public sector employees were female
- 36.4 per cent of executives were female;
- The median age of public sector employees was 45.5 years;
- Youth aged under 25 years made up around 5 per cent of total public sector employees while workers aged 55 or older made up 20 per cent;
- 63.5 per cent of public sector workers were employed on an ongoing basis, 27.1 per cent were on contracts and 9.1 per cent had other arrangements;
- 38.1 per cent were employed part-time and 84.2 per cent of part-time workers were female; and
- 78 per cent were employed in the CBD or Adelaide metropolitan area and 22 per cent worked in regional areas.

Table 2 South Australian public sector employment, 1991 to 2009

Year	FTEs	Persons	Change	% Change	% of SA workforce
1991	101647	115700			18.1
1992	96960	111025	-4675	-4.04	17.7
1993	96259	110781	-244	-0.22	17.4
1994	90885	105836	-4945	-4.46	16.7
1995	86498	102899	-2937	-2.78	15.9
1996	79432	94808	-8091	-7.86	14.4
1997	76392	91812	-2996	-3.16	13.9
1998	77601	91818	6	0.01	14.4
1999	70517	84199	-7619	-8.30	12.7
2000	68615	83543	-656	-0.78	12.3
2001	68884	82953	-590	-0.71	12.3
2002	69770	83821	868	1.05	12.1
2003	71373	85576	1755	2.09	11.9
2004	72141	86885	1309	1.53	12.0
2005	76720	89979	3094	3.56	12.1
2006	78211	92848	2869	3.19	12.2
2007	79715	94780	1932	2.08	12.4
2008	81270	96905	2125	2.24	12.3
2009	83885	100597	3692	3.81	12.7

Source: (Spoehr, 2006; Commissioner for Public Employment, 2008, 2009).

Table 3 shows the relative size of state public sectors: the number of employees per state, population, the number of public servants per 1000 population and the rank, with 1 indicating the largest public sector employment per capita and 8 the lowest. It is expected that states with the largest population share will have a smaller number of public servants on a per capita basis due to scale efficiencies. South Australia is ranked fourth with 66.6 public servants per 1000 population which is similar to the size of the Queensland public sector and smaller than Western Australia despite the fact that South Australia has a smaller population than both these states. These figures suggest that the South Australian public sector is relatively lean.

Table 3 State public sector employees, June 2009

	Employees	Population	Employees (per 100 population)	Rank
NSW	429700	7191500	59.8	7
VIC	310300	5496400	56.5	8
QLD	295300	4473000	66.0	5
SA	108800	1633900	66.6	4
WA	159100	2270300	70.1	3
TAS	38100	505400	75.4	2
NT	23700	227700	104.1	1
ACT	21700	354900	61.1	6

Source: (ABS, 2009c; ABS, 2010d)

3 Background to the 2010-11 budget

South Australia's Strategic Plan (Government of South Australia, 2004) and the Strategic Infrastructure Plan for South Australia (Government of South Australia, 2005) provide the framework for delivery of policy in the state. The Strategic Plan elaborates the role of the government in economic and social development. The objectives include:

- Growing Prosperity
- Improving Wellbeing
- Attaining Sustainability
- Fostering Creativity and Innovation
- Building Communities
- Expanding Opportunities

Progress against the Strategic Plan is evaluated every two years. In 2010 the South Australia's Strategic Plan Audit Committee (2010) found that there had been negative movement against 14 of the 98 targets, two targets were not reached and it was unlikely that another 22 targets would be reached.

The Strategic Infrastructure Plan for South Australian was released in 2005 and has 10 year framework. The Plan provides a framework for development of infrastructure by the public and private sectors covering the areas of transport, industrial land, information and communications technology, education and training, science, technology and innovation, health, community services and housing, and utilities.

Some infrastructure projects have been brought forward as a result of the Commonwealth Nation Building – Economic Stimulus Plan. The 2009 Budget announced \$11.4 billion worth of infrastructure expenditure over four years that included Commonwealth funding for schools, social housing and transport.

3.1 Commonwealth – State fiscal arrangements

The Australian federal system of government exhibits vertical fiscal imbalance, a situation where there is a mismatch between the revenue raising capacity and responsibilities for service provision for different levels of governments. The Commonwealth has had a greater ability to raise revenues since the transfer of income taxation powers in the 1940s. Transfers

from the Commonwealth to State governments as a proportion of state's total revenue indicates the extent of vertical fiscal imbalance. In 2008-09 Commonwealth funding was estimated to be around 49 per cent of total state revenue. These transfers include:

- National Specific Purpose Payments (SPPs).
- National Partnership Payments
- General revenue assistance – GST and other general revenue assistance

SPPs include: the National Healthcare SPP; the National Schools SPP; the National Skills and Workforce Development SPP; the National Disability Services SPP; and the National Affordable Housing SPP. Grants are determined on a per capita basis according to population shares and are indexed annually. In the case of the National Schools SPP payments are based on the state share of full-time equivalent students enrolled in government schools. National Partnership payments include payments for specific projects, facilitation payments and reward payments and have been the major vehicle for delivery of the economic stimulus grants to the states.

A new Intergovernmental Agreement at COAG in November 2008 provided \$1.25 billion for South Australian (\$15.2 billion nationally) over five years for health, education, skills and affordable housing. Commonwealth funding in response to the GFC provided significant additional funding. The \$4.7 billion Nation Building Package was announced in December 2008. This was followed in February 2009 with the announcement of the \$42 billion Nation Building – Economic Stimulus Plan to support economic activity and jobs, with funding over five years (Commonwealth Coordinator-General, 2010). This consisted of:

- \$16.2 billion over three years for the Building the Education Revolution program – building and rebuilding school infrastructure around Australia to support economic activity.
- \$1.12 billion for Regional and Local Community Infrastructure program for local government to provide community infrastructure such as playgrounds, community centres and recreational infrastructure such as sporting fields and swimming pools.
- \$2.3 billion for road and rail infrastructure.
- \$5.2 b for the construction of new social housing and \$400 million for repairs and maintenance. \$245.6 million for Defence Housing
- \$12.2 billion in bonus payments to individuals
- \$2.7 billion for business investment tax breaks
- \$3 billion for Energy Efficient Homes

The \$1.8 billion South Australian share of this package provided \$1.3 billion for health, \$477 million for social housing and \$29 million for transport (Foley, 2009).

The Nation Building Plan for the Future announced by the Commonwealth in May 2009 provided additional funding for infrastructure in South Australia, including:

- \$294 million toward completion of the Gawler rail line upgrade;
- \$291 million to extend the Noarlunga rail line to Seaford;
- \$200 million to build new a Health and Medical Research Institute;
- \$61 million for the O-Bahn highway CBD link;
- \$14.6 billion for TAFE facilities; and

- \$228 million for the Adelaide Desalination Plant

From July 2011 Commonwealth health funding under the National Health and Hospitals Network will combine existing National Healthcare SPP funding and an amount of GST dedicated to health spending.

3.2 Fiscal outcomes prior to the 2010-11 budget

South Australia's fiscal position was affected by the GFC through reduced revenues as economic activity contracted. Table 4 lists some of the changes to economic and fiscal forecasts after the onset of the GFC. Estimates of GSP and employment growth were initially revised down dramatically and subsequently revised up as the economy performed above expectations. Forecasts of the net operating balance have changed substantially, even over short time periods. The 2008-09 MYBR revised the net operating balance for 2008-09 from a surplus of \$160 million (at the time of the 2008-09 Budget) to a deficit of \$112 million. This was revised down further in the 2009-10 budget and the final result was a deficit of \$233 million that was reported in the 2008-09 Final Budget Outcome. The forecasts for the net operating balance for 2009-10 gyrated as economic conditions changed. The revised forecast in the 2008-09 MYFR of a deficit of \$81 million was later replaced by a surplus of \$167 million in the 2010-11 Budget.

Table 4 Economic and Budget forecasts

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
	\$ m	\$ m	\$ m	\$ m	\$ m	\$ m	\$ m
Net operating balance							
2008-09 Budget	373	160	356	434	424		
2008-09 MYBR		-112	-81	107	288		
2008-09 Final Budget Outcome	464	-233					
2009-10 budget		-265	-304	78	96	304	480
2009-10 MYBR			-174	13	27	316	
2010-11 budget			167	-389	55	216	370
GSP							
2008-09 MYBR	3.80	2.00	2.25	2.75	2.75		
2009-10 budget	3.80	1.00	-0.50	2.25	4.25	4.25	
2009-10 MYBR		1.40	2.25	2.50	3.50	3.50	
2010-11 budget		1.40	2.00	2.75	3.50	2.75	2.75
Employment							
2008-09 MYBR	2.10	1.50	0.75	1.00	1.00		
2009-10 budget	2.80	0.75	-1.25	0.50	1.25	2.25	
2009-10 MYBR		1.10	0.00	1.25	1.75	1.75	
2010-11 budget		1.70	0.90	1.25	2.00	1.50	1.00

Source: South Australian Budget Papers, Mid Year Budget Reviews and Final Budget Outcomes, various years

The South Australian Government responded to the GFC with expenditure cuts. The 2008-09 Budget included savings of \$250 million to be achieved over three years (\$25 million in 2009-10, \$75 million in 2010-11 and \$150 million in 2011-12). In the 2009-10 Budget an additional \$75 million was added to the ongoing savings for 2012-13 so that total savings in that year would be \$225 million.

In addition to these savings the Government announced staff cuts in the public sector in the 2008-09 MYBR. In total 1600 FTEs would be cut, including 1200 in 2009-10 and a further

200 in 2010-11 and 2011-12. These staff reductions are in addition to the annual efficiency dividend of a 0.25 per cent per annum reduction in employee expenses announced in the 2006-07 Budget.

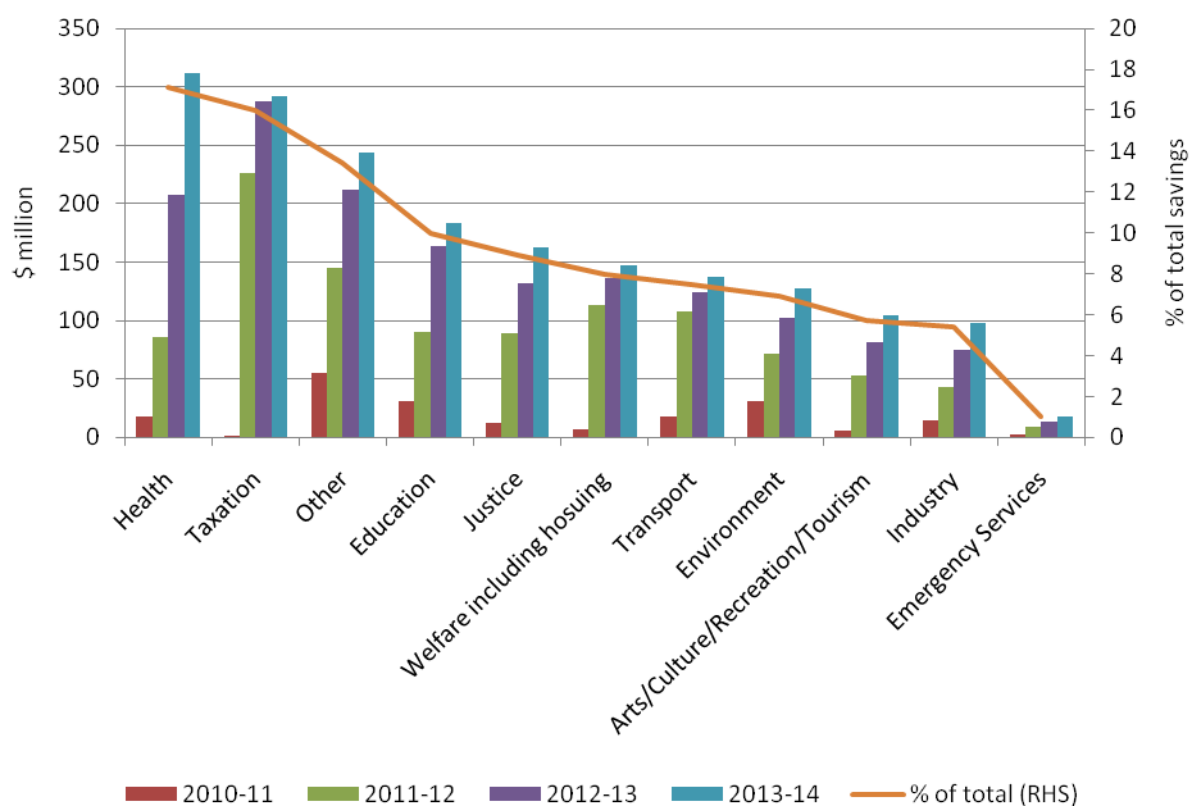
3.3 The Sustainable Budget Commission

The Sustainable Budget Commission was announced in the 2009-10 Budget to “recommend strategies to achieve additional budget improvement measures of \$750 million in the forward estimates period, with \$150 million to be achieved in 2010-11, \$250 million in 2011-12 and \$350 million in 2012-13” (Foley, 2009: 5).

Despite the improvement in economic performance since the establishment of the Commission and the observation that “The South Australian Budget is not in crisis” (Sustainable Budget Commission, 2010: vii) the report urged the Government to proceed with large savings measures and maintain a net operating surplus large enough to make adequate contributions to fund capital expenditure to “avoid a marked deterioration in the State’s net financial liabilities-to-revenue ratio” (Sustainable Budget Commission, 2010: 19).

The Commission identified savings measures totalling \$1.8 billion to 2013-14 for the Government to choose from. Of these around 70 per cent were reductions in spending, 20 per cent were increases in cost recovery and 10 per cent were increases in general revenue. Recommendations included measures to reduce waste and duplication to increase public sector efficiency but also included cuts to, and elimination of, some programs that the Commission acknowledged had merit.

Figure 4 Savings recommended by the Sustainable Budget Commission, 2010-11 to 2013-14



Source: (Sustainable Budget Commission, 2010: 168) Second Report Vol. 2, Table 4

The full impact of recommended savings is shown in Figure 4. While there would be significant impacts in 2010-11 the major impacts would be felt in later years. The largest savings were identified in the health portfolio while taxation measures would make the next largest contribution.

