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Labor's debt timebomb

A BANK is very happy to lend you money when you don't need it. It's only when you get into trouble that the bank makes it hard to get a loan. Before 2008 there was no limit on the amount the federal government could borrow. There was no need. The government wasn't borrowing. It was in the business of repaying its debts.

It was the government of Kevin Rudd and Wayne Swan that introduced the debt limit, initially \$75 billion. They explained that they did not want to spend all this money, that it was just to help financial traders who wanted to be able to trade more Commonwealth bonds.

When he moved the legislation in the House of Representatives, the ever-so-serious Chris Bowen (then the assistant treasurer and now the shadow treasurer) assured the public: "The government's commitment to strong fiscal discipline means that there is no need to issue debt securities to finance spending."

Back then no one could imagine the government would actually spend a loan of \$75 billion. Until it did.

So in 2009, Labor increased the debt ceiling to \$200 billion - just to be sure it could borrow enough money to cover all its spending proposals. It spent its way up to that.

So in 2011 it raised the limit to \$250 billion. Last year it was increased further to \$300 billion and pretty soon - possibly in a few days - the government will spend its way up to that limit as well.

So the argument is whether the debt ceiling should go to \$400 billion as Bowen says, or \$500 billion as Hockey says, or to no limit as the Greens say.

Bowen - the man who said there was no need to spend up to the initial ceiling of \$75 billion - has no credibility on this issue. All of the Coalition government's borrowings are going to fund the Budget deficit he left for this financial year, and the next, and for budgets after that.

And the Greens? Well I had hoped that one of the positives to come out of the nightmare of the past three years would be that no one would ever listen to them again - and certainly not listen to them on economic issues.

The debt ceiling has to be increased.

The incoming treasurer deserves to be able to implement his proposals but, as we know, Labor and the Greens are still running the Senate. This means he may not get his optimal position.

Australia cannot afford to default on its borrowings. The last person who tried a stunt like that was the Labor premier of NSW in the 1930s, Jack Lang. We don't hear much about him these days but he thought it was better to default on government bonds and use the money for "stimulus" spending. He split the Australian Labor Party and lost government. Hopefully, Lang cured Australia for all time of the delusion that a government can get away with defaulting on its debts.

So if Australia can't finance the ramp-up in spending except by borrowing to pay for it, the debt ceiling has to go up. We have no choice but to raise it. So it is worth asking whether there is any point in having a limit at all?

Without a limit the government could borrow all that it wanted to spend without having to go to parliament and having the messy business of amending the law. It would take the uncertainty out of the process.

But there is a value in all that messy business. The value is that it focuses the minds of the public and their elected representatives on how the debt is growing and forces them to consider other alternatives - like cutting spending or increasing taxes.

The United States is a case study here. Unlike Australia, in the early 2000s, the US did nothing to reduce its government debt. It blew out. The government hit its debt ceiling. There have been acrimonious and regular debates in recent years about lifting that ceiling.

Although the different sides of politics cannot agree on a Budget they have agreed that the Budget deficit must be reduced and they are doing it. They are cutting spending. The process is working. It is working because the public started to get alarmed about the debt situation and the Congress began to feel heat over the issue.

There is something beneficial in forcing this debate into the public forum. Without that mechanism it would be much easier just to keep on borrowing with no thought for the consequences. That, no doubt, is what the Greens have in mind.

A debt limit would also strengthen the hands of the economic ministers inside the cabinet. Their colleagues will always have new proposals for spending. If there is a limit to the borrowing allowed, this will set a limit on the spending. The threat of a debt limit, and the threat of a messy process to increase it, will give economic ministers a way of pushing back on new spending proposals.

Ultimately the way to stay within a debt limit is to spend no more than you earn.

Another way to describe that situation is to balance the budget. It's going to be a long road back but it's the only lasting solution, and it is the road the country has to take.

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