
The Funding Illusion: The 2% of GDP Furphy in Australia's Defence Debate

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One of the most effective rhetorical punches thrown by the Coalition during its period in Opposition was the (accurate) claim that Australia's defence spending had slipped to the lowest levels since 1938. In turn the Coalition nominated a target of spending two per cent of Australia's gross domestic product on Defence, should it win the 2013 election. This promise was later echoed by the Labor Government. This article explores how the 1938 comparison emerged, how it morphed into a two per cent of GDP policy target and argues that this debate has been unhelpful for Australia's security. It argues that the Coalition, now in office, should abandon the two per cent target and return to a more orthodox approach to funding defence.

In the lead up to the 2013 Australian Federal election both of the major political parties committed to a significant increase in defence spending. While pre-election bidding wars are not unusual, this one was different. First, a bipartisan consensus was reached over the funding target. Second, this target was not to fund particular capabilities or even a specific dollar figure, but rather to peg the Defence budget at two per cent of Australia's Gross Domestic Product (GDP). Third and finally, the vast majority of portfolios are not funded in this way² and the use of GDP, as an explicit target, goes against a long tradition of defence budgets (at least theoretically) being a negotiation between an assessment of the strategic environment, the capabilities sought to meet those challenges, and the available financial capacity of the nation.³

While the two per cent of GDP policy target has been welcomed by many in Australia's defence community,⁴ there are a significant number of analytic and practical difficulties associated with using a nation's GDP as a way of

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² A policy target using Gross National Income has been applied to Australia's Foreign Aid budget, as part of a global push under the Millennium Development Goals for a global standard. For reporting purposes GDP is also used in some official reports and academic publications as one of many ways to discuss and examine larger portfolios such as Health or Education.

³ For a detail analysis of the budget for the 2013 Defence White Paper see Mark Thompson, 'Defence Funding in 2013: Means, Ends and Make Believe', *Security Challenges*, vol. 9, no. 2 (2013), pp. 51-58.

⁴ See, 'Defence in Depth: Expert views on the Defence Budget', Lowy Institute for International Policy, <<http://www.youtube.com/watch?v=ekLtlf69Szk&feature=youtu.be>> [Accessed 13 November 2013]. See in particular the comments of former Army generals Jim Molan and Peter Cosgrove.

both analysing and enacting defence policy.⁵ This article sets out to explore how the two per cent policy target was adopted in Australia and its implications for the nation's defence policy. It shows how the GDP measure emerged as a way for the Coalition and commentators to draw a historical link between Australia's defence spending in 2012 and 1938,⁶ a comparison that both captured and distorted the public debate. This article will demonstrate how the repeated heavy use of the 1938 comparison legitimised the use of GDP to measure defence and in turn led to the adoption of the two per cent target by both the Coalition and Labor parties.

The funding of a portfolio involving billions of dollars, spent on tens of thousands of individuals, hundreds of major projects and dozens of operations and locations is a necessarily complex effort. It is not surprising, nor automatically harmful, that politicians use simplified measures to communicate their approach to this or any other portfolio. Earlier periods have seen politicians and the military use GDP as one way to assess and guide the defence budget.⁷ For instance the 1997 Strategic Review stated that one of the "most common measures of defence spending is the proportion of GDP spent." However it also noted that while this "is a handy shorthand comparison ... it has no strategic significance in indicating whether a government is spending enough to achieve its strategic objectives."⁸ In the Howard and Rudd years the most persistent financial pledge was in relation to achieving an annual three per cent 'real growth' in

⁵ Notably, the Australian Department of Defence does not publish its funding as a proportion of GDP. For this reason the authors have largely had to rely on the work of the Australian Strategic Policy Institute, cross checked against the work of Joan Beaumont, *The Australian Centenary History of Defence. Vol. 6, Australian Defence: Sources and Statistics* (Melbourne: Oxford University Press, 2001) to identify and verify GDP figures used.