The Government was generally supportive of the majority of recommendations by the Commission. They did not support a number of proposals that included abolition of the Department of Trade and Economic Development and the transfer of its functions to other departments, the abolition of Bio Innovation SA and Zero Waste programs, changes to government procurement or the sale of SA Lotteries and Forestry SA (Government of South Australia, 2010).

4 The 2010-11 Budget

The South Australian Government has the following fiscal targets (Foley, 2010a: 6):

- To achieve at least a net operating balance in the general government sector in every year
- To achieve net lending outcomes that ensure the ratio of net financial liabilities to revenue continues to decline towards that of other triple-A rated states.
- To ensure that the state has an effective tax regime having regard to the government's social and economic objectives
- To provide value for money community services and economic infrastructure within available means
- To fully fund accruing superannuation liabilities and progressively fund past service superannuation liabilities
- To ensure that risks to state finances are managed prudently to maintain a triple-A rating
- To ensure public non-financial corporations (PNFCs) will only be able to borrow where they can demonstrate that investment programs are consistent with commercial returns (including budget finding).

Table 5 Key assumptions underlying the budget and forward estimates

	2009-10	2010-11	2011-12	2012-13	2013-14
	Actual ^(a)	Forecast	Forecast	Forecast	Forecast
South Australia					
Gross State Product (GSP) – real growth (%)	2	2.75	3.5	2.75	2.75
Employment – growth (%)	0.9	1.25	2	1.5	1
Australia					
Gross Domestic Product (GDP) – real growth (%)	2.25	3	3.75	3	3
Employment – growth (%)	2.75	2.25	2	1.5	1.5
Unemployment rate (%)	5.25	5	4.75	5	5

Source: (Foley, 2010b; Swan and Tanner, 2010b)

(a) For South Australia GDP and employment growth are ABS outcomes. GSP is an estimate.

The key economic assumptions underlying the budget are shown in Table 5. South Australian forecasts of economic growth are slightly less than the Commonwealth estimates for

Australia. This is in line with the historically lower growth rate. Similarly, the forecasts for employment growth over the forecast period are equal to or lower than the Commonwealth forecasts.

There are three major strategies evident in the 2010-11 Budget. First, there are large new expenditure commitments (\$2 billion over four years) that concentrate on delivery of services that include recruitment of front-line workers such as health workers, police, teachers and child protection workers. Second, there are large savings measures that offset the cost of new initiatives. Savings will total \$1.5 billion over the forward estimates. These concentrate on efficiency measures and the abolition of lower priority programs and functions. These savings are accompanied by large staff cuts in addition to recently achieved reductions. In short, the Budget is dedicated to ensuring that front-line services are maintained or expanded and administrative functions curtailed to minimise expenditure increases. The third strategy is the continuation of high capital expenditure as a result of both State and Commonwealth initiatives. Commonwealth stimulus programs are reflected in large increases in both revenues and expenses in the Budget. Capital investment will total \$10.7 billion over the forward estimates period. New revenue measures will also raise \$0.5 billion over this period.

Table 6 General government indicators, 2008-09 to 2013-14

		2008- 09	2009- 10	2010- 11	2011- 12	2012- 13	2013- 14
		Actual	Estimated	Budget	Estimate	Estimate	Estimate
Budget balances							
Net operating balance	\$m	-233	167	-389	55	216	370
Net lending	\$m	-872	-1124	-1791	-841	-194	126
Cash surplus	\$m	-721	-1121	-1773	-793	-139	163
Revenue and expenses							
Revenue real growth	%	1.8	12.3	-5.4	0.2	0.5	-0.7
Expenses real growth	%	7.4	9.2	-1.9	-2.7	-0.5	-1.6
Interest ratios							
Net interest to revenue ^{(a)(b)}	%	0.2	0.1	0.8	1.2	1.3	1.5
Net Interest plus nominal superannuation interest to revenue ^(b)	%	3.1	3.1	3.6	4.0	4.0	4.0
Balance sheet indicators							
Net debt	\$m	475	1587	3335	3633	3864	3847
Net debt to revenue	%	3.5	10.2	22.1	23.4	24.1	23.6
Unfunded superannuation	\$m	8939	9476	9442	9445	9428	9389
Net financial liabilities	\$m	11562	13271	15096	15558	15967	16105
Net financial liabilities to revenue	%	85.5	85.4	100.1	100.2	99.8	98.8
Net worth	\$m	24146	25192	25392	26162	27245	28379

Source: (Foley, 2010a:1.8) 2010-11 Budget Statement: Budget Paper 3, Table 1.7

Note: Real-terms calculations use the Adelaide Consumer Price Index

(a) Net interest does not include nominal superannuation interest cost

(b) Revenue does not include interest income

Table 6 provides a summary of the key general government sector indicators over the forward estimates period. The net operating balance achieved a \$233 million deficit in 2008-09 and a surplus of \$167 million in 2009-10. Concerns over the net operating deficit of \$389 million for 2010-11 need to be tempered by an understanding of some of the drivers of the deficit. The fact that Commonwealth grants for stimulus spending were primarily paid to the States in 2009-10 but expenditure will be spread over a longer time period suggests that a more accurate picture of the fiscal position requires consideration of results over a longer time period.

The increases in net lending and net debt relate to the large capital expenditure program that will deliver infrastructure that will bring ongoing economic and social benefits to the people of South Australia. The debt will be repaid over the life of the assets.

The remainder of this section outlines specific expenditure and revenue measures contained in the 2010-11 Budget, including specific measures by portfolio.

4.1 Expenditure

This section examines operating expenditure and capital expenditure as well as the impact of expenditure cuts on public sector staffing.

4.1.1 Operating expenditure

Table 7 details operating expenditure in the general government sector by portfolio for 2009-10 and 2010-11. In 2010-11 operating expenditure is expected to increase by \$407 million. Major reductions in expenditure will apply to Water (36.6 per cent), Primary Industries and Resources (18.2 per cent), Tourism (13.9 per cent) and Planning and Local Government (10.7 per cent). Families and Communities will obtain the largest relative increase of 9.6 per cent, followed by the Auditor-General (7.7 per cent), Further Education, Employment, Science and Technology (7.1 per cent), Health (5.1 per cent) and Education and Children's Services (4.6 per cent). Specific Budget expenditure initiatives are detailed in the next section.

Table 7 Operating expenditure by portfolio

	2009-10 \$m	2010-11 \$m	Change (%)
Legislature	23	23	0.0
Premier and Cabinet	309	296	-4.2
Trade and Economic Development/Defence SA	96	88	-8.3
Treasury and Finance	216	218	0.9
Planning and Local Government	28	25	-10.7
Justice	1407	1466	4.2
Primary Industries and Resources	324	265	-18.2
Transport, Energy and Infrastructure	1294	1320	2.0
Health	4242	4460	5.1
Education and Children's Services	2421	2533	4.6
Families and Communities	1670	1831	9.6
Environment	252	243	-3.6
Water	290	184	-36.6
Tourism	72	62	-13.9
Further Education, Employment, Science and Technology	536	574	7.1
Auditor-General	13	14	7.7
Total operating expenditure	13194	13601	3.1

Source: (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3, Table 2.9, page 2.13

4.1.1.1 Expenditure initiatives

The 2010-11 Budget announced \$1937.4 million in new expenditure initiatives over the forward estimates period. The cost of new initiatives is shown for each year and the total expenditure over four years. The change in expenditure as a consequence of new initiatives is detailed in Table 8 by portfolio. Negative values indicate additional expenditure. Additional expenditure is spread fairly evenly over the four years, with somewhat higher expenditure planned for years 2 and 3.

Table 8 New operating initiatives, 2010-11 to 2013-14

	2010-11	2011-12	2012-13	2013-14	Total
	\$ m	\$ m	\$ m	\$ m	\$ m
Legislature	-	-	-	-	-
Premier and Cabinet	-0.6	-1.8	-10.7	-2.0	-15.1
Trade and Economic Development/Defence SA	-11.5	-11.8	-11.5	-9.5	-44.3
Treasury and Finance	-0.2	-85.2	-0.2	-0.2	-85.8
Planning and Local Government	-	-	-	-	0.0
Justice	-27.8	-34.7	-44.4	-56.7	-163.6
Primary Industries and Resources	-10.7	-4.4	-4.4	-3.3	-22.8
Transport, Energy and Infrastructure	-3.8	-9.5	-9.9	-13.8	-37.0
Health	-159.2	-172.1	-194.0	-205.1	-730.4
Education and Children's Services	-8.2	-11.5	-15.1	-14.4	-49.2
Families and Communities	-73.2	-71.3	-75.4	-76.1	-296.0
Environment	-0.4	-0.4	-0.4	-0.4	-1.6
Water	-0.5	-	-	-	-0.5
Tourism	-	-	-	-	-
Further Education, Employment, Science and Technology	-32.8	-34.0	-35.0	-35.7	-137.5
TVSP scheme expenditure provision	-94.9	-86.7	-123.9	-48.3	-353.8
Total operating initiatives	-423.7	-523.3	-524.9	-465.5	-1937.4

Source: (Foley, 2010a: 2.2) 2010-11 Statement: Budget Paper 3, Table 2.2

In line with the Government's announced Budget strategy, new expenditure initiatives are concentrated in portfolios delivering front-line services. The largest increase in expenditure will be in the Health portfolio. Other large increases in expenditure as a result of new initiatives in the 2010-11 Budget are in Families and Communities (\$296 million), Justice (\$163.6 million) and further Education, Employment, Science and Technology (\$137.5 million). Expenditure for new TVSPs is expected to reach \$353.8 which is second only to Health initiatives

Complete details of all new initiatives are included in the *2010-11 Budget Measures Statement: Budget Statement 6* (Foley, 2010c). The remainder of this section provides details of major expenditure measures for each portfolio. Unless another time period is specified expenditure figures relate to the four years from 2010-11.

The major expenditure initiative in **Premier and Cabinet** is \$10.8 million for the Adelaide Festival, with \$9.2 million in 2012-13.

Additional funding for existing programs and new programs in **Trade and Economic Development** is offset by savings from existing programs due to a refocussing of Departmental programs towards more targeted support for specific industries (see Section 4.1.1.2). New funding commitments include:

- \$5.45 million over three years from 2010-11 in additional support for the Clean Tech industry strategy.
- \$6.25 million in additional support for manufacturing industries. Assistance will be provided for business development of small to medium enterprises for innovation and development of new technology and for the manufacture of medical devices.
- \$20 million to establish the Riverland Sustainable Futures Fund. This regional package seeks to foster economic development and increase industry diversity in the Riverland region.
- \$8 million to establish the Strategic Industry Development Fund.
- \$4.5 million to establish the Upper Spencer Gulf Enterprise Zone to facilitate economic and employment development with a focus on meeting the needs of the mining industry.

The major new initiative for **Treasury and Finance** is \$85 million for the redevelopment of Adelaide Oval in 2010-11.

The **Justice** portfolio will record increased expenditure across Departments. The major commitments include:

- \$94.7 million for 300 additional police officers by 2013-14 and the purchase of hi-tech fighting equipment. Expenditure will increase over four years to reach \$41.7 million in 2013-14.
- An additional \$5 million per annum, (an indexed total of \$20.6 million), for the Department for Recreation and Sport's annual grant program.
- \$11.6 million for the "Street Crime: You damage it – you fix it" program that will require offenders who vandalise property to repair the damage.
- Grants in 2010-11 for the Campbelltown Leisure Centre (\$3 million) and Port Augusta sports hub (\$5 million) to redevelop the Central Oval precinct.
- \$6.8 million to implement changes to domestic violence legislation by providing additional resources to manage the expected increase in intervention orders.
- \$6.5 million for additional security on public transport by employing additional police from January 2011 to patrol public transport.
- \$9.5 million in additional funding to the Legal Services Commission due to increased demand for services.
- \$12.9 million for the Prepare.Act.Survive education program for bushfire safety to ensure that the community is prepared and understands how to survive bushfires.

Primary Industries and Resources has two main expenditure initiatives in the 2010-11 Budget:

- \$12.8 million additional support has been allocated for 2010-11 for the Plague locust control program.

- \$10.2 million over four years in additional support for the Plan for Accelerating Exploration (PACE 2020) and to assist mining companies with exploration through the provision of online geological and geophysical information.

The major operating initiatives for **Transport, Energy and Infrastructure** are for public transport services including additional expenditure of \$18.1 million for outer metro bus services. An initiative prior to the 2010-11 budget provided \$16 million for the Greater Edinburgh Parks road and rail upgrade.

Additional funding for **Health** services totals \$730 million over four years in addition to \$118 million in 2009-10. The 2010 *National Health and Hospitals Network Agreement* provides additional funding to the States as the Commonwealth Government increases its proportion of public hospital funding to 60 per cent. New health initiatives in the 2010-11 Budget include:

- Additional funding under *Every Patient Every Service*. This funding includes \$88.6 million for elective surgery to provide an additional 260,000 procedures. Elective surgery hubs will be established at Modbury Hospital and The Queen Elisabeth Hospital. Funding of \$109 million is dedicated to achieve the four hour emergency department target by 2013. \$9.8 million will be provided for 50 additional nurse practitioners capable of working in multidisciplinary teams in palliative care, aged care or other specialty areas.
- \$502.2 million will facilitate additional resources for health services over four years to meet additional costs. This amount also incorporates the removal of previous savings measures. The Budget papers do not provide details of what the savings measures were or why they are being reversed.
- \$3.8 million for additional resources for additional cancer services for country local health services.
- \$7.3 million in additional health resources associated with the redevelopment of the Women's and Children's Hospital

Major operating initiatives prior to the 2010-11 Budget included \$86.9 million in additional resources for sub-acute services and \$23.1 million in additional support for residential rural GPs (including \$2.6 million in 2009-10).

