

AUSTRALIAN CONFERENCE OF ECONOMISTS  
6-9 JULY 2025, SYDNEY  
ECONOMICS FOR A CHANGING WORLD

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# A louder bark for Australia's fiscal watchdog

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**Our focus is on the case for more robust fiscal rules for Australia .....**

**and more influential role for the Parliamentary Budget Office (PBO).....**

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# Firstly, why are fiscal rules and PBOs needed.....

- To be a countervailing force against biases in fiscal decision-making
- Public choice theory suggests many reasons for these biases (Brandle and Elsener 2024; Yarrad 2019)
- Some are:
  - lobbying to increase spending by small groups is successful
  - if debt financed, the costs are borne by future generations
  - spending ministers see prestige and promotional prospects from increased spending
  - public servants also see prestige and promotional prospects from increased spending

# What do fiscal rules do.....

- Designed to influence future fiscal policy decision-making and involve some combination of targets for:
  - debt/GDP and sometimes a hard \$ ceiling
  - budget balance or deficit target
  - cap for government expenditure/GDP
  - cap for tax/GDP
- Australia has had all of these at various times, including from 2008 a hard \$m debt ceiling – abandoned in 2013
- Literature (Brändle & Elsener 2024) suggests fiscal rules effective – *they lower debt, lower public spending volatility, improve sovereign bond ratings*
- Evidence suggests that expenditure caps especially important - indeed may be “decisive” in effectiveness of budget balance/debt rules (OECD 2015)

# Fiscal rules in practice.....

- All OECD economies have fiscal rules (OECD 2023) and 93 globally (IMF 2022)
- First use of fiscal rules in Australia Hawke/Keating 1985 “trilogy” commitments (no increase in tax/GDP, expenditure/GDP to fall and deficit to fall)
- Charter of Budget Honesty 1998 (Costello) legislated that governments must **specify** fiscal objectives and targets
- Fiscal rules from the 1998-99 budget to the early 2020s generally numerically testable (but not always precise eg “balance the budget over the cycle”)
- Budgets from 2022-23 (October) to 2025-26 have had much looser rules with few numerically testable rules, after some loosening in prior years

## To illustrate .....

1998-99 budget strategy:

- Return the underlying budget to surplus in the life of the Parliament
- Maintain surpluses over the forward estimates period while economic growth prospects remain sound
- Halve the ratio of Commonwealth general government net debt to GDP by the turn of the century
- No new taxes or increase in existing taxes over the term of the Parliament
- Significantly reduce outlays to GDP through to turn of the century

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## To illustrate (continued).....

- 2022-23 (October) to 2025-26 budget strategy include:
  - Allow tax receipts and income support to respond in line with changes in the economy
  - Direct majority of improvements in tax receipts to budget repair
  - Limit growth in spending until gross debt as a share of GDP is on a downwards trajectory, while growth prospects are sound and unemployment is low
  - Ensure the government has the fiscal buffers to withstand economic shocks
  - Focus new spending on investments and reforms that build the capability of our people, expand the productive capacity of our economy etc.....
- Do the 2022 (October) to 2025-26 fiscal rules meet the Charter of Budget Honesty legislation which require?
  - the government "**specify** the key fiscal measures ..... against which fiscal policy will be **set and assessed**" (emphasis added)



# Turning now to PBOs/Fiscal Councils – Independent Fiscal Institutions (IFIs).....

- 29 OECD countries have IFIs with 50 IFIs world-wide (OECD 2021, IMF 2022)
- Literature suggests that IFIs improve compliance with fiscal rules (Lebrun 2017). Further, IFIs with higher media impact reinforce effectiveness of fiscal rules i.e:
  - by “barking loud enough in the face of undesirable behavior, fiscal watchdogs could foster democratic accountability and fiscal soundness” (Debrun & Kinda 2017)
- Australian PBO established in 2012 following a commitment by Malcolm Turnbull in opposition that:
  - “honesty in fiscal policy would be served by the creation of Australia’s version of America’s Congressional Budget Office”

# Current role of Australian PBO.....

- Provide independent and non-partisan analysis of fiscal policy
- This includes (selective):
  - analysing budget sustainability over a 40-year horizon
  - costing of policy proposals
  - self initiated research e.g. “Small Model of Australian Representative Taxpayers (SMART)” and budget useful explainers e.g. on off-budget financing
  - presentations and seminars – most are on how PBO operates rather than policy focused (though these are very good)
- Functions explicitly exclude:
  - preparing economic forecasts;
  - preparing budget estimates
- PBO must therefore use the budget forecasts and estimates for the next 4 years i.e. over the forward estimates period

# Comparison with IFIs in 15 large OECD economies.....

Mandate	Australia	Austria	Belgium	Canada	France	Germany	Ireland	Italy	Korea	Mexico	Netherlands	Spain	Sweden	UK	US
Costing	✓	✓	✓	✓			✓	✓	✓	✓	✓	✓		✓	✓
Analysis of long-term fiscal sustainability	✓	✓	✓	✓			✓	✓	✓		✓	✓	✓	✓	✓
Prepares forecasts/estimates or assesses		✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Monitors fiscal rule compliance		✓	✓		✓	✓	✓	✓				✓	✓	✓	
Press conferences/TV/radio appearances		✓	✓	✓		✓	✓	✓			✓	✓	✓	✓	✓
Provides normative policy recommendations		✓	✓		✓	✓	✓						✓		Options

# **We propose tighter fiscal rules and more influential PBO - but why would a government make these changes and so constrain future policy flexibility....**

- In government to commit to sound policy (Hawke/Keating 1985 “trilogy”)
- From opposition to commit to sound policy in government and to demonstrate capacity as an economic manager (e.g. Costello in 1996 and UK Labour opposition in 2024 after UK bond crisis)
- Committing or re-committing to them in response to a financial crisis to demonstrate resolve to financial markets (UK Conservative govt after it caused the UK bond crisis)



# Firstly, we suggest stronger fiscal rules by amendments to Charter of Budget Honesty....

- Rules must set down specific numerical targets (ratios to GDP for debt, budget balance and expenditure (and/or taxation) and a precise time frame e.g over the next three years
- If rules not being met (e.g. as assessed by PBO as below) explain why and how they will be met
- If escape clause triggered, explain why and when rules will be met

## **Secondly, a more influential PBO which conducts.....**

- Assessment of compliance with fiscal rules – currently, non-compliance is not ‘called out’
- Scenario analysis within the forward estimates period and able to comment on budget forecasts (not fully fledged forecasting capacity)
- Media conferences after major reports (UK OBR is an example)
- Parliamentary committee appearances to discuss fiscal policy issues
- More extensive policy focused research publications

# Current legislation may allow the following initiatives....

- A higher public profile with more active pursuit of media coverage including media conferences
- Appearances before parliamentary committees to discuss major reports
- Under its remit to undertake self-initiated research:
  - more frequently publish and present policy focused research
  - assess compliance with fiscal rules
- Broader change will require amendments to PBOs enabling legislation (*Parliamentary Service Act 1998*)

# PBO to make fiscal policy recommendations.....

- PBO making policy recommendations is perhaps controversial but:
  - many other examples of Australian independent government entities recommending (sometimes deciding) on economic policy –
    - Productivity Commission (tariff cuts a notable change recommended by its predecessors); former Australian Fair Pay Commission (decided minimum wages from 2005 to 2009 avoiding a quasi-judicial approach); RBA (decides monetary policy).
    - Other independent entities have substantial economic impact eg Net Zero Economy Authority and AEMO
- Need some checks and balances – establish a PBO Board with decision-making powers over the work of PBO (not fiscal policy itself). Current PBO Panel of Experts advisory only meets once a year.



# Conclusion....

- We have proposed:
  - more specific numerically testable fiscal rules
  - a more influential PBO which assesses compliance with fiscal rules, adopts a higher public profile and recommends fiscal policy positions
- These changes are designed to be a stronger countervailing force against fiscal policy biases
- A stronger institutional framework cannot prevent fiscal biases, but it can make it harder for government decisions to be influenced by them
- In the end, voters need to be the judge, and it may require an economic crisis to break through fiscal biases and will require political leadership

# Questions?

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