
Defence Funding in 2013: Means, Ends and Make Believe

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The 2009 Defence White Paper set out an ambitious vision for the modernisation and expansion of the Australian Defence Force. But no sooner had it been released, than funding began to be cut in a headlong rush to bring the Commonwealth budget into surplus. Between 2009 and 2012, around \$20 billion of promised funding was lost. The 2013 White Paper largely reconfirmed the goals of 2009 and restarted growth in defence funding. But the growth is occurring from a lower base, and the difference between the funding promised in 2009 and that announced in 2013 amounts to a deficit of around \$33 billion for the period 2009 to 2022. It follows that, with less money than its predecessor, the 2013 White Paper is underfunded. And while opportunities exist to make Defence more efficient, the scale of possible saving will not be sufficient to balance the books. At some point, either more money will need to be found or capability ambitions reduced. With troops returning to barracks following more than a decade of high operational tempo, the natural tendency will be to cut the size of the Army to free up resources for investment in high-end and maritime capabilities. Recent experience in East Timor and Solomon Islands should temper that impulse.

A mismatch between means and ends is nothing unusual in Australian defence planning. Governments often find it easier to promise money than to deliver it, and the Department of Defence usually finds it easier to spend more than to find efficiencies. Even if such failings never occurred, Defence's plans consistently exceed what can be afforded with anticipated funding.

Usually it takes a year or two following a White Paper for the gap between funding and planned capability to become apparent. There's no such honeymoon likely for the 2013 White Paper. More so than any of its predecessors, it's clear from the start that its plans for the Australian Defence Force (ADF) are unaffordable in the long-term. Put simply, the government's plans for the ADF have remained ambitious while its willing to fund defence has manifestly lessened.

This article examines Australian defence funding in the context of the 2013 White Paper. The first section examines the political, economic and fiscal background to 2013 White Paper. The second explains the funding promised in 2013 White Paper and compares it with current plans for the ADF to see if there are sufficient resources for the task. The third explores the prospects for future defence funding. A final section explores the consequences of the present situation for Australia's defence.

Background

RECENT TRENDS IN DEFENCE FUNDING

After an East Timor inspired funding boost in 1999, Defence funding grew in real terms by an average of 3.7 per cent a year out to 2007.¹ Over the same period, the size of the Defence workforce grew from 50,335 full-time uniformed and 16,292 civilians to 53,167 and 20,391 respectively. At the same time, plans for the ADF grew in ambition and many large acquisition projects were initiated, including air warfare destroyers, amphibious assault vessels, airborne early warning and control aircraft, air-to-air refuelling aircraft and several fleets of helicopters.

By the time the Rudd Government took power in later 2007, it was commonly judged that planned funding would be inadequate to sustain the growing force and make good on remaining plans for its modernisation. The 2009 White Paper set out to resolve the mismatch between funding and plans. The 2009 White Paper carried forward almost all of the plans made by the Howard government and expanded ambitions in the maritime domain, most especially by doubling the planned size of the submarine fleet. In terms of funding, 3 per cent real growth was promised until 2017-18 and 2.2 per cent after that until 2030. In addition, a decade-long Strategic Reform Program was initiated, with the goal of freeing up \$20 billion in savings for investment in military capability.

Less than two weeks after the release of 2009 White Paper, the government reneged on its funding promise and deferred \$8.8 billion of promised funding to beyond 2016. There followed three budgets in which a total of another \$11.2 billion was either deferred or cut outright from defence funding. The \$20 billion of lost and delayed funding was driven by two factors. First, Defence found it difficult to spend its budget in 2011, thereby encouraging the government to claw back some funding. Second and more important, the government systematically reduced defence funding in a failed attempt to return its finances to surplus in 2012-13, following the economic downturn in the global financial crisis.

ECONOMIC AND FISCAL SITUATION

The impact of the financial crisis on Australia was less adverse than experienced by most other developed countries. Although Australia went into debt as the economy slowed and stimulus spending was enacted, net Australian Government debt had only reached 11 per cent of GDP by mid-2013. With debt so low, it is clear that the headlong rush to achieve a surplus in 2012-13 was motivated by politics rather than any underlying economic imperative. The global financial crisis is no excuse; throughout the

¹ The facts and figures mentioned herein come from a variety of sources. Unless otherwise noted, the primary sources are detailed in Mark Thomson, *The Cost of Defence: ASPI Defence Budget Brief 2013-14* (Canberra: Australian Strategic Policy Institute, 2013).

period that Defence funding was reduced, Australia's economic outlook improved relative to the dark prospects envisaged when the 2009 funding commitment was made.