Expenditure details in the Budget for **Education and Children's Services** include appropriations in relation to measures announced prior to the Budget in addition to those announced in the Budget. Prior to the 2010-11 Budget, funding of \$12.2 million was provided for Indigenous Early Childhood Development under a National Partnership (including funding of \$1.1 million for 2009-10). \$16.4 million was also committed over four years to upgrade information technology and data management systems of the South Australian Certificate of Education (SACE) Board (\$10.6 million) and for additional assessment and moderation activities associated with the introduction of new SACE (\$5.9 million).

In the 2010-11 Budget the major new operating initiatives were:

- \$10.8 million in additional support for children's centres due to the establishment of 10 additional centres. The centres will offer a range of services including preschool, childcare and parenting services.
- \$9.7 million to support better behaviour centres and truancy officers. Six new better behaviour centres will be established to provide early intervention programs and support. An additional 12 truancy officers will also be employed.

- \$8.7 million to support specialist maths and science teachers. The funding will facilitate expansion of the numbers of maths and science teachers through a number of initiatives including recruitment of 40 graduates to train as teachers as well as supporting existing teachers to gain qualifications in maths or science.
- Non government schools will obtain \$16 million over four years. Half of this funding will be used to address student needs including behaviour management of students with English as a second language. The other half will support skill development of teachers in maths and science.

New operating initiatives for **Families and Communities** total \$332.9 million over the five years to 2013-14. Major initiatives concentrate on services for children and people with disabilities, including:

- \$162.9 million (including \$25.2 million in 2009-10) for children requiring alternative care arrangements and will include home based, residential and emergency care.
- \$72 million for Disability SA (including \$7.8 million in 2009-10) to support people with disabilities and carers. Assistance includes accommodation and community support, community access and respite services for carers.
- \$17.5 million (including \$3.7 million in 2009-10) to provide equipment to people with disabilities and clinical assessments.
- \$71.6 million to increase concessions and extend eligibility. Energy concessions will increase to \$150 per annum and will be indexed by five per cent annually until 2013-14. Similarly, water, sewerage and emergency services levy fixed property concessions will be indexed by five per cent. Eligibility for energy and the emergency services levy fixed property concession will be extended to low income earners.

The major expenditure initiative for **Further Education, Employment, Science and Technology** is \$136 million over four years for additional training places for a range of training courses from literacy and numeracy to higher level skill courses. The program will deliver 62,000 places over six years to 2015-16 (total cost of \$194 million). When combined with the Productivity Places Program an additional 100,000 training places will be provided.

Targeted Voluntary Separation Packages (TVSPs) will continue to be a substantial operating expense over the forward estimates period. The cost of additional TVSPs detailed in the 2010-11 Budget totals \$353.8 million over four years from 2010-11. Costs are estimated on the assumption that 3000 packages will be taken up at an average cost of \$118000. Table 8 above shows that the cost of TVSPs over the next four years is larger than the cost of operating initiatives for any government department with the exception of Health.

TVSP payments were made to 1187 employees in 2009-10 at a cost of \$126.9 million. The Auditor-General notes that there is a pay-back period of almost 18 months before the savings equal the cost of TVSPs (Auditor-General, 2010).

4.1.1.2 Expenditure savings

Total expenditure savings over the four years to 2013-14 will be \$1525.9 million (Foley, 2010a). These savings are in addition to substantial savings in previous budgets. Table 9 shows savings initiatives by portfolio for each year and the total savings over four years. The largest savings will be made in Health (\$316 million). Across government savings constitute the second highest amount (\$308.5 million) and relate primarily to changes in employment conditions for public sector workers, recalibration of the first home bonus grant and cessation of other benefits such as the fuel subsidy scheme.

Table 9 Savings by portfolio, 2010-11 to 2013-14

	2010-11	2011-12	2012-13	2013-14	Total
	\$ m	\$ m	\$ m	\$ m	\$ m
Legislature	-	-	-	-	-
Premier and Cabinet	3.8	8.6	17.0	25.0	54.4
Trade and Economic Development/Defence SA	14.0	23.5	29.9	34.9	102.3
Treasury and Finance	5.4	12.7	17.8	19.9	55.8
Planning and Local Government	0.5	0.9	1.9	1.9	5.1
Justice	4.8	18.4	29.2	32.2	84.7
Primary Industries and Resources	14.2	18.2	22.4	25.6	80.5
Transport, Energy and Infrastructure	6.9	31.2	37.2	43.4	118.7
Health	17.6	61.8	103.8	132.7	316.0
Education and Children's Services	8.7	28.3	49.1	59.6	145.7
Families and Communities	2.2	11.3	22.4	24.4	60.4
Environment	6.0	11.5	22.3	29.8	69.6
Water	2.5	3.2	3.6	3.4	12.5
Tourism	1.1	3.0	4.0	4.6	12.7
Further Education, Employment, Science and Technology	11.4	21.4	29.1	37.2	99.1
Across government	25.8	73.1	101.4	108.1	308.5
Total saving initiatives	124.8	327.2	491.2	582.7	1525.9

Source: (Foley, 2010c) 2010-11 Budget Measures Statement: Budget paper 6.

In contrast to the situation where new operating initiatives were relatively constant over the forward estimates, projected savings increase steadily over the period and more than offset the new expenditure measures by 2013-14 when total savings are \$582.7 million compared to total spending on new initiatives of \$465.5 million. Major savings initiatives are detailed below by portfolio. Savings for all portfolios include reductions in total salaries due to the large reductions in FTEs announced in the 2010-11 as well as ongoing savings from past reductions. Full details of all savings are in Budget Paper 6 (Foley, 2010c).

Premier and Cabinet has several savings initiatives of less than \$1 million for specific programs and rationalisation of functions. Major savings which were recommended by the Sustainable Budget Commission are:

- \$18 million reduction in government advertising
- \$13.3 million in reduced support to the arts

For **Trade and Economic Development** savings are concentrated on refocussing activities. The reduction in activities to provide general support to economic and trade activities reflected here offsets the expansion of more targeted programs as detailed in the previous section on new expenditure initiatives. Programs that have been wound back or scrapped include:

- \$21.9 million savings from streamlining international market development
- \$13.7 million savings from refocusing economic and industry policy
- \$14.7 million due to reduction of corporate functions

- \$11.2 million due to non-renewal of funding agreements for Innovate SA and the Technology Industry Association. Most of these savings are scheduled for 2012-13 and 2013-14.

Treasury and Finance will save a total of \$24.5 million through administrative efficiencies. Further savings of \$6 million will accrue due to the abolition of the Strategic Industry Support Fund.

Savings in **Justice** are concentrated on restructuring activities and the generation of Departmental efficiencies. The main components of savings are:

- Departmental efficiencies of \$23.2 million in the Attorney-General's Department; \$5.7 million in the Department for Correctional Services
- Establishment of the Building Communities Division is expected to save \$9.9 million
- \$9 million from the restructure of the South Australian Fire and Emergency Services Commission (SAFECOM)

Primary Industries and Resources will implement a number of efficiency and rationalisation measures. In addition, major initiatives include:

- \$46.3 million from the restructure of Rural Solutions SA and cost recovery (less revenue offsets of \$34.3 million)
- \$15.9 million due to reduction of state and externally funded research in SARDI (less revenue offsets of \$7.4 million)

Transport, Energy and Infrastructure will also focus on generating savings by improving efficiencies with such measures as:

- Departmental operational efficiencies of \$65 million
- Facilities management efficiencies of \$31.5 million over three years from 2011-12
- \$11.8 million from rationalisation of information and communication technology services

Health will implement significant savings measures which will offset new expenditure initiatives. Expenditure reductions will be achieved through:

- \$118 million from efficient price reform across metropolitan public hospitals
- \$76 million from reform of outpatient services
- \$56.9 million due to reform of corporate services
- \$30.7 million from the consolidation of medical imaging services, to be realised in the three years from 2011-12.
- \$13.4 million from consolidation of pharmacy services from 2011-12.

Education and Children's Services will implement the following savings measures:

- Discontinuing adult re-entry programs in public schools will save \$20.3 million over the three years from 2011-12
- Departmental efficiencies will save \$22.9 million
- \$8.1 million from cessation of Basic Skills Test grants
- Amalgamation of collocated schools will save \$8.2 million in 2012-13 and 2013-14

- Stopping continuous intake will save \$8.2 million in 2012-13 and 2013-14
- \$8.8 million due to ICT learning efficiencies
- \$12.1 million due to standardisation of arrangements for small school additional grants
- \$9.7 million from changes to the management of surplus teachers

Families and Communities savings measures span efficiency measures and changes in services such as:

- \$28 million due to the adjustment to rent assessments for pensioners in public housing.
- \$7.1 million savings from improving government service delivery and a further \$6.7 million from departmental efficiencies
- Reforms to delivery of financial assistance will result in savings of \$8 from 2011-12

Environment expenditure reductions will result from:

- \$26 million due to refocussing support for the State Natural Resources Management Program
- \$11.3 million savings due to efficiencies in corporate and business services and a further \$10.7 million for efficiencies in information technology services

Further Education, Employment, Science and Technology will reduce expenditure through administrative efficiencies, staff reductions and changes in services:

- \$21.1 million from salary savings due to staff reductions (including executives).
- Efficiency savings of \$21.3 million due to the departmental restructure and a further \$11 million for training and other services
- \$11.4 million due to the rationalisation of training support grants
- The creation of the Sustainable Industries Education Centre will produce savings of \$10.6 million

Across government savings of \$308.5 million over four years will accrue as a result of reductions in employment conditions for public sector workers, administrative changes and reductions in assistance to individuals and the community. The major measures are:

- Changes to the First home bonus grant will produce savings of \$76.9 million and the introduction of a property cap for eligibility for the First Home Buyers Grant will produce further savings of \$7.4 million
- Cessation of the petroleum subsidy scheme will produce savings of \$49.8 million
- Savings from management of the motor vehicle fleet will save \$28.2 million
- Rationalisation of support for Ministerial offices will save \$8.9 million
- Changes to conditions for public sector employees will result in savings of \$46.6 million for the two years to 2013-14 due to changes in recreation leave loading. A further \$90.7 million will be saved from 2011-12 as a consequence of reforms to long service leave accruals after 15 years of service.

4.1.2 Cuts to public sector employment and conditions

This section will discuss the reductions to public sector employment and conditions announced in the 2010-11 Budget. As outlined in the previous section the Budget proposed changes to public sector entitlements in relation to leave loadings and long service leave accruals. The abolition of the 17 per cent leave loading for recreation leave and provision of an additional two days leave will result in savings of 22.8 million in 2012-13 and 23.7 million in 2013-14 (total savings of \$46.6 million).

Long service leave is currently available after 10 years service. After 15 years service the accrual rate increases from 9 days per year of service to 15 days per year. The Budget initiative reduces the accrual rate after 15 years service from 15 days to 9 days. This will produce savings of \$90.7 million over three years from 2011-12 (\$28.7 million in 2011-12; \$30.1 million in 2012-13; \$31.9 million in 2013-14).

Table 10 FTE impact of new initiatives in 2013-14

	Expenditure initiatives (1)	Savings initiatives (2)	Total (3)
Premier and Cabinet	7	-63	-56
Trade and Economic Development	1	-90	-89
Treasury and Finance	6	-80	-74
Planning and Local Government	0	-18	-18
Justice	349	-206	143
Primary Industries and Resources	7	-186	-179
Department of Water, Land and Biodiversity Conservation	0	-17	-17
Transport, Energy and Infrastructure	0	-213	-213
Health	1277	-957	320
Education and Children's Services	66	-350	-284
Families and Communities	140	-108	32
Environment	2	-153	-151
Tourism	0	-51	-51
Further Education, Employment, Science and Technology	127	-183	-56
Total 2010-11 initiative FTEs	1981	-2673	-692
Previously announced savings requirements			-1070
Total FTEs			-1762

Source: (Foley, 2010a:2.6) 2010-11 Budget Statement: Budget Paper 3, Table 2.5.

The staff cuts continue and deepen the cuts previously imposed. Table 10 shows the impact of staffing initiatives from the 2010-11 Budget. Columns 1 and 2 show FTE increases and reductions respectively and the overall staffing position is shown in column 3. Staffing changes resulting from the 2010-11 Budget will result in an overall staffing reduction of 692 FTEs. When combined with reductions already announced for the forward estimates period (1070 FTEs) there will be an overall reduction of 1762 FTEs.

Column 1 shows staffing increases by portfolio to deliver the new initiatives outlined in Section 4.1.1.1. The additional staffing will be predominantly in front-line service delivery areas such as health workers, police, teachers, and child protection workers in line with the budget strategy. The FTE reductions in column 2 have not yet been identified.

The staffing reductions recently achieved and those planned for the future place a financial burden on the government in the short-term with the promise of savings in the future. The

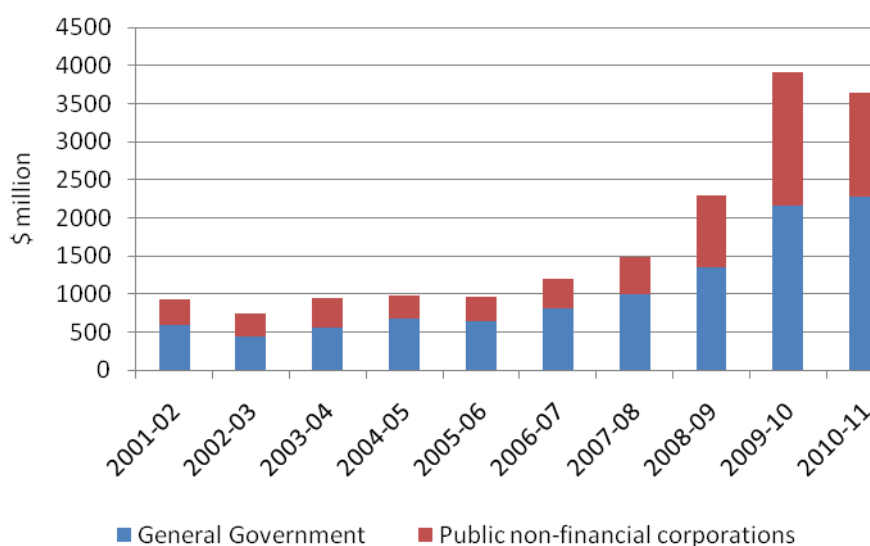
1187 TVSPs achieved in 2009-10 cost \$126.9 million and were estimated to produce savings of \$86.5 million in a full year (Auditor-General, 2010). It will therefore take around 18 months to recoup the cost of the packages. The additional 3000 TVSPs announced in the 2010-11 Budget are expected to cost a further \$353.8 million over four years. Other implications of the large staff reductions will be discussed in Section 5.

