



# *Worth Noting*

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***Worth Noting is the weekly management journal of research and conferences company L21. It is focused on management strategy issues of relevance to senior executives.***

## **Government Spending Patterns**

The Federal Budget is one of the biggest components of Australian GDP, accounting for almost one quarter of all economic activity in the nation. It has huge capacity to influence the fate of companies, regions, industries and individuals.

It is interesting, then, that so little attention is given to Federal spending in the Australian economy. Even the most basic facts about the budget are not well known – except by a tight-knit (and tiny) sub-culture of economists. Many managers would argue that Federal spending is not particularly relevant to them. In many respects, that argument is right: government doesn't make the factory run or the customers buy.

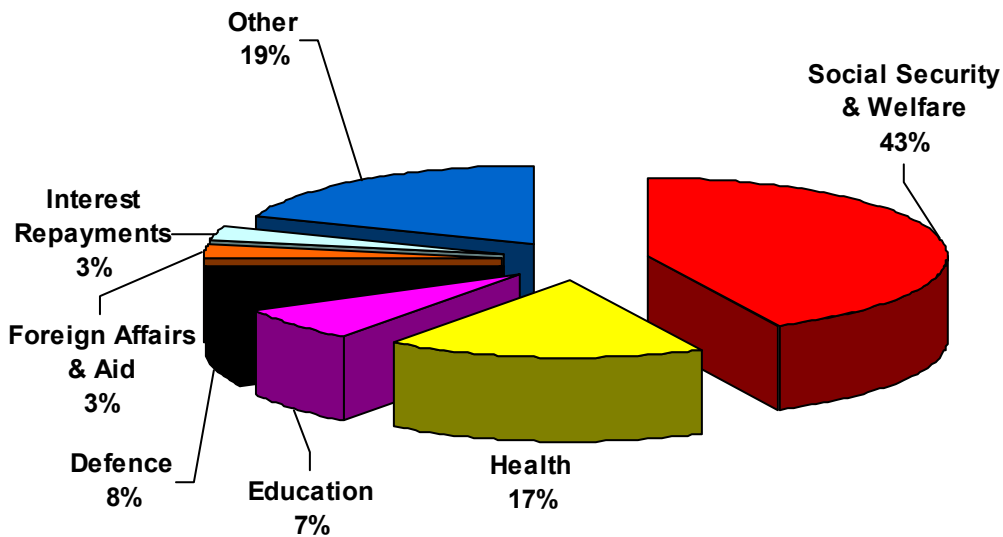
But equally, Federal spending can have a major impact on business. Industry assistance programs can impact on margins and sales. Government procurement can (and often does) form the core of a company's sales operation. And government spending on education clearly has an impact on the nature of the workforce which business inherits from schools and universities.

In analysing Federal Government spending in Australia, the United States, and the UK, we have identified a number of trends which we believe are worth noting. Lobbying government is an important aspect of business for many large and small corporations, and being armed with the facts of what government does with our money can only be of use in this task.

## Social Security is Big – Everywhere

The most striking feature of Federal spending in all three nations is the extent to which Social Security and Welfare payments dominate the mix. The current Australian budget calls for Social Security & Welfare spending totaling 43% of government expenditure.

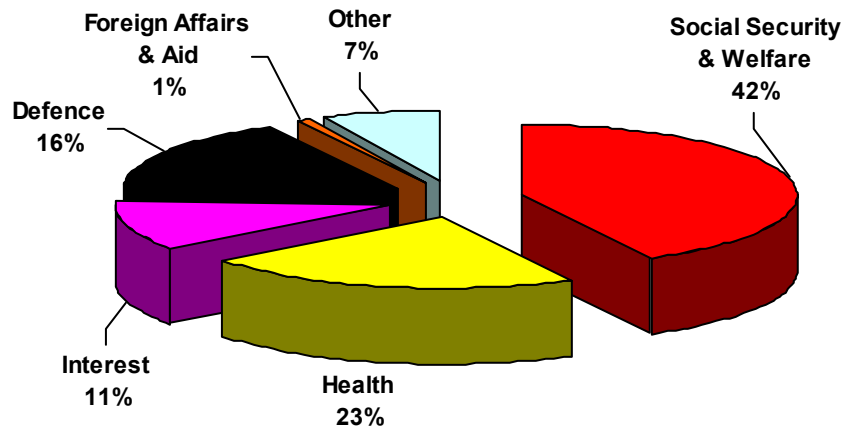
**Australian Federal Budget Spending Breakdown, 2002/3**