In May 2012 the projected surplus for the forthcoming financial year was a wafer thin \$1.5 billion. By May 2013 the projected outcome had been revised down to a deficit of \$19.4 billion. Several factors contributed to the \$21 billion write down, including weak capital gains and a 17 per cent deterioration in Australia's terms of trade. According to the government's latest estimates, the budget will remain in deficit for another two years until 2015-16.

Paradoxically, the failure to achieve a surplus opened up the possibility of reversing some of the recent cuts to defence funding. In the peculiar world of Australian politics, the accumulation of debit is secondary to the symbolic prize of delivering a surplus. So, with a surplus out of reach for the moment, a boost to defence spending was possible even though it was not considered likely by most commentators.

Defence Funding in the 2013 White Paper

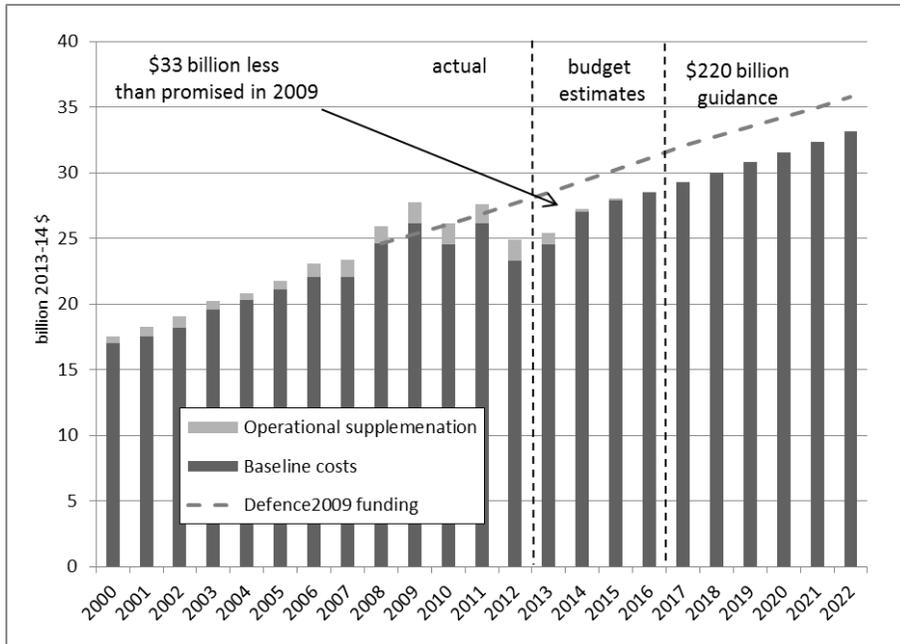
In the 2013 White Paper and the budget that followed eleven days later, the government confounded many observers by providing around \$3 billion of additional funding spread over three years commencing in 2013-14. As a result, defence spending will grow in real terms by 2.3 per cent to reach \$25.4 billion in 2013-14, representing 1.6 per cent of GDP. Over the four years disclosed in the budget, defence spending will grow in real terms by an average of 3.6 per cent each year.

As part of a new approach adopted in 2013 White Paper, the government has provided a single aggregate funding figure for the six years subsequent to the four years of the budget estimates. At \$220 billion, there's enough money to smoothly grow the defence budget in real terms by 2.5 per cent a year out to 2022 (assuming inflation of 2.5 per cent). Figure 1 shows the funding picture for Defence as a result of 2013 White Paper.

Looking at the consistent growth planned in defence spending foreshadowed for the next ten years, it is important to remember that the growth is occurring from a low base created by recent cuts. It will be two more years before defence spending climbs out of the hole dug in search of a surplus. Assuming that Australia experiences economic growth at the rate forecast in the budget over the next four years and as anticipated by Treasury's 2010 Intergenerational Report² thereafter, the defence share of GDP will not exceed 1.7 per cent over the next decade.

² Treasury, *The 2010 Intergenerational Report* (Canberra: Commonwealth of Australia, 2010).

Figure 1: Past and Planned Defence Funding 2000-2022



Note: 2000 = FY2000-01 etc.

Source: Mark Thomson, *The Cost of Defence: ASPI Defence Budget Brief 2013-14* (Canberra: Australian Strategic Policy Institute, 2013).

IS THERE ENOUGH MONEY?

It is difficult to be precise about the difference in funding promised in 2009 and that available today. Taking the commitment of 2009 at face value and using defence funding in 2008-09 exclusive of operations as base year funding, a difference of \$32.9 billion over the period 2009 to 2022 results, equivalent to roughly a 10 per cent shortfall.

