

**Senate Standing Committee on Economics**

**ANSWERS TO QUESTIONS ON NOTICE**

**Treasury Portfolio**

Budget Estimates

29 May – 31 May 2012

**Question: BET 138**

**Topic: Contingency Reserve #2**

**Hansard Page: Thursday 31 May 2012, page 44-45**

**Senator BUSHBY asked:**

Senator BUSHBY: I am once again just a little bit confused. Table 1 on page 2-12 talks about domestic economy forecasts and lists a whole range of outputs and so forth. Footnote E looks to me like it denotes those which contribute to growth, but public final demand does not have an E next to it.

Dr Gruen: That is right.

Senator BUSHBY: I was just curious as to that. Even though we have just said it has 0.25 per cent impact on growth.

Dr Gruen: So, the number in the table for public final demand is the growth rate of public final demand and, when you look at the table, you will see that in 2012-13 the growth rate of public final demand is minus a half. Okay?

Senator BUSHBY: Yes.

Dr Gruen: Then Dr Morling added the further piece of information that its contribution to growth in that year is minus a quarter; at least it rounds to minus a quarter. But you are right, that is not in that table.

Senator BUSHBY: Okay, that makes it clearer. I want to clarify some issues on the contingency reserve, as well. Just to summarise and make sure my understanding of that is correct, Treasury made a late stage reduction in its near-term CPI forecasts stemming from the lower than expected March quarter CPI results. It also made a corresponding late stage reduction to its forecasts for the nominal GDP deflator.

Dr Gruen: Just the GDP deflator; you can leave the 'nominal' off.

Senator BUSHBY: Hence, the GDP growth for the same reason?

Dr Gruen: Nominal GDP growth, yes.

Senator BUSHBY: So, that is where the nominal comes in?

Dr Gruen: Yes, that is where the nominal comes in.

Senator BUSHBY: I have to get my terminology right.

Dr Gruen: So the way you get nominal GDP growth is real GDP times the GDP deflator. That gives you nominal GDP growth.

Senator BUSHBY: So that is right in essence then, with those corrections. The lower CPI forecasts would then have flowed through to reductions in expected spending on various outlays and items, which would have been captured in the contingency reserve, because it would have been too late by then to allocate them out to the portfolios.

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Dr Parkinson: We think that. We would have to check that with them. We are not certain about that detail.

Senator BUSHBY: You did say you would take that bit on notice, but that is possibly what has happened and you will clarify that.

Dr Parkinson: Maybe; I do not know. We would have to check that. You are right, if there is not much time then you do a bottom line adjustment, but if you can you try and flow it through to all of the individual items. Frankly, we would have to get the people who are doing that to give us the right answer.

Senator BUSHBY: And similarly you would have to find out, or can you tell me now, whether the lower nominal GDP forecast will conversely also have flowed through to lower expected tax revenues?

Dr Parkinson: Yes, absolutely.

Dr Gruen: That is true and that is in the forecasts.

Senator BUSHBY: That latter bit then should—would that not mean that it remains a bit mysterious why the contingency reserve for the—that would have actually had an upward impact?

Dr Parkinson: No, because coming back to the nature of the way in which the budget is put together, the revenue forecasts were all done in house and we can actually change them very easily. The outlays measures are done in the department of finance. It is an incredibly complicated process. To feed them and to run everything and to get it out, the consolidated results can take 24 hours, depending on how long it has got to flow through. So, it is much easier for us to flow them through to revenue changes than it is to outlays changes. We know they have been flowed through to revenue; we would have to find out whether they were flowed through to outlays or put into the contingency reserve.

Senator BUSHBY: I would appreciate if you would find that out—

Dr Parkinson: Yes, we are happy to take that on notice.

Senator BUSHBY: because, as I understand, it a negative contingency reserve value is a fairly rare occurrence. The last time was, I think, last century, late nineties, and it certainly was not anything of this size either. I am just curious. Even asking you today, it is not entirely clear why we have ended up with such a large negative figure, and some clarification on that would be good because it does seem a bit of a mystery.

#### **Answer:**

The Contingency Reserve balance is negative in the budget year primarily owing to the inclusion of revised economic parameters received late in the Budget process which reduced overall spending. Given the timing, these adjustments were not able to be allocated to individual agencies or functions. This is consistent with longstanding practice.

A negative Contingency Reserve balance in the budget year has a precedent in the MYEFO publications, but it has not previously occurred in the Budget since at least 2000-01.