4.1.3 Capital expenditure

Figure 5 shows capital expenditure from 2001-02 to 2010-11. Capital expenditure in the general government sector is depicted in blue and expenditure by public non-financial corporations (PNFCs) is in red. Capital expenditure was flat in nominal terms and fell in real terms during the first half of this decade. Capital expenditure has increased following the introduction of the South Australia Strategic Plan in 2005 and the South Australian Infrastructure Plan in 2005. It has accelerated as a result of Commonwealth stimulus expenditure since 2008-09. Expenditure increased from \$1461 million in 2007-08 to \$2296 million in 2008-09 and then \$3868 in 2009-10 and an estimated \$3641 in 2010-11.

Investment for PNFCs will reach \$1381 million in 2010-11, down from \$1761 million in 2009-10. PNFC investment expenditure increased from around one-third of total investment in 2008-09 to more than 40 per cent in 2009-10. This was primarily due to large investment programs in 2009-10 by SA Water (\$1227 million) and the South Australian Housing Trust (\$393 million).

Figure 5 Capital expenditure, 2001-02 to 2010-11



Source: (Foley, 2010d) Capital Investment Statement: Budget Paper 5, 2010-11

Note: Figures to 2008-09 are actual expenditures, figures for 2009-10 are estimated results and figures for 2010-11 are budget figures

Investment will total \$10.7 billion over the forward estimates period to “rebuild and expand the state’s strategic economic and social infrastructure” (Foley, 2010d: 1). These investments include: the 100 gegalitre desalination plant to secure South Australia’s water supply, major road and rail projects and public housing construction and redevelopment. Investment expenditure for 2010-11 is detailed by portfolio in Table 11 along with estimated expenditure from 2009-10. Investment programs in the general government sector totalled \$2162 million in 2009-10 and will climb to \$2283 million in 2010-11.

Table 11 General Government investment, 2009-10 and 2010-11

	2009-10	2010-11
	\$m	\$m
Legislature	-	4
Premier and Cabinet	24	55
Trade and Economic Development/Defence SA	98	45
Treasury and Finance	13	18
Planning and Local Government	1	-
Justice	101	191
Primary Industries and Resources	7	9
Transport, Energy and Infrastructure	1005	953
Health	263	424
Education and Children's Services	539	721
Families and Communities	15	69
Environment	18	30
Water	19	6
Tourism	-	-
Further Education, Employment, Science and Technology	49	28
Auditor-General	-	-
Contingencies and other	9	29
Provision for capital slippage	-	-300
Total capital expenditure	2162	2283

Source: (Foley, 2010a:2.14) 2010-11 Budget Statement: Budget Paper 3, Table 2.10. Note: Figures for 2009-10 are estimated results and figures for 2010-11 are Budget estimates.

The increase in general government investment expenditure was concentrated in Education, Health and Transport and Communication (Foley, 2010a). Transport and Communication capital expenditure increased from \$601 million in 2008-09 to \$926 million in 2009-10 and will remain at the high level of \$752 million in 2010-11. Due to the *Funding the Education Revolution*, investment expenditure in Education increased from \$64 million in 2008-09 to \$583 million in 2009-10 and is expected to reach \$650 million in 2010-11. Investment in Health increased from \$183 million in 2008-09 to \$256 million in 2009-10 and the Budget estimate for 2010-11 is \$385 million.

4.1.4 Capital expenditure initiatives

This section details major new investment initiatives by portfolio for the general government sector announced in the 2010-11 Budget.

The major investment expenditure in the **Justice** portfolio is \$11.6 million investment associated with additional police resources and hi-tech fighting equipment

Transport, Energy and Infrastructure will invest \$488.5 million over four years in new initiatives such as:

- \$445.5 million over three years to 2013-14 for duplication of the Southern Expressway
- \$12 million in additional support over four years for the Rural Road Safety and Black Spot programs
- \$15.2 million for additional buses and services
- \$9 million for greenways and cycle paths
- Initiatives prior to 2010-11 budget

- \$29.9 million for refurbishment of Port Bonython jetty
- \$8 million for the road and rail upgrade for Greater Edinburgh parks

Department of Health investment will total \$153.1 million with major investments in:

- Modbury Hospital redevelopment will cost \$46 over the three years to 2012-13
- \$35.6 million for redevelopment of Queen Elizabeth Hospital in 2012-13 and 2013-14.
- \$ 64.4 million for redevelopment of Women's and Children's Hospital over 4 years

Education and Children's Services investment expenditure of \$106.9 million includes:

- \$60 million for expansion of state high schools
- \$16.5 million for amalgamations of co-located schools in 2011-12 and 2012-13) (there will be offsetting savings of \$8.2 million in 2012-13 and 2013-14)
- \$15.6 million for children's centres
- \$9 million for new disability units
- \$5.4 million for better behaviour centres

Investing initiatives prior to the budget for Education and Children's Services included:

- \$14.1 million in additional support for bus services
- Indigenous Early Childhood Development expenditure of \$13 million under a National Partnership

Families and Communities will invest \$10.7 million over 3 years to 2012-13 to improve government service delivery. This includes improving client access to Housing, Families and Disability services by replacing ageing service centres at The Parks Community Centre (this initiative will save \$7.1 million over four years and there will be ongoing savings of \$4.8 million per annum from 2013-14).

Further Education, Employment, Science and Technology will invest \$99.3 million in the Sustainable Industries Education Centre in the Sustainable Technologies precinct in Tonsley Park to provide a state of the art trade training facility for the building and construction, water and renewable energy industries. There will be some offsetting savings due to closure and sale of three TAFE campuses

4.2 Revenue

Revenues reached a historically high level in 2009-10, growing by 13.3 per cent to \$15530.8 million. This was a consequence of stronger than expected economic growth and the high level of revenue from the Commonwealth from the Nation Building – Economic Stimulus plan. This section will discuss the trajectory of various revenue streams over the forward estimates period.

Table 12 details general government sector revenues for the forward estimates period. Total general government sector operating revenues are expected to decline by 2.9 per cent in 2010-11; from \$15530.8 million in 2009-10 to \$15085.8 million in 2010-11. This is due to reductions in Commonwealth grants and reductions in some South Australian Government revenue streams.

Table 12 General government sector revenues

	2009-10	2010-11	2011-12	2012-13	2013-14
	Estimated result	Budget	Estimate	Estimate	Estimate
	\$ m	\$ m	\$ m	\$ m	\$ m
Taxation revenue	3640.5	3857.9	4188	4424.1	4656.6
Grant revenue	8857.2	8319.4	8163.9	8252.4	8101.1
Sales of goods and services	1932.7	1876.8	2040.6	2108.0	2146.8
Interest income	163.2	142.6	126.8	151.9	173.8
Dividend and ITE ^(a) revenue	425.0	353.1	388.2	420.2	549.1
Other revenue	512.2	536	619.8	648.1	666.5
	15530.8	15085.8	15527.3	16004.7	16293.8
% change on previous year	14.8	-2.9	2.9	3.1	1.8

Source: (Foley, 2010a: 3.5)2010-11 Budget Statement: Budget Paper 3, Table 3.3.

Note: Totals may not add due to rounding; (a) Income tax equivalent

Commonwealth grant funding includes general revenue (primarily comprised of GST revenue) and other grant revenue (SPP and NP agreements). **GST revenue** will increase steadily over the forward estimates period as the economy continues to recover and gains in consumer confidence are consolidated.

Other grant revenues from the Commonwealth will be negatively affected by the combination of the winding back of stimulus spending and reductions in some National Partnership grants. As a consequence, grant revenue will fall from 57 per cent of total revenue in 2009-10 to 55.1 per cent in 2010-11. The first full year effect of the cessation of the First Home Owners Boost scheme will be felt in 2010-11. There will also be a reduction in Commonwealth assistance in the form of exceptional circumstances drought funding. Capital grant revenue will contract sharply, from \$1819.4 million in 2009-10 to only \$201.4 million in 2013-14. Major reductions in Commonwealth grants include:

- Reduced grants to **South Australian Housing Trust** (from \$744.5 million in 2009-10 to \$458 m in 2010-11) due to reductions in Commonwealth Nation Building – Economic Stimulus Plan grants (\$299.2 million to \$100.9 million) and reductions under the National Partnership agreements on Social Housing and Remote Indigenous Housing (\$112.9 million to \$20.3 million in 2010-11).
- Reduced **Building the Education Revolution** stimulus funding to non-government schools (from \$306.9 m in 2009-10 to \$139.0 million in 2010-11).
- The Commonwealth brought forward \$34.3 million of **local govt assistance** grant for SA for 2010-11 to 2009-10.
- Payments to the **Department of Primary Industries and Resources** for the exceptional circumstances interest rate subsidies support measures will be reduced from \$41.9 million in 2010-11 to \$4.2 million in 2011-12.

According to the budget estimates, **taxation revenue** will increase from 25.6 per cent of total revenue in 2010-11 to 28.6 per cent in 2013-14. Over the same period sales of goods and services will increase from 12.4 per cent to 13.2 per cent and dividends and ITE revenue will increase from 2.3 per cent to 3.4 per cent.

Taxation revenues will increase due to economic recovery and tax measures in the 2010-11 Budget. Increased economic activity will have a positive impact on payroll tax and property

taxes in particular. The 2010-11 Budget contains a number of specific revenue measures. State fees and charges have been indexed by 3.3 per cent to reflect increased costs of service delivery. However, specific policy decisions have resulted in larger increases for some services:

- **Water usage charges** have been increased by around 32 per cent to comply with the National Water Initiative Pricing Principles that require SA Water to earn an economic rate of return on all investments. These increased charges will have a significant impact on household budgets, especially for low income earners.
- **Compulsory third party (CTP) insurance premiums** have been raised by 7.2 per cent to offset losses in asset values in the fund as a result of the GFC.

Dividend and ITE revenue will contract in 2010-11 (from \$425 to \$353.1 million). SA Water dividends are expected to fall from \$169 million in 2009-10 to \$105.4 million in 2010-11 while income tax equivalent revenue from SA Water is projected to decline from \$77.6 million in 2009-10 to \$49.7 million in 2010-11. The decline in SA Water contributions is due to higher operating expenses and debt levels as a result of major infrastructure projects. Contributions from Forestry SA and the Land Management Corporation are also expected to fall. Conversely, the dividend from the South Australian Financing Authority is expected to increase from \$11.5 million in 2009-10 to \$53.4 million in 2010-11 as investment returns recover.

4.2.1 Revenue initiatives, 2010-11 Budget

The major taxation measure in the 2010-11 Budget is the exemption of payroll tax on the wages of trainees and apprentices. This measure is expected to reduce revenue by \$29.2 million in 2010-11 and \$79.7 million in total over four years. Increases in stamp duty will increase revenues by \$50 million over the three years commencing 2011-12. The phasing out of the payroll tax exporters rebate scheme will raise \$9.8 million over three years from 2011-12. Increased motor vehicle fees will boost revenues by \$22.9 million over the three years from 2011-12. The reduction in payroll tax in 2010-11, while revenue raising measures commence one year later, results in a drain on revenue for that year.

Provision of land tax relief prior to the Budget will reduce revenues by \$338.6 million over the four years to 2013-14. The abolition of stamp duty on non-real property transfers and non-quoted marketable securities in compliance with the Intergovernmental Agreement on the Reform of Commonwealth-State Financial Arrangements will reduce revenue by \$40.9 million in 2012-13 and \$43.2 million in 2013-14.

Non taxation revenue measures will add \$406.5 million to revenues over the four years to 2013-14 with only \$11.4 million in 2010-11 (see Foley, 2010c, Table 1.2 for further details). Specific revenue measures by portfolio include:

- The **Justice** portfolio will raise an additional \$44.8 million through an increase in expiration fees and \$48.9 million due to an increase in the Victims of Crime Levy.
- **Primary Industries and Resources** will gain a \$64.5 million increase in mining royalties, with most of the revenue raised in 2012-13 and 2013-14.
- **Transport, Energy and Infrastructure** will raise an additional \$36.5 million through increases in fees for driver's licences and \$22.8 million for taxi licences. The introduction of fees for land title information will raise a further \$11 million.

- **Health** will raise \$16 million by sub leasing office space.
- **Environment** will boost revenues by \$17.7 million through an increase in the Solid Waste Levy and a further \$8.3 million by cost recovery measures for coast protection.
- **Water** will use cost recovery for water planning and management to raise a total of \$44.6 million.
- **Further Education, Employment, Science and Technology** will increase fees to boost revenues by \$9.9 million with \$7.5 million coming from increased student fees.

5 Impact of the 2010-11 Budget on the public service

The 2010-11 Budget cuts to FTEs in the public sector continue and accelerate staffing cuts that have occurred in recent years. Following a review of spending designed to prioritise front-line services, the 2006-07 Budget introduced savings of \$695 million over four years and introduced an annual 0.25 per cent efficiency dividend. In response to the GFC the Government announced a reduction of 1600 FTEs in the three years commencing 2009-10. The 2010-11 Budget included further reductions of 2673 FTEs.

The rationale for the staff cuts has been twofold:

- the Budget position requires expenditure cuts; and
- it is necessary to eliminate backroom, administrative positions in order provide front-line workers to deliver services to the community.

Staff reductions are to be achieved by not filling vacancies or by identifying positions that are no longer required. Some reductions have been achieved by efficiency measures. Others are achieved by offering staff Targeted Voluntary Separation Packages (TVSPs). TVSPs will offer non executive staff 20 weeks pay plus three weeks pay for each year of service up to a maximum of 116 weeks pay.