⁶ For example see Peter Hartcher in 'Defence in Depth: Expert Views on the Defence Budget'; Dennis Shanahan, Brendan Nicholson and Cameron Stewart, 'Incoming Defence Chief's Warning on Spending Cuts', *The Australian*, 18 September 2012; Tony Abbott, 'Labor Leaves Australia Vulnerable to Wolves', *The Daily Telegraph*, 26 September 2012; Peter Jennings, 'The Politics of Defence White Papers', *Security Challenges*, vol. 9, no. 2 (2013), pp. 10, 14; James Brown and Rory Medcalf, *Fixing Australia's Incredible Defence Policy*, Lowy Institute Analysis, October 2013, p. 3.

⁷ The 1987 Defence White Paper noted that "the levels of defence capability and the priorities reflected in this Paper, there is a need, over the life of the program, for an allocation of resources generally within the order of 2.6 per cent to 3.0 per cent of GDP" *The Defence of Australia* (Canberra: Australian Government Publishing Service, 1987), p. 112. The 1994 Defence White Paper also stated that 'the Government plans that defence spending will be sustained at approximately 2 per cent of Gross Domestic Product', though this target was not met. *Defending Australia Defence White Paper 1994* (Canberra: Commonwealth of Australia, 1994), p. 146.

⁸ *Australia's Strategic Policy* (Canberra: Commonwealth of Australia, 1997), p. 50. Of the two other major reviews in the 1990s the 1991 *Force Structure Review* only mentions that defence spending could decline as a percentage of GDP if financial resources fall significantly over the decade. *Force Structure Review* (Canberra: Commonwealth of Australia, 1991), p. 6. In relation to the 1993 Strategic Review the only mention of GDP is a reference to the comparative size of Australia's economy in the region and in reference to declining defence spending in New Zealand. See *Strategic Review 1993* (Canberra: Commonwealth of Australia, 1993), pp. 14, 21.

the defence budget.⁹ A focus on GDP to measure defence funding can also be found overseas where the North Atlantic Treaty Organisation (NATO) has had a policy, since 2006, of member nations spending two per cent of their GDP on defence. A problem emerges however, when one type of measurement dominates the debate above all others, and replaces more nuanced thinking about what and where Australia needs to spend its limited resources to ensure its security.

This article argues that what was new during the 2012-2013 period was that GDP as a form of measurement, and specifically two per cent of GDP, became something of a 'magic number', replacing sensible debate about what Australia wants from its defence force. This article argues that the new Abbott Government should quietly abandon the use of GDP to measure defence and return to more traditional model of determining the defence budget; one based on a long term budget certainty¹⁰ built on assessments of the strategic environment and capability requirements needed to protect Australia's strategic interests and achieve its strategic objectives. The ideal time to return to this more orthodox approach to defence funding will be via a new Defence White Paper, which was part of the election platform of the Coalition, and is due for release in 2015.

This article touches on, but does not seek to directly engage the debate over whether increases in Australia's defence spending are needed. Both authors believe defence spending should be driven by a clear assessment of Australia's strategic environment, interests and objectives, and appropriate force structure and capabilities. For Australia's current position, this may well require higher spending on defence. The major concern addressed in this article is the emergence of an arbitrary form of budget analysis and policy development. Understanding what is required to ensure Australian security is a function not of spending, but an assessment of the regional environment and potential threats. It is only when examining the capacity of a nation to spend enough to counter the threats it faces or obtain its objectives does the size and scope of a nation's economy become relevant. While GDP can be useful as one amongst a number of measurements of defence spending, as an indicator of the government's priorities,¹¹ or as a rhetorical tool, when it becomes the sole touchstone for policy development there is great potential for poor policy outcomes. It is sound-bite policy for a sound-bite era; and while it may well have been an effective political

⁹ Only four of NATO's 28 members currently meet this target. *The Secretary-General's Annual Report 2012*, NATO Public Diplomacy Division, 2013, p. 11.

¹⁰ The authors acknowledge that achieving long term budget certainty in the face of short election cycles and an evolving national and global economy is very difficult to accomplish and has rarely, outside of wartime, been achieved.

¹¹ Mark Thomson, 'There's No Perfect Measure for Defence Spending', *The Strategist*, 23 April 2013, <<http://www.aspistrategist.org.au/on-measures-of-defence-spending/>> [Accessed 13 November 2013].

approach to discuss defence funding from opposition, it is a poor approach to making policy in government.

The Rise of GDP Spending for Defence in the