Comparisons between the funding outlook in 2009 and 2013 are important because the scale and sophistication of plans for the development of the ADF have not fallen appreciably over the intervening four years. Where some capabilities such as the Offshore Patrol Combatant have been put on the back burner, others have been brought forward, such as the replacement of the Navy's two afloat support ships. In terms of personnel, the target of 59,000 permanent members in the ADF has been retained.

Two particular decisions announced in 2013 White Paper are likely to add to costs in the years ahead. In the maritime domain, the setting aside of off-the-shelf options for the replacement of the Collins class submarines in favour of the two most costly and risks options can only add to future

demands for money. Similarly in the air domain, not only is Australia purchasing twelve additional Super Hornet aircraft equipped with the advanced Growler electronic warfare package, but it is now planned to keep the Super Hornets flying concurrent with the soon-to-be-acquired F-35 Joint Strike Fighter. Doing so will impose the additional cost of maintaining three different combat aircraft fleets in service over the decades ahead—an outcome that had previously been carefully avoided. In addition, the 2013 White Paper outlines a series of major facilities projects arising from the 2012 Force Posture Review.³

With more capability planned but less money available than in 2009, it is clear that the 2013 White Paper is underfunded. Given that the medium-term real rate of growth of defence funding (2.5 per cent) is less than historically needed to keep up-to-date ships, planes and troops in a modern armed force on a unit-cost basis (around 3 per cent),⁴ there is probably not enough planned funding to maintain, let alone expand, the ADF.

WHY UNDERFUND DEFENCE?

Although the failure to achieve a surplus in 2012-13 provided breathing space for additional defence funding this year, boosting defence funding was not politically pain free for the government. The additional \$3 billion provided to Defence in the near-term exceeds the \$2.5 billion savings from the popular baby bonus. With only single one mention of defence in the Treasurer's budget speech, it is clear that there are no votes in defence at this time, economics having long ago replaced national security in the mind of the electorate.

The conclusion therefore must be that the government has restored defence funding because they remain committed to strengthening Australia's defences at some level. Why then have they not provided sufficient funding to deliver all that is planned? The most charitable explanation is that they hedging against deterioration in the strategic environment by providing just enough funds to keep the option of a stronger ADF open. A less charitable view is that they are unable to face the hard decisions necessary to either pare back on current plans or to free-up money through higher taxes or reduced public services.

Irrespective of the explanation, this make believe approach to defence planning has been embraced by both sides of politics. Far from a having robust debate over what sort of ADF Australia needs and how much it should spend, the discussion has been reduced to echoing recitals of 'aspiring' to

³ Department of Defence, *ADF Posture Review Final Report* (Canberra: Commonwealth of Australia, 2012).

⁴ Mark Thomson, *Trends in US defence spending: implications for Australia* (Canberra: Australian Strategic Policy Institute, 2010).

spend 2 per cent of GDP on defence—without any explanation of why this is necessary or when it might be achieved.

Future Prospects

WHAT CAN AUSTRALIA AFFORD?

From an economic perspective, Australia can afford to spend more on defence if it decides to.⁵ Its debt is low, the economy is strong, and the country has broadly favourable demographic prospects compared to other developed economies. If it was judged necessary, Australia could spend far in excess of what even the most hawkish commentators would ask for.

But just because it can, does not mean that it should. A rational approach⁶ would be to spend only as much on defence as could be expected to deliver a net benefit compared with the alternative uses of the money. This is hardly a radical suggestion; it is the criterion that should guide all public expenditure. For example, there is no reason to spend a single cent on defence if greater benefit is available from investment in infrastructure, and vice versa.

Unfortunately, defence is rarely thought of that way in Australia. Instead, defence spending is buffeted by shifting perceptions of risk with little regard to costs and benefits. The more worrying Australia's strategic circumstances become, the more likely it is that money will be found for defence. Conversely, the more worrying economic circumstances become, the less likely it is that money will be found.

FISCAL UNREALITY

There is a rich prize on offer for the political party that returns the government's finances to surplus. In Australian politics, a fiscal surplus is synonymous with sound economic management. Given that the last time a Labor Government presided over a surplus was 1989, it is understandable why the Rudd and Gillard Governments were so eager to do so as quickly as possible—hence the cuts to defence spending from 2009 to 2012.

But the Commonwealth is not in surplus yet. Whoever takes government in September 2013 will have three opportunities to deliver a surplus prior to the next election. Based on the pattern of defence spending following the recessions in the early 1980s and 1990s and the surplus that was not to be in 2013, it is likely that defence spending will again come under pressure to help the Treasurer get over the line.