There will be considerable encouragement for employees who are declared redundant to take up the TVSPs. First, after six months redeployment the maximum package will be reduced to 88 weeks pay. The second means of encouraging take up is the threat of forced redundancies. To date Government policy has included a commitment that there would be no forced redundancies. The sustainable Budgets Commission recommended that “there should be a non-voluntary separation policy for managing staff who are excess to agency requirements” (Sustainable Budget Commission, 2010: 84). The Government has moved away from its commitment, announcing in the 2010-11 Budget that “if the required reduction in employee numbers is not achieved in 12 months through redeployment and voluntary separation packages, the government will reconsider its ‘no forced redundancy’ policy” (Foley, 2010e: 5).

To date there have been significant staffing reductions through natural attrition and TVSPs. As mentioned previously there were 1187 TVSP packages in 2009-10. TVSPs were to be made available to employees whose position was being abolished and these positions were to be removed from departmental structures. The Auditor-General found that “It is not clear that agency structural and management arrangements and systems, support the ability to demonstrate that positions are abolished as part of a TVSP settlement” (Auditor-General, 2010: 6).

Aside from the impact of redundancy on the public sector workers made redundant and their families the staff cuts have three potential impacts:

- Reductions in economic activity;

- Repercussions for remaining employees; and
- Effects on service delivery

5.1 Impact on economic activity

The job cuts will occur in a period where the boost to economic activity from the stimulus measures is winding down. The withdrawal of the stimulus in combination with the public sector job losses and other saving measures will reduce economic activity. Private sector activity will need to increase commensurately to ensure that the productive resources released from these activities are fully employed.

Cook and Mitchell (2009) found that the 1600 FTE reduction announced in the 2008-09 MYBR would result in a reduction in employment in South Australia of between 5268 and 5432 FTE jobs when the full effects of the spending reductions worked through the economy. Since around one-third of jobs in South Australia are part-time the actual reduction in jobs would be higher. The job cuts announced in the 2010-11 Budget are much larger and will have an even greater impact on employment levels.

Job destruction of this magnitude will also cause the number of unemployed to increase in the short-term. Since many of the redundant workers are likely to be older workers it is possible that some would remain unemployed for long periods of time. This would shift the fiscal burden to the Commonwealth through increased claims for Newstart and other benefits in addition to the loss of income tax revenue that would be paid if these workers had jobs. Additional cost for the Commonwealth include the provision of services such as Centrelink, Job Services Australia. Both the Commonwealth and State Governments could face additional costs associated with increased need for community services, health and housing assistance.

5.2 Impact on remaining workers

While redundancies are supposed to eliminate the duties of the position this may not be the case and some of the duties of redundant workers may be redistributed to other staff. Remaining employees may be required to accept additional duties without sufficient training and without the prospect of mentoring by the previous incumbent. Moreover, where previous functions are not performed there could be repercussions for continuing workers due to reduced support or access to information. The removal of administrative workers may result in processing delays that impact on customers with repercussions for front-line workers who are increasingly dealing with frustrated and angry clients (Rafferty, Schutz and Yu, 2010).

Even in situations where work intensification does not occur there are likely to be major impacts on the working lives of the remaining workforce. During the period of uncertainty about whether individuals will be directly affected by redundancy, efficiency and work output will deteriorate. The continual downsizing process is likely to increase stress levels, induce concerns for the future and reduce commitment of employees who feel that they cannot trust their employer and are not valued. Therefore, work performance may decline and absenteeism may rise, resulting in additional stress on the remaining workforce.

5.3 Impact on service delivery

The Budget strategy enunciated by the Government was to reduce administrative costs so that there would be less impact on front-line services. There are a number of factors that determine the impact on front-line workers and the quality of service delivery.

There is a danger that a large proportion of workers made redundant are among the most productive and experienced. This is because individuals faced with the prospect of voluntary redundancy weigh up the costs and benefits of accepting the offer. Those with the best prospects of securing employment elsewhere are more likely to accept the package while those with few employment prospects are likely to seek redeployment because the long-term cost outweighs the short-term benefit of accepting the offer. The loss of experienced, productive staff is compounded by the loss of corporate memory, reducing the organisation's ability to deliver high quality services.

As mentioned previously, front-line workers may be affected through the loss of support services or through increased workloads. Another important issue is whether there is a clear division between administrative staff and front-line staff. Given the Government contention that redundancies will be concentrated in back office administrative positions, with the implicit assumption that these positions have minimal impacts on service delivery, it is important to ascertain whether this is, in fact, the case.

5.4 The experience of South Australian public servants

A recent survey of 3000 South Australian public servants by Rafferty, Schutz and Yu (2010) provides some insight into these issues. The survey was conducted following the announcement of the 1600 FTE staff cuts and sought to investigate experiences with previous staff reductions as well as expectations about current and impending cuts. The survey found that there is no clear delineation between back office administration and front-line staff.

A high proportion of workers were involved in front-line service delivery in some way. Around 30 per cent of respondents described themselves as predominantly engaged in front-line service delivery and 27 per cent as predominantly administrative support. However, 43 per cent said that they performed a combination of front-line and administrative functions. Rafferty, Schutz and Yu (2010: 4) conclude:

Put simply, we found that the planned cuts in staffing of the public sector can be expected to have a deleterious effect on the availability and quality of public services, and will increase workload pressures on remaining staff. The proposition advanced by the Government – that by concentrating cuts on so called back office administrative staff, the cuts will not affect services finds no support in this research.

Respondents reported significant working issues including working unpaid overtime (55 per cent), not being able to get through their workload during normal working hours (30 per cent), having too large an administrative burden (36 per cent) and feeling stressed or overworked (39 per cent).

Of those who had experience staff cuts in the past: 80 per cent experienced more stress and pressure; 70 per cent reported increased workloads, 55 per cent reported an increase in administrative duties that took them away from front-line service delivery. In addition, there were longer queues (45 per cent), delays in meeting client needs (73 per cent), failure to meet client needs (54 per cent) and more aggression toward staff (55 per cent). Moreover, 57 per cent reported performing duties without appropriate training. In total, 66 per cent of service delivery workers were of the opinion that further staff cuts would result in “a one-for-one or greater diminution of service delivery” (Rafferty, Schutz and Yu, 2010: 22).

The magnitude of the staff cuts to be achieved over the next four years and the evidence of the adverse impacts of previous staff reductions suggests that there will be reductions in working conditions for remaining staff and that the quality of service delivery is also likely to decline. The stated intention of the Government of harvesting staff reductions predominantly

from administrative functions is likely to be extremely difficult to achieve since the majority of public sector workers have at least some service delivery functions.

6 Analysis of Budget outcomes

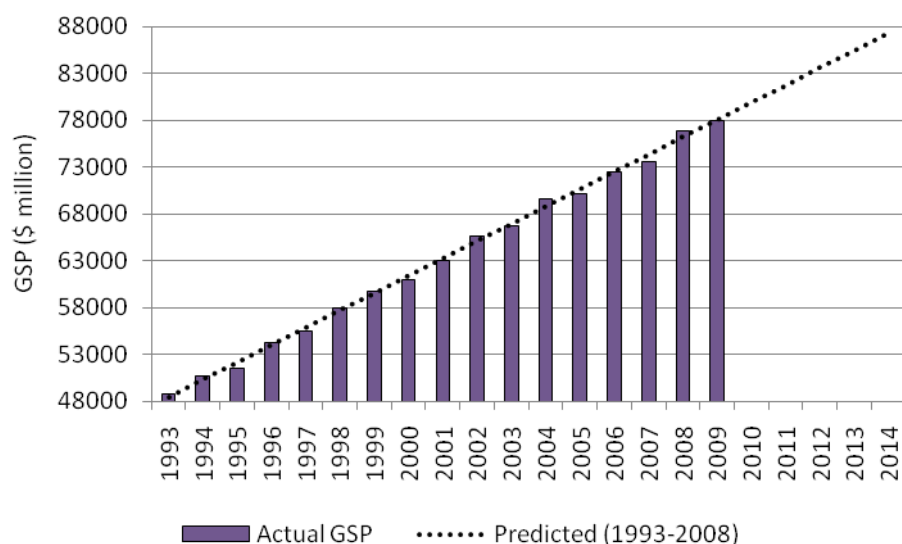
6.1 Budget outcomes in South Australia

The global downturn resulting from the GFC impacted on government finances in a number of ways. At the Commonwealth level there was a negative impact on the budget due to the fall in revenues and additional expenditure on income support payments as the automatic stabilisers were activated. There were further large impacts on the budget bottom line due to large expenditures to stimulate economic activity and support employment.

In 2009-10, the Commonwealth fiscal balance was in deficit by \$52.9 billion or 4.1 per cent of GDP (Swan and Tanner, 2008; Swan and Wong, 2010). This followed a deficit in 2008-09 of \$29.7 billion or 2.5 per cent of GDP and a surplus of 1.9 per cent of GDP in 2007-08. Australian Government revenue fell from 26.8 per cent of GDP in 2007-08 to 22.5 per cent in 2009-10 and expenses increased from 24.8 per cent to 26.1 per cent of GDP.

The economic downturn has also impacted on the level of economic activity and the fiscal outcomes in South Australia since 2008. Figure 6 shows Gross State Product (GSP) in South Australia to 2008-09 and suggests that there has been only a mild impact on the recent economic slowdown on the South Australian economy. The GSP figures for 2010 are not yet available. The small impact on GSP to 2008-09 may be attributable to Commonwealth expenditure on various stimulus measures designed to support economic activity and employment.

Figure 6 GSP and predicted GSP

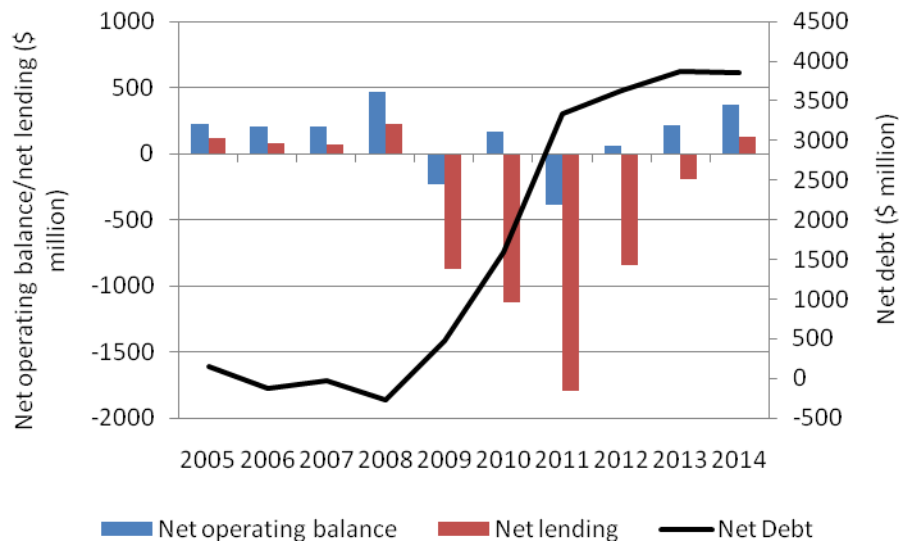


Source: (ABS, 2009c) Cat no. 5220.0 Australian National Accounts: State Accounts, Table 1: Gross State product, Chain volume measures and current prices.

The columns in Figure 6 show actual GSP from 1993 to 2009. An OLS regression using data from 1993 to 2008 was used to construct a trend line for the period prior to the GFC and the estimates were then used to forecast future GSP. These values are represented by the dotted line. The Figure shows that GSP growth has been very stable over the entire period with only minor deviations from trend growth. Actual GSP in 2008-09 is around \$60 million below the predicted value. However, this result may represent a financial year with above trend growth

in the beginning of the year and below trend growth in the remainder of the year. There may be more substantial shortfalls in GSP in 2009-10 which is the first full financial year after the GFC as well as in subsequent years. Notwithstanding the mild economic effect of the slowdown following the GFC, there may be a substantial effect on the State Government fiscal position.

Figure 7 Fiscal outcomes for South Australia, 2004-05 to 2013-14



Source: (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3, 2010-11

Note: 1998-99 to 2008-09 are actual outcomes; 2009-10 to 2013-14 are forecasts

Figure 7 shows that after several years of net operating surpluses, expenses outstripped revenues in 2008-09 to produce a net operating deficit. The situation was reversed in 2009-10 and a net operating surplus is expected in the forward estimate period with the exception of 2010-11 where a net operating deficit is forecast. Net lending was positive until the adverse impact of the GFC and increased infrastructure investment combined to produce a net borrowing outcome in 2008-09. This situation will continue to produce net borrowing until 2012-13 and then return to a position of net lending. As a result of increased investment and the net operating deficits, net debt increased rapidly from 2008-09 and will record lower growth from 2011-12.

6.2 Understanding budget outcomes

The State Government's budget balance which is published in the Budget Papers each year is the difference between total state revenue and total state outlays. So if total revenue is greater than outlays, the budget is in surplus and vice versa. Many observers and politicians use the actual reported budget balance to indicate the fiscal stance of the government. So if the budget is in surplus they conclude that the fiscal impact of government is contractionary (withdrawing net public spending) and if the budget is in deficit they conclude that the fiscal impact is expansionary (adding net public spending).

However, the complication is that we cannot then conclude that changes in the fiscal impact reflect discretionary policy changes. The reason for this uncertainty is that there are automatic stabilisers which are in-built into the budget outcome and vary with the level of economic activity independent of discretionary policy changes.

To see this, a simple model of the budget balance can be written as:

Budget Balance = Revenue – Spending.

Budget Balance = (Tax Revenue + Other Revenue) – (Welfare Payments + Other Spending)

We know that Tax Revenue and Welfare Payments move inversely with respect to each other, with the latter rising when growth in State Product falls and the former rises with growth in State Product. These components of the Budget Balance are the so-called automatic stabilisers. In other words, without any discretionary policy changes, the recorded Budget Balance will vary over the course of the business cycle.