Source: Treasury Department

In the United States, Social Security spending is almost exactly the same percentage of Federal spending as in Australia.

### US Federal Budget Spending Breakdown, 2002/3

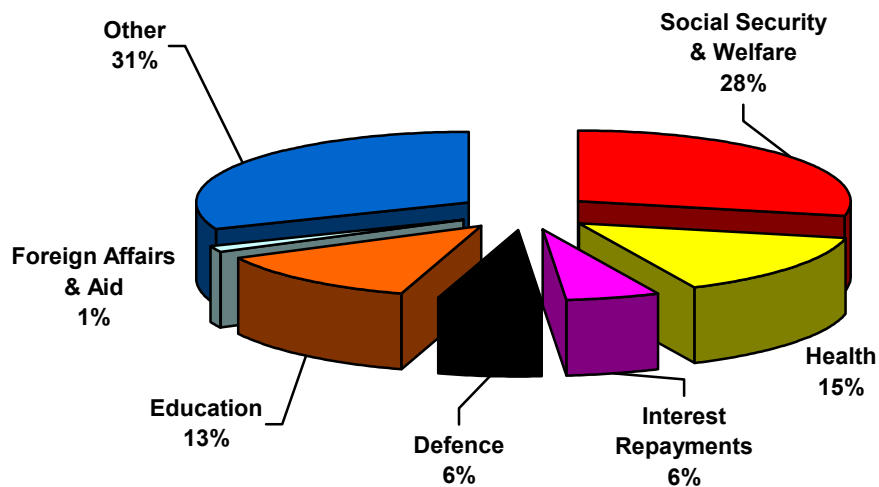


Source: US Treasury

It could be argued that the US Social Security figure is even higher. We have classified the popular Medicaid program as “Health” spending, though in effect it is a social security payment to certain members of the community.

Taking a look at the United Kingdom, we see that Social Security is also easily the largest expenditure. The “Other” category is made up of literally hundreds of different government expenditure items.

### UK Federal Budget Spending Breakdown, 2001/2



Source: HM Treasury

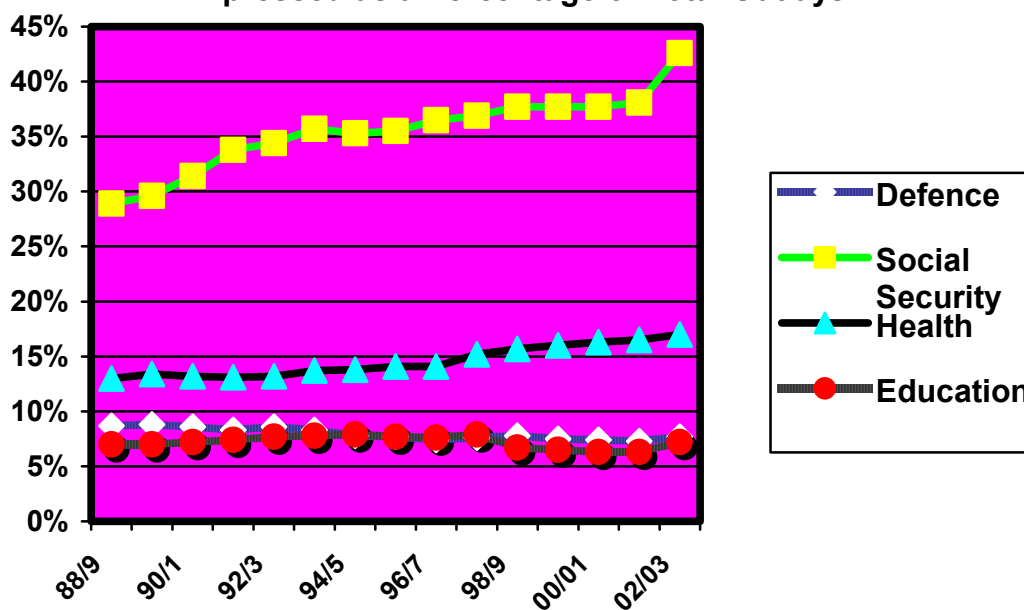
The distribution of government spending in the three countries supports the following conclusions:

- Social Security is by far the largest item of government expenditure
- Health, Defence and Education (in Australia and the UK) are the only other sectors in which governments spend more than 5% of their total budgets
- All other areas of government spending and policy have a relatively minor impact on the budget outcome
- Australia's interest repayments are relatively lower than the other nations, reflecting a lower past reliance on debt financing – particularly when compared to the US

### How did we get here?

Having surveyed the way things *are*, we thought it would be useful to survey the way things *were*. For this exercise we focused on trends in spending in particular areas over times, expressed as a percentage of total government outlays. In Australia and the UK, we focused on the four key spending areas of Social Security, Health, Defence and Education. In the US, where education spending is less relevant to the Federal budget, we assessed the first three areas.

**Australian Federal Budget Spending Over Time,  
Expressed as a Percentage of Total Outlays**



Source: Treasury Department

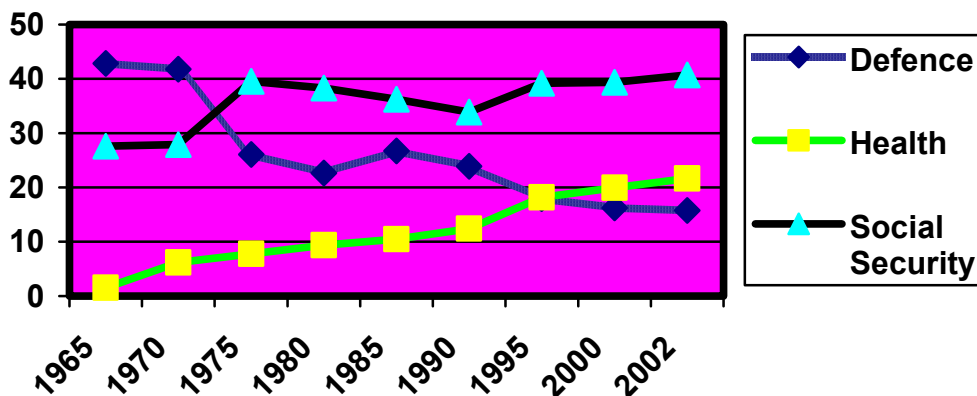
In Australia, Social Security spending has increased rapidly in the past decade. The 2002/3 budget calls for Social Security spending of \$73B of a total outlay of \$171B – 42% of the total, and a record.

Health has seen steady rises in over the past decade, driven by an aging population, increasing complexity of medical care, and higher expectations in the electorate.

The other two large items in the budget – defence and education – have been in slight decline over the past decade. Defence saw a reduction in its relative allocation in the early 90s, while education saw a substantial cut in 1998/9. Both sectors have seen their relative weighting increase moderately in recent years.

In the United States, we took our analysis right back to the 1960s, so as to gauge the changes brought about in that nation by President Lyndon Johnson’s Great Society Program, the end of the Cold War, and other large events. The statistics are quite remarkable.