⁵ Mark Thomson, *Crying poor? The affordability of defence expenditure* (Canberra: Australian Strategic Policy Institute, 2012).

⁶ Mark Thomson, 'Thinking about defence and risk', *The Strategist Blog*, <www.aspistrategist.org.au/thinking-about-defence-and-risk/> [accessed 11 June 2013].

More generally, the next government will face continuing risks to tax revenues in the years ahead coupled with growing demands from areas such as the National Disability Insurance Scheme. The heady days prior to 2008 when revenues consistently delivered windfall gains to the government are unlikely to be repeated. It is now increasingly judged that the resource boom was a once in a generation event that is now receding. Hard decisions are likely across all areas of government expenditure and revenue generation.

WASTE AND REFORM

Reform continues within Defence, even though reporting against the savings targets of the 2009 Strategic Reform Program has ceased. Materiel sustainment is being progressively refined, and ongoing reforms to the delivery of shared services are expected to eventually save around 700 positions. Nevertheless, it will be surprising if Defence is not subject to another round of reforms and efficiencies over the next few years. For one thing, the rapid growth in senior officer and executive numbers (and their military equivalents) since the year 2000 has not been reversed.

But while there is every reason to pursue as lean and efficient a Defence organisation as possible, one needs to be realistic about the scale of savings possible. Removing administrative layers and streamlining processes is more likely to improve effectiveness than boost efficiency—having 1,000 fewer civilians only saves around \$100 million a year or less than 0.5 per cent of the overall budget.

Over the past two decades, Defence has been subject to multiple reform programs, from the Commercial Support Program through to the Defence Reform Program and most recently the Strategic Reform Program. As a result, most of the activities that can be practically transferred to the private sector have already been outsourced. The low-lying fruit has largely been harvested. What remains is likely to be difficult and risky. Consolidation of the defence bases is often cited as an area of potential savings, but it would take decades to recoup the massive investment needed to create megabases by bringing together dispersed units.⁷ And while it would be possible to outsource some of the operational support activities presently done by uniformed ADF personnel, institutional resistance would be strong and the risks of relying on the private sector in wartime would be real.

THE DAY OF RECKONING

There is nothing unique about there being a gap between means and ends in Australian defence planning. The goals of successive Defence White Papers have either been revised downward or delivered much more slowly than planned. One way or another, reality eventually catches up. Following

⁷ Andrew Davies and Mark Thomson, *Who goes where? Positioning the ADF for the Asia-Pacific century* (Canberra: Australian Strategic Policy Institute, 2011).

the 1987 White Paper, it was the 1991 Force Structure Review that adjusted means and ends. Occurring at the end of the Cold War, the result was a cut to the land forces in order to free up money for investment in high-end air and maritime assets. Even then, the replacement of platforms proceeded slowly and on the basis of 'fitted-for-but-not-with' sensors and weapons. In 2003, the Defence Capability Review sorted out the legacy of the 2000 Defence White Paper by cutting existing air and maritime platforms while retaining plans to expand the Army.

The adjustments to the force structure made in 1991 and 2003 were products of their time, reflecting the perceived risks of their era. What then might the reckoning look like for 2013 White Paper if circumstances do not give rise to more funding? If nothing else, there will be the long-standing dilemma of Australian defence: finding a balance between air and maritime capabilities on the one hand, and expeditionary land capabilities on the other. Or, in terms of missions, the balance between defending Australia from attack and conducting ground operations in the near region or in coalition with others further afield.

Now that the Army is returning to barracks after more than a decade offshore in various theatres, the natural tendency will be to sacrifice the land force to allow higher levels of investment in advanced air and maritime platforms. With the replacement of the jet fighter fleet and submarines looming large, this tendency will be reinforced. Be that as it may, instability in East Timor and Solomon Islands over the past 14 years should temper that impulse. At the same time, geopolitical developments in the Asia-Pacific continue to confirm the risks identified by 2009 White Paper—even if the carefully crafted strategic narrative of 2013 White Paper tries hard to convince us otherwise.

Conclusion

Unless defence funding rises more quickly than planned in the medium to longer term, there will not be enough money to deliver the capabilities sought in 2013 White Paper. As in the past, the challenge will be to allocate the available resources to mitigate as much strategic risk as can be. Given the likely continuing concurrent demand for both air/maritime and land capabilities, without a proper funding base Defence is at risk of being unable to fulfil any of the strategic designs placed upon it.

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