When the economy is weak – tax revenue falls and welfare payments rise and so the Budget Balance moves towards deficit (or an increasing deficit). When the economy is stronger – tax revenue rises and welfare payments fall and the Budget Balance becomes increasingly positive. Automatic stabilisers attenuate the amplitude in the business cycle by expanding the budget in a recession and contracting it in a boom.

As a result, we cannot conclude that a rising budget deficit indicates that the State government has suddenly become of an expansionary mind. In other words, the presence of automatic stabilisers makes it hard to discern whether the fiscal policy stance (chosen by the government) is contractionary or expansionary at any particular point in time. Any statements that suggest the budget deficit is "too large" and program cut-backs are required thus have to be assessed with considerable caution.

To overcome this uncertainty, economists devised what was called the Full Employment or High Employment Budget. In more recent times, this concept is now called the Structural Balance. The Structural Balance is a hypothetical budget balance that would be realised if the economy was operating at potential capacity or full employment. In other words, we would calibrate the budget position (and the underlying budget parameters) against some fixed point (full capacity) and thus eliminate the swings in the budget balance that arise from variations in the business cycle. These cyclical swings in activity around full employment or capacity would be separated out from the underlying budget position which would reflect the discretionary fiscal stance chosen by the government.

If the structural component of the budget outcome is balanced then it means, conceptually, that total outlays and total revenue would be equal if the economy was operating at total capacity. If the budget was in surplus at full capacity, then we would conclude that the discretionary structure of the budget was contractionary and vice versa if the budget was in deficit at full capacity.

An important point to understand is that the actual budget balance is to a major extent out of the control of the State government because the cyclical component reflects the variations in the spending decisions of private sector agents (household, business firms, external relations). As a result, it is often counter-productive for a government to attempt to cut back the budget outcome with discretionary spending cuts and/or taxation increases because it fears the budget balance is excessive. In these circumstances, the imposition of austerity may then cause State Product to contract and the automatic stabilisers (principally, tax revenue at the State level) to push the budget further into deficit. It also follows that a growth strategy underpinned by discretionary stimulus spending and/or tax cuts can drive reductions in the budget deficit outcome as the level of economic activity increases and tax revenues recover.

We thus urge caution when dealing with discussions surrounding the dynamics of the State budget and efforts have to be taken to decompose the structural and cyclical components of the actual reported budget outcome before any analysis of the discretionary fiscal stance is

engaged. It is impossible to make any sense of the appropriateness of the fiscal stance of the State government without undertaking this decomposition.

In the following Section, we attempt to provide some guidance on these components. It is not an exact science but aims to provide a starting point for further State government analysis. It is simply unacceptable to conduct discussions about the appropriateness of the fiscal stance by only referencing the actual reported budget position.

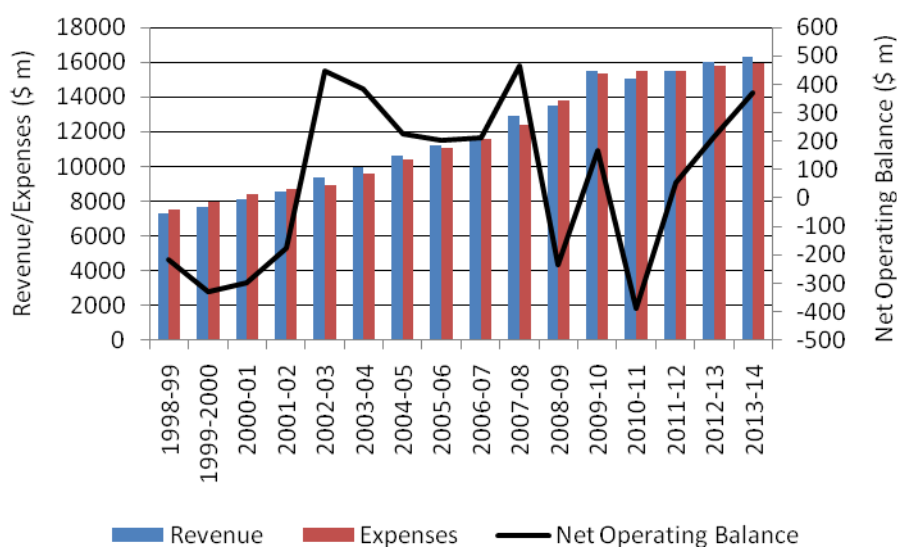
6.3 The cyclical budget component

As explained above, to fully appreciate the impact of variations in the business cycle on the actual budget outcome, we need to decompose the aggregate movements into those movements which indicate cyclical changes in the level of activity (the cyclical or automatic stabiliser component) and the movements that arise from discretionary changes in fiscal policy parameters.

Several techniques have been developed to estimate the structural budget deficit at the national level. Estimates are produced by the IMF and the OECD using somewhat different methodologies. In general, the process involves three main steps: estimating potential output and the output gap (the gap between potential and actual output); quantifying the cyclical component of expenditures and revenues; and subtracting the estimated cyclical components from the actual levels. Calculations of the Structural Balance are complex and sensitive to underlying assumptions so they provide indicative rather than precise estimates.

In the following discussion we provide some guidance on what the movements in the cyclical and structural components may have been in recent years. We attempt to evaluate the cyclical budget component for South Australia by examining budget revenues and expenditures in order to make some approximate estimates of the Structural Balance. We restrict the analysis to an examination of the net operating balance. Capital investments are excluded from the analysis because it is inappropriate to include long-term financial commitments and benefits. Investments will deliver economic and social benefits over the life of the assets and will be financed over the same period.

Figure 8 Revenues, expenses and net operating balance, South Australia



Source: (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3.

Notes. Figures for 1998-99 to 2009-10 are actual, figures for 2010-11 are proections.

In 2009-10 and 2010-11 revenue and expenses are impacted by the Stimulus Plan

Figure 8 above shows revenues, expenses and the net operating balance for South Australia from 1998-99 to 2013-14. Revenues and expenses increased significantly in 2008-09 and 2009-10. In 2009-10 revenues increased by 12.3 per cent in real terms while expenses increased by 9.2 per cent. Both revenue and expenses peaked in that year at around 19 per cent of GSP. The increases were primarily due to the Commonwealth economic stimulus packages and Figure 8 above shows that outlays and receipts will stabilise (at around 16 per cent of GSP) over the forward estimates period. The net operating balance exhibits a counter-cyclical pattern with strong surpluses in the period of economic growth prior to the GFC turning to temporary deficits afterward before returning to surplus.

The impact of the economic downturn on the South Australian budget position operates through both revenues and expenditures. The revenue effects may be due to the effect of changes to revenues received from the Commonwealth or direct impacts on State revenues. Expenditure effects at the State level are much smaller than at the federal level since welfare payments are primarily a federal responsibility. There may be spill-over effects due to a deterioration in living standards of those directly affected, or by the social consequences that may include increased crime or adverse impacts on health or family functioning. In national estimates of cyclical effects, expenditure effects are generally limited to the impact of additional welfare payments due to higher unemployment. This is not relevant to South Australia since welfare payments are the responsibility of the Commonwealth. The major expenditure effect in South Australia has been due to spending generated by the Commonwealth's economic stimulus measures.

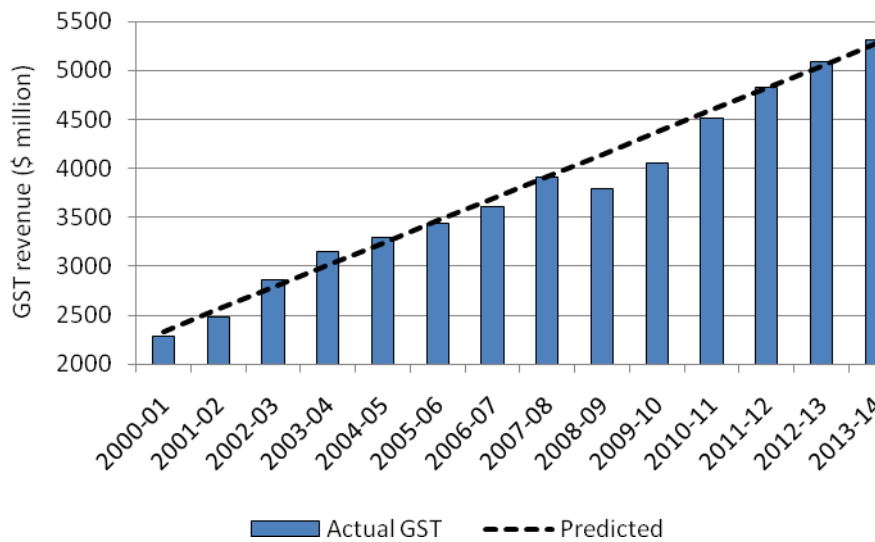
6.3.1 Payments from the Commonwealth

This section will consider and attempt to quantify the major impacts of the cyclical downturn on South Australia's fiscal position due to variations in Commonwealth payments to South Australia. The major impacts on revenues from the Commonwealth Government are through ongoing revenue streams that are sensitive to variations in economic activity such as GST revenue and discretionary expenditure as part of the various components of stimulus initiatives.

Figure 9 shows actual and forecast GST revenue from 2000-01. The columns represent actual GST revenue transferred from the Commonwealth to the South Australian Government from the introduction of the GST in 2000-01 until 2008-09 and forecast GST revenue from 2010-11 to 2013-14. The dotted line represents predicted values which are an attempt to remove the variation in GST expenditure emanating from cyclical factors. Predicted values were estimated by using an OLS regression to estimate GST revenue for the period prior to the GFC (2000-01 to 2007-08). The estimated model was then used to predict future values over the forward estimates period.

The cyclical impact of the economic slowdown is evident in Figure 9. GST revenues were affected by the slowdown in economic activity after the GFC as consumers adopted a more cautious attitude to discretionary expenditure. There is a sharp drop in actual GST revenue in 2008-09 (from \$3914 million in 2007-08 to \$3786 million in 2008-09). GST revenue deviated from the trend rate by \$315 million in 2009-10 and, according to the forward estimates revenue will return to trend by 2011-12.

Figure 9 South Australian GST revenue, 2000-01 to 2013-14 (actual, forecast and trend)

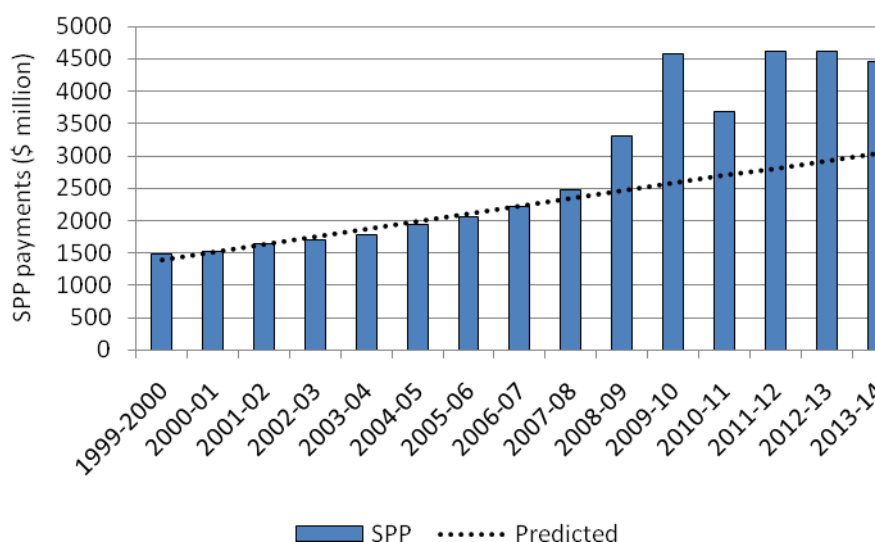


Source: Commonwealth Budget Paper 3, 2010-11; Final Budget Outcomes, various years

Note: Figures up to 2009-10 are actual, figures from 2010-11 are estimates.

The second pathway for cyclical revenues to affect the South Australian Budget is through Commonwealth funding under the economic stimulus packages that comprises part of Specific Purpose Payments (SPPs). Specific Purpose Payments (SPP) to the States increased by 30 per cent in 2008-09 and a further 26 per cent in 2009-10 but will decline by 13.5 per cent in 2010-11 as the stimulus measures are wound back (Swan and Tanner, 2010b). The large increases in SPPs to the States counteracted the negative impact of the GFC on GST revenues and provided a further impetus to economic activity.

Figure 10 SPP and NPP payments to South Australia



Source: Final Budget Outcomes, (comm), various years; Budget Paper 3, 2010-11 (comm)

The increases in SPPs are evident in the Figure 10 that shows SPP grants to South Australia. The columns show the actual SPP payments (incorporating NPP payments) received by the State between 1999-2000 and 2009-10 along with forward estimates from the 2010-11 budget. The dotted line is the trend of what SPP payments would have been the past

trajectory had been maintained. The impact of additional expenditure from the economic stimulus packages is evident in the large rise in grants from 2008-09, taking payments above the trend. The graph shows that this is a temporary injection of funds since grants fall substantially in 2010-11. The forward estimates are affected by the new arrangements for health funding that will result in the transfer of part of the States GST grants to SPP for public hospitals from 2011-12 (with the exception of Western Australia) as part of the *National Health and Hospitals Network Agreement*.

The impact of the stimulus packages on the finances of South Australia has been considerable (Swan and Tanner, 2010b). General government sector operating revenues in South Australia grew by 12.3 per cent (in real terms) in 2009-10 mainly due to Commonwealth funding for the Nation Building – Economic Stimulus Plan. These revenues are expected to decline by 2.3 per cent in 2010-11 due to decreased Nation Building funding, discontinuation of the First Home Owners Boost scheme in December 2009 and reduced expenditure for exceptional circumstances drought relief.

Table 13 shows the SPP and NP payments to South Australia as part of the economic stimulus package. The largest payments were in 2009-10 with payments totalling \$1733 million. Grants will be reduced from 2010-11 as the stimulus expenditure is wound back.

Table 13 SPP and NPP payments due to economic stimulus measures

	2009-10	2010-11	2011-12	2012-13	2013-14
	\$ m	\$ m	\$ m	\$ m	\$ m
National Building and Jobs Plan - Building the Education Revolution	826.9	456.1	42.7	0.0	0.0
Nation Building and Jobs Plan-Social Housing	294.0	100.9	14.7	0.0	0.0
National Building Program- road and rail	448.3	118.7	224.2	299.1	156.5
Nation Building Plan for the Future- Major sites (road and rail)	5.0	27.1	28.9	0.0	0.0
Regional and Local Community Infrastructure Program - Local Governments	20.3	17.6	0.0	0.0	0.0
National Building Package -TAFE facilities	14.6	0.0	0.0	0.0	0.0
First Home Owners Boost	77.3	5.3	0.7	0.0	0.0
Jobs Fund - Infrastructure employment projects	0.4	0.8	0.0	0.0	0.0
Exceptional circumstances assistance	46.6	13.2	0.0	0.0	0.0
Total	1733.3	739.7	311.2	299.1	156.5

Source: (Swan and Wong, 2010: Swan and Tanner, 2010a)

There is a mismatch between the timing of the receipt of grants from the Commonwealth for the Nation Building – Economic Stimulus Program and expenditure by the State. Most of the payments from the Commonwealth were received by the States in 2009-10 although expenditure is spread over a longer time period. Stimulus expenditure by the States was around \$10.2 billion in 2009-10 and is expected to reach \$5 billion in 2010-11. This pattern is evident in South Australia. Grants from the Commonwealth for schools totalled \$826.9 million in 2009-10 but South Australian expenditure was only \$474.5 million. Similarly, part of the \$294 million in Commonwealth grants for social housing in 2009-10 will be realised in 2010-11 (expenditure on social housing under the program was \$201.6 million in 2009-10).

6.3.2 State Government revenues

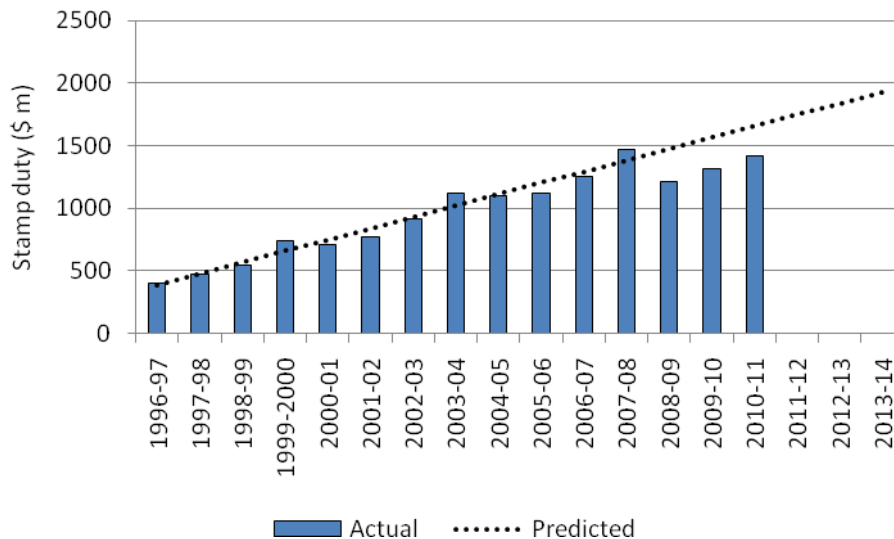
State governments do not levy income taxes nor are they responsible for increased income support payments during periods of reduced economic activity. They are therefore less exposed to economic downturns than the Commonwealth. Grants from the Commonwealth account for around half of the revenue of State Governments and are relatively stable with the exception of GST revenues which are pro-cyclical and, in the aftermath of the GFC, Commonwealth discretionary expenditure in the form of anti-cyclical stimulus expenditure, as detailed in the previous section.

The most important State generated revenue streams relate to fees and charges for transactions and services provided by the public sector. Investments by the State and income from PNFCs also contribute to revenue. For revenues generated at the State level the major cyclical impacts are due to variations in stamp duty and payroll tax receipts.

6.3.2.1 Stamp duty

Revenue collections fell in 2008-09 due to the impact of the GFC. Figure 11 below shows actual stamp duty receipts to 2008-09 and trend or predicted amounts based on the period 1996-97 to 2007-08 (prior to the GFC). The deterioration in economic activity had a large impact on stamp duty receipts that declined in nominal terms from \$1470 million in 2007-08 to \$1218 million in 2008-09. Improvements in stamp duty collections are expected for 2009-10 and 2010-11 so that revenue in 2010-11 is expected to be \$1421.6 million. If this amount is achieved stamp duties will remain around \$235 million below the trend rate. The shortfall from 2008-09 is cyclical and revenue should return to trend in the longer term.

Figure 11 Stamp duty revenue, South Australia



Source: Department of Treasury and Finance, South Australia: Annual Reports, various years; (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3. Note: Figures to 2008-09 are actual receipts. From 2009-10 they are estimates.

The decline in stamp duties has been driven primarily by the sharp fall in conveyancing revenues on property sales which declined from \$931 million in 2007-08 to \$734 million in 2008-09, while conveyancing on share sales declined from \$11 million to \$6 million in the same year.

Figure 12 Median house prices and house transfers, Adelaide, 2002 to 2009



Source: (ABS, 2010e) Cat no. 6416.0, 2010 House Price Indexes: Eight Capital Cities

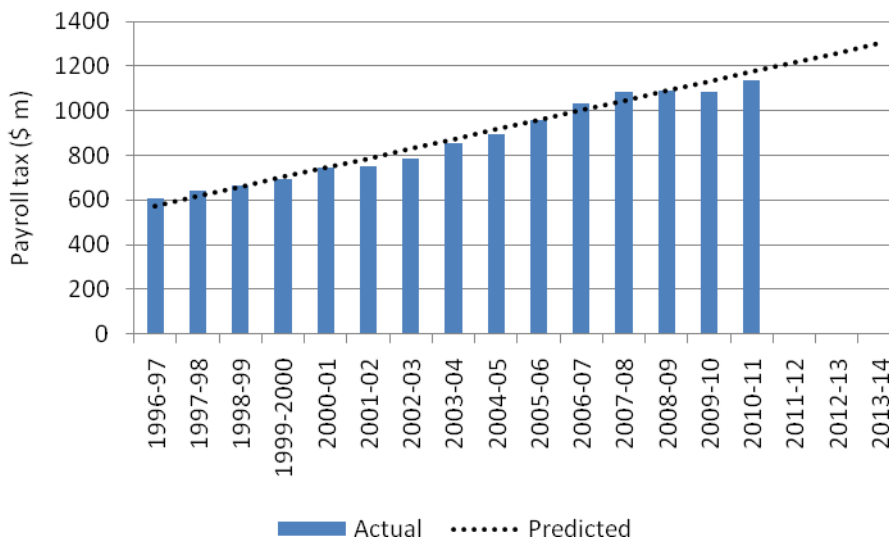
Conveyancing revenues were affected by falling property values and a significant fall in the number of established house sales. Figure 12 shows that the median price of established houses in Adelaide fell in late 2008 and early 2009 before recovering strongly. In addition to the price fall there was an even more dramatic decline in the number of transfers of established houses that had a major impact on conveyancing revenues. In June 2007 the number of house transfers reached a peak of 5830 houses. The subsequent fall and partial recovery meant that house transfers only reached 4909 by June 2009 and then declined again.

6.3.2.2 Payroll tax

The second major source of revenue that is likely to respond to cyclical factors is payroll tax. South Australia levies payroll tax at a rate of 4.95 per cent on businesses with payrolls in excess of \$600,000 per annum. The rates and thresholds for payroll tax have been amended over time with rates gradually being reduced from 5.75 per cent in 2001 to 4.95 per cent from 1 July 2010. Figure 13 shows actual payroll tax receipts between 1996-97 and 2008-09 and estimates to 2010-11. The trend over the pre-GFC period has been used to forecast future trend revenues. Figure 13 shows that payroll tax revenues exhibit cyclical variations with receipts below trend between 1999-2000 and 2004-05 and above the trend amount from 2006-07 to 2008-09. As a consequence of the economic slowdown payroll taxes fell \$45.7 million short of trend in 2009-10 and despite signs of recovery they are expected to remain \$40.4 million below trend in 2010-11.

For the forward estimates period payroll taxes will be impacted by structural as well as cyclical factors. From 1 July 2010 employers of trainees and apprentices are exempt from liability for payroll taxes at an estimated cost to the Government of \$29.2 million in 2010-11 and a further \$50.5 million over the forward estimates period).

Figure 13 Payroll tax revenues, South Australia

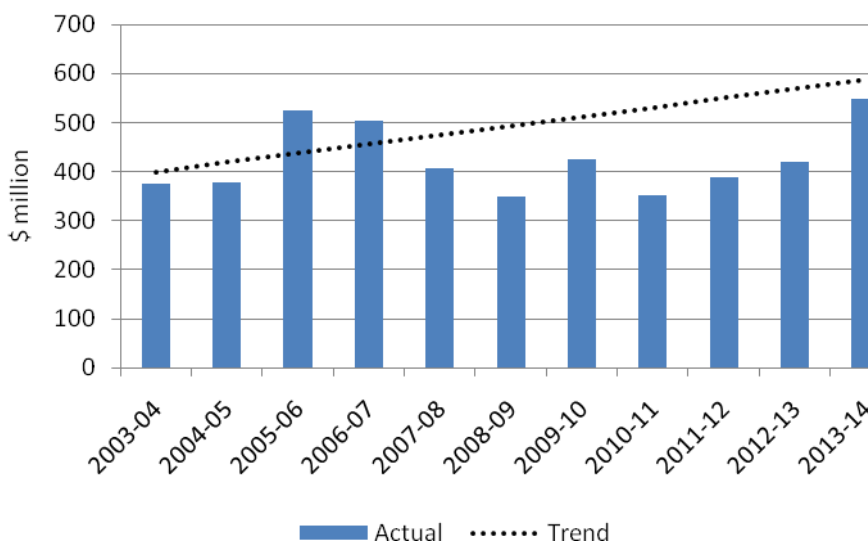


Source: Department of Treasury and Finance, South Australia: Annual Reports, various years; (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3.

6.3.2.3 Other revenue

Transfer payments from public non-financial corporations (PNFCs) and public financial corporations (PFCs) are another source of revenue for the South Australian Government. These corporations make dividend payments and also contribute income tax equivalents. The actual and forecast contributions are shown in Figure 14. The trend was calculated using data from 2003-04 to 2007-08 and future trend values were forecast by extending the trend to show the growth path if the trend had continued. Dividends and ITE payments have been below trend since 2007-08 and will not reach the trend rate by 2013-14.

Figure 14 Dividends and ITE from PNFCs and PFCs



Source: Department of Treasury and Finance, South Australia: Annual Reports, various years; (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3.

Expected revenues from these sources in 2009-10 and 2010-11 are detailed in Table 14 below. Changes in the forward estimates for dividends and income tax equivalents for PNFCs are mainly due to structural rather than cyclical factors. The major reduction in revenue stems from a significant fall in both dividends and income tax equivalent revenue from SA Water. SA Water has been affected by water restrictions and increased expenses due to investment in the desalination plant to ensure adequate, good quality drinking water to the community.

The size of dividend payments continues to be adversely affected by past policy decisions such as the privatisation of electricity. While privatisation provided short-term gains in terms of reduced interest payments on debt it has continuing budget impacts on the Government's revenue raising ability. In 1998-99 the Electricity Trust of South Australia (ETSA) contributed dividends of \$103.3 million and tax equivalent payments of \$52.7 million (Lucas, 1999). It is reasonable to assume that contributions would be considerably larger had ETSA been retained in public ownership.

Table 14 Dividend and income tax equivalent payments

	Dividends		Income Tax Equivalents	
	2009-10	2010-11	2009-10	2010-11
	\$m	\$m	\$m	\$m
PNFC				
Electricity Lease Entities	0.8	-	-	-
Forestry SA	31.1	29.2	13.6	13.9
Land Management Corporation	53.6	49.6	18.3	15.0
Public Trustee	-	1.7	0.5	0.8
SA Lotteries	-	-	8.8	6.4
SA Water	169.0	104.5	77.6	49.7
South Australian Government Employee Residential Properties	1.7	1.7	1.4	1.5
South Australian Housing Trust	-	-	3.3	-
West Beach Trust	-	-	0.4	0.5
PNFC Total	256.2	186.7	124.0	87.8
PFC				
HomeStart Finance	4.7	8.2	5.0	4.4
South Australian Asset Management Corporation	23.5	4.0	-	-
South Australian Government Financing Authority	11.5	53.4	-	8.5
PFC Total	39.7	65.6	5.0	12.9
PNFC and PFC Total	295.9	252.3	129.0	100.7

Source: (Foley, 2010a:5.3) Budget Statement: Budget Paper 3, Table 5.2.

The South Australian Government Financing Authority (SAFA) provides a range of services to public sector that include:

- treasury services (fundraising, client lending, investment, portfolio management, financial and risk advisory services);

- insurance services (insurance cover, catastrophe reinsurance and risk management advice and assistance); and
- other business services (corporate governance, transaction and contract management and administration support services).

SAFA was adversely affected by the economic downturn, making an operating loss before tax of \$45.3 million in 2008-09 due to losses on insurance investments and higher expense provisions (SAFA, 2009). The insurance activities generated an operating loss of \$61.7 million while the treasury activities returned a profit of \$16.4 million. This situation is attributed to cyclical influences and it is expected that SAFA will make a \$53.5 million contribution to the South Australian Government in 2010-11.

6.4 The structural budget balance

This section attempts to quantify the impact of the cyclical downturn on South Australia's fiscal position. The methodology deviates from that discussed in Section 6.2. These estimates calculate the deviation from the trend revenues and expenses in the period prior to the GFC by using data to 2007-08 but the trend figures do not necessarily correspond to the full employment or full capacity output as described in Section 6.2. The trend forecasts used in this section represent what the revenues or expenditures would have been if the trend prior to the GFC had continued. Therefore, these figures are based on fiscal policies in place at that time which may have been expansionary or contractionary at the structural level.

There are three steps involved in removing the cyclical influences from the revenue and expenditure data:

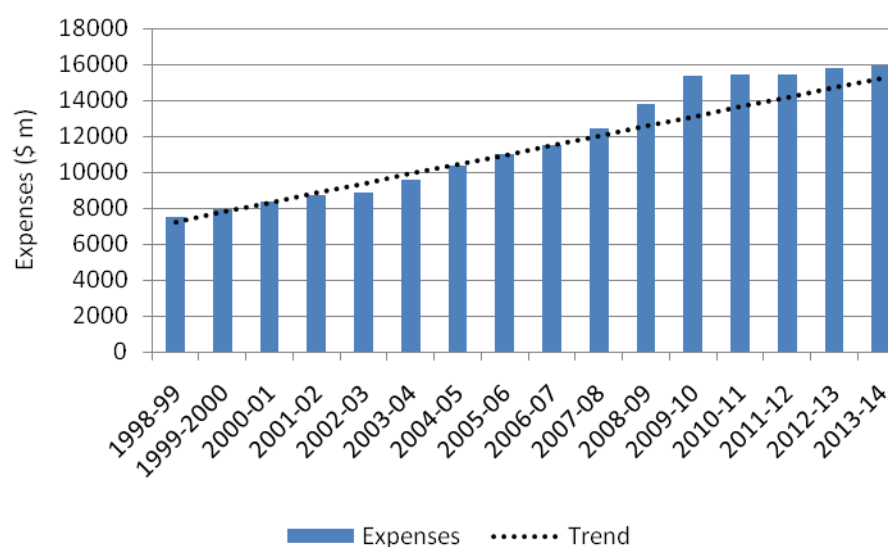
- The first step involves estimating trend data based on the actual revenue and expenditure data up to 2007-08. This is achieved by OLS regressions on the data and then forecasting trend values from 2008-09 onward.
- The trend data is then subtracted from the actual data to reveal the impact of the economic cycle which we refer to as the cyclical gap. Negative values indicate that actual values for revenue or expenditure are below the level that would be expected in the absence of the cyclical downturn. Positive values represent an increase in revenue or expenditure as a result of cyclical influences.
- To eliminate the cyclical effect we then subtract the trend expenses from the trend revenue (estimated in step 1) to reveal the structural balance that approximates what the net operating balance would have been in the absence of cyclical influences.

As discussed in Section 6.2 this is an approximate calculation and should be considered as indicative only.

6.4.1 Expenses

Figure 15 shows actual operating expenses and trends for the period 1998-99 to 2013-14. The cyclical variation in expenses following the GFC is evident as expenditure rises significantly above trend from 2008-09 and returns close to trend in 2013-14 according to the budget forecasts. Table 15 shows the actual and trend figures for each year and the gap between these. A positive/negative gap indicates that actual expenses are above/below the trend level. This indicates that cyclical or temporary influences have increased/decreased the actual figure. The large temporary increase in expenses as a result of the Commonwealth stimulus measures is evident from 2008-09. This indicates that the cyclical change in expenditure will cause the net operating balance to deteriorate (move toward a deficit or increase the deficit).

Figure 15 Operating expenses



Source: (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3.

Note: Figures up to 2008-09 are actual, figures from 2009-10 are budget estimates.

Table 15 Expenses

	Expenses	Trend	Cyclical gap
	\$ m	\$ m	\$ m
1998-99	7505	7244	261
1999-2000	7974	7777	197
2000-01	8406	8310	96
2001-02	8713	8844	-131
2002-03	8898	9377	-479
2003-04	9570	9910	-340
2004-05	10368	10443	-75
2005-06	11040	10977	63
2006-07	11547	11510	37
2007-08	12414	12043	371
2008-09	13764	12577	1187
2009-10	15364	13110	2254
2010-11	15474	13643	1831
2011-12	15472	14177	1295
2012-13	15789	14710	1079
2013-14	15924	15243	681

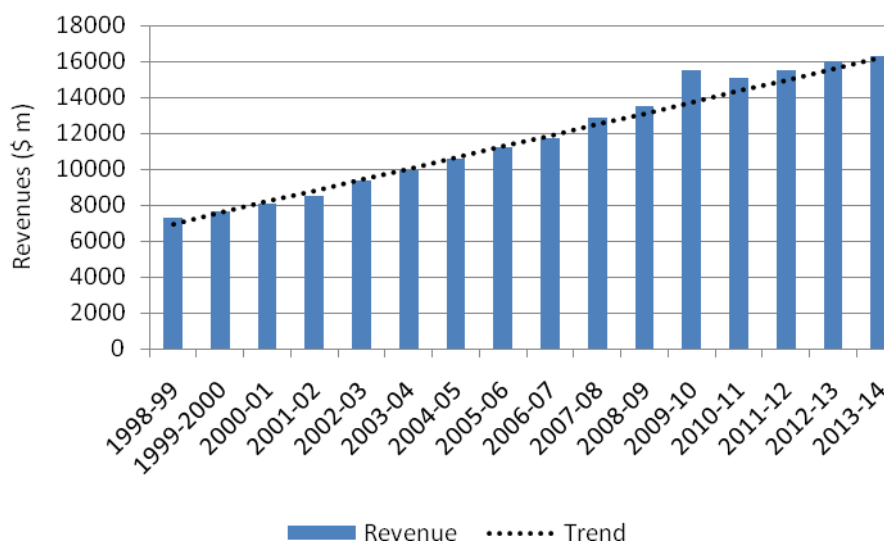
Source: (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3.

Note: Figures up to 2008-09 are actual, figures from 2009-10 are budget estimates.

6.4.2 Revenues

Figure 16 shows operating expenses from 1998-99 to 2013-14. The variation from trend is evident as revenues increase in 2008-09 and peak in 2009-10 before returning to trend by 2013-14. The variation from trend is much smaller for revenues than for expenses due to the countervailing influences on the revenue side. While the decline in economic activity decreases revenues to below the level they would have been in the absence of the downturn, the Commonwealth stimulus increases revenues. The net impact is an improvement in the net operating balance because revenues are higher than would have been expected in the absence of the cyclical variation. This is due to the large size of the stimulus package that outstrips the decline in revenues due to reductions in general revenue from the Commonwealth and State generated revenues.

Figure 16 Operating revenues 1998-99.



Source: (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3.

Note: Figures up to 2008-09 is actual, figures from 2009-10 are budget estimates.

Table 16 provides annual data for both the actual revenue figures and the trend estimates and the gap or deviation. The cyclical gap is calculated by subtracting the trend figure from actual revenue to reveal the extent that actual revenues have been increased (positive) or decreased (negative) as a result of cyclical influences. The large increase in revenues due to Commonwealth expenditure is evident in the rise in the gap in 2009-10 when the major portion of the stimulus revenues were paid by the Commonwealth. Again the positive figures indicate that revenues are above trend in the forward estimates period. In this case, the increase in revenues will improve the net operating surplus.

Table 16 Revenues

	Revenue	Trend	Cyclical Gap
	\$m	\$ m	\$ m
1998-99	7290	6966	324
1999-2000	7644	7581	63
2000-01	8108	8197	-89
2001-02	8538	8812	-274
2002-03	9346	9427	-81
2003-04	9955	10043	-88
2004-05	10592	10658	-66
2005-06	11242	11273	-31
2006-07	11757	11889	-132
2007-08	12879	12504	375
2008-09	13531	13120	411
2009-10	15531	13735	1796
2010-11	15086	14350	736
2011-12	15527	14966	561
2012-13	16005	15581	424
2013-14	16294	16196	98

Source: (Foley, 2010a) 2010-11 Budget Statement: Budget Paper 3.

Note: Figures up to 2008-09 is actual, figures from 2009-10 are budget estimates.

6.4.3 Structural balance

This section uses the actual and estimated data to complete step 3 of the methodology described at the beginning of this section. Table 17 displays data on revenues, expenses and the net operating balance from 2008-09 to 2013-14. Revenue figures are shown in columns 1 to 3. Column 1 contains the actual revenue data, the trend figure is in column 2 and the cyclical gap is in column 3. Corresponding figures for expenses are shown in columns 4 to 6. The cyclical gap is positive in both instances. This indicates that the cyclical impact of revenues will improve the net operating balance while the cyclical increase in expenses will cause the net operating balance to deteriorate.

The actual net operating balance is calculated by subtracting actual expenses from actual revenues and is shown in column 7. It is in deficit in 2008-09 (\$233 million) and is estimated to be in deficit in 2010-11 (\$388 million). The change in net operating balance from surplus in 2009-10 to deficit in 2010-11 is due to expenses increasing while revenues are decreasing. As mentioned previously, the primary reason for this situation is that the major part of Commonwealth stimulus revenues were paid to the States in 2009-10 but much of the expenditure will occur after that period. According to Budget forecasts the net operating balance is expected to return to surplus from 2011-12 (\$55 million) and increase in the latter years of the forward estimated.

Table 17 Structural balance

	Revenues			Expenses			Net Operating Balance	
	Actual	Trend	Gap	Actual	Trend	Gap	Budget	Structural
	\$ m (1)	\$ m (2)	\$ m (3)	\$ m (4)	\$ m (5)	\$ m (6)	\$ m (7)	\$ m (8)
2008-09	13531	13120	411	13764	12577	1187	-233	543
2009-10	15531	13735	1796	15364	13110	2254	167	625
2010-11	15086	14350	736	15474	13643	1831	-388	707
2011-12	15527	14966	561	15472	14177	1295	55	789
2012-13	16005	15581	424	15789	14710	1079	216	871
2013-14	16294	16196	98	15924	15243	681	370	953

The structural balance or structural net operating balance is calculated by subtracting trend expenses from trend revenues. These figures are shown in column 8 and show that, when the cyclical or temporary influences on revenues and expenses are removed there are surplus structural balances in each year.

The increases in the structural balance in each year of the forward estimates clearly demonstrates the contractionary fiscal stance of the South Australian Government and demonstrates that there is considerable capacity to adopt a more flexible approach to fiscal strategy.

7 Concluding remarks

This report has examined the 2010-11 Budget of South Australia. The fiscal strategy is contractionary since the Government has set the target of achieving at least a net operating balance in the general government sector in every year. Budget estimates indicate that this target will not be met in 2010-11 since the Budget forecasts a net operating deficit of \$389 million. This is largely due to the timing differences between the receipt of grants and actual expenditure associated with Commonwealth stimulus measures.

The Budget will deliver new expenditure initiatives to fulfil election promises and will continue implementation of a large investment program. However, it contains ambitious savings targets for 2010-11 that will accelerate in the remainder of the forward estimates period when net operating surpluses are forecast. There are large reductions in public service staffing that will build on and deepen the impact of previously announced savings that are currently being actualised.

The Government has been implementing substantial budget cuts since the deterioration in the budget balance was revealed in the 2008-09 MYBR. Despite the fact that the economic downturn was much milder in Australia than in the remainder of the OECD, and that the economy continues to perform better than forecast, the South Australian Government has persisted with savings targets announced in the 2009-10 Budget and concretised by the Sustainable Budget Commission.

The Auditor-General (2010: 4) warns that the “2010-11 budget projects negative, annual real terms change in expenses over the four years to 2013-14”. The severity of the cuts to expenditure is also evident from our analysis in the previous section. When we removed the cyclical component from both sides of the budget (revenues and expenses) we demonstrated that the structural balance will return increasing net operating surpluses annually. The South

Australian Government is in a position to exercise far greater discretion over expenditure than has been indicated.

The contractionary stance of the South Australian Government has several implications. In the first instance it will have a dampening effect on the economy through the operation of expenditure multipliers. As explained in Section 6.2 the actual budget balance is the outcome of spending decisions by businesses and individuals. Decisions to impose austerity through large cuts to government expenditure or increases in taxation will influence spending decisions in the private sector and can prove counter-productive by causing Gross State Product to contract and thereby reduce State revenues and worsen the budget balance. The alternative strategy of fostering growth by discretionary stimulus spending and/or tax cuts can drive reductions in the budget deficit outcome as the level of economic activity increases and tax revenues recover.

The second difficulty that could be encountered is that the ambitious expenditure cuts may not be met. Previous experience suggests that some savings have proven difficult to achieve. For example, projected savings for Shared Services SA have not been fully realised. Savings in 2009-10 are \$28 million short of the target of \$60 million and targets for the following three years have been revised by a total of more than \$30 million (Auditor-General, 2010).

The Auditor-General (2010:5) cautions that:

The 2010-11 Budget incorporates a very large savings program combining past savings announcements with new measures in this Budget... Experience is that some savings are difficult to achieve and/or to achieve within the desired timeframes.

The large cuts to public sector staffing in the Budget will compound the effect of previous cuts. The Budget proposes additional cuts of 2673 FTE in addition to already announced reductions of 1070 and reductions that have been achieved in recent years. New initiatives will deliver an additional 1981 staff.

In addition to lost economic output and reductions in consumption due to the staff cuts there will be detrimental impacts on service delivery. Past experience suggests that staff cuts will be accompanied by increased workload for the remaining staff who will be working in a resource constrained environment. There are likely to be adverse impacts on morale, loyalty and commitment of staff and a loss of organisational capacity and corporate memory as experienced staff exit the public sector. There is evidence that past staffing reductions have also worsened service delivery and further large reductions will exacerbate this situation.

Our analysis demonstrates the cyclical or temporary nature of the net operating deficits that followed the recent economic downturn. In response to the GFC the South Australian Government decided to make large expenditure cuts and established the Sustainable Budget Commission to recommend where savings could be made through efficiency measures, rationalisation or abolition of programs and functions. In other words the Government chose to respond to what was essentially a cyclical problem through the introduction of structural measures that reduce the role of government and eliminate a large number of jobs in the public sector. This strategy may prove to be counter-productive.

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