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Plan to manage resources wisely

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Fiscal sustainability: What's it all about? Helen Scarborough from Deakin University explores the importance of government budgeting for future generations.

‘In terms of fiscal policy, sustainability focuses on the distribution between generations of the level of government debt, the tax burden and the benefits from government expenditure.’ - Helen Scarborough

MOST of us are used to sustainability being an accepted focus of environmental policy, but how many of us associate sustainability with the Federal Government Budget?

This month's Budget included an emphasis on the importance of fiscal sustainability.

Sustainability is about what we pass on to future generations.

In an environmental sense, it focuses on the management of our environmental resources and passing on to future generations an environment at least as well preserved as that which the current generation inherited.

In terms of fiscal policy, sustainability focuses on the distribution between generations of the level of government debt, the tax burden and the benefits from government expenditure.

In simple terms, intergenerational equity means that future generations should not bear the costs for items which benefit only the current generation.

Likewise, it implies that the current generation should not bear all the costs for items, such as infrastructure, which will have ongoing benefits for future generations.

The Government has recognised the importance of fiscal sustainability.

The Intergenerational Report released in 2002 forecast the development of a significant gap between future revenues and expenditures as the population ages.

In particular, the Government is also concerned about the unfunded public sector superannuation liabilities of the current generation.

On the surface, the argument that passing debt onto future generations is not fair sounds quite reasonable. However, this view requires more detailed analysis.

From an economic perspective, sustainability focuses on the capital stock and the productive capacity we pass on to future generations.

This capital stock includes four types of capital; human capital (an educated workforce), social capital (a democratic, stable system of government), natural capital (the environment) and manufactured or man-made capital (the productive capacity of the economy, for example, buildings and roads).
Definitions of the degree of sustainability vary depending on the assumptions made about the substitutability between types of capital.

For example, do we assume that we will be able to develop alternative energy sources if oil reserves are depleted?

What has this to do with this year's Budget?

The focus of the fiscal sustainability measures of the Government is the establishment of a future fund into which Budget surpluses from the current generation are placed to at least initially fund superannuation liabilities.

It is anticipated these funds will be invested in financial markets. Proceeds from asset sales such as the sale of the remaining government holding of Telstra are also expected to go into the fund.

This could result in the Government selling Telstra, placing the funds in the future fund which then pays administrators to invest in, among other investments, Telstra shares.

However, another way of addressing fiscal sustainability is to focus on the state of the capital stock which the next generation will inherit.

For example, the human capital stock, or quality and productivity of the labour force in the future, is dependent on the investment in educating the current generation.

In 2005-06, only 7.6 per cent of Federal Government expenditure has been allocated to education; about the same as the allocation to defence.

Is this an accurate indication of community priorities?

In terms of man-made capital, both the Business Council of Australia and the Productivity Commission have recently released reports expressing concerns about the state of infrastructure, particularly with respect to electricity, rural and urban water and interstate freight and urban passenger road and rail networks.

Hence, in terms of sustainability and our legacy to future generations, we believe we need to think more broadly than the future fund and investments in financial markets.

Not investing in our capital stock, both in education and infrastructure, results in an antiquated capital stock for future generations.

This limits the productive capacity of future generations to meet the demands of the future and may be just as unfair as leaving them unfunded superannuation liabilities.

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