**US Federal Budget Spending Over Time,  
Expressed as a Percentage of Total Outlays**



Source: US Treasury

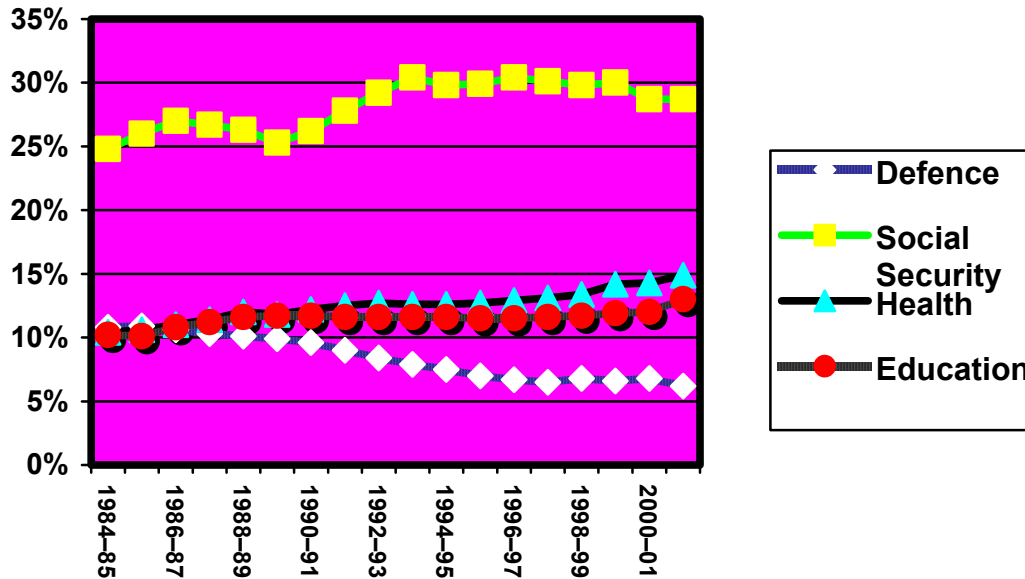
Here, we see Defence spending fall from over 40% of all outlays in the 1960s to 16% today. It is a testament to the power of the US economy that the nation has been able to drop its Defence spending by such substantial levels and yet maintain absolute dominance in the military sphere. Consider this statistic: the US Treasury projects that the Government will spend less money on Defence in 2002 than it did in 1989. The nation has plenty of capacity to increase spending in this area were it considered desirable.

Continuing the comparison with 1989, in that year the US spent \$366B on Social Security Programs, as we have defined them. This year, the US is expected to

spend \$722B – an increase of 96%. As in Australia, Social Security has grown very rapidly.

The UK is most notable because of its relatively modest shifts in spending priorities over recent years. Social Security has also increased its relative importance, but not at the same rate as in the US and Australia.

### UK Federal Budget Spending Over Time, Expressed as a Percentage of Total Outlays



Source: HM Treasury

The UK has maintained Social Security spending at generally less than 30% of total expenditure. In the current year, its spending in this area is projected to be 28% of outlays – 14% less than Australia and 15% less than the United States. Also, the UK has clearly benefited from the “peace dividend” post the end of the Cold War through a sustained and substantial reduction in relative Defence spending.

As with the other nations, we see a sustained increase in Health spending as a percentage of total outlays.

### Summary

Government budgets tend to be perceived as a hazy mystery, full of beauracritic jargon, impenetrable prose, and reams of hard-to-access data. This is true enough, but the facts that lie at the core of government budgets are straightforward. Firstly, only four areas are genuinely material to budget outcomes – with the addition of interest payments, when previous governments have run up a tab. Secondly, Social Security is by far the largest expenditure item and has been consistently increasing as a percentage of outlays in recent

decades. Thirdly, defence expenditures have fallen relative to outlays since the end of the Cold War. Fourthly, health spending continues to rise. Finally, the government's relatively limited activities outside of these key areas emphasise that it does not, and cannot, possess a magic wand to solve all the nation's problems.

All facts which, in our view, are worth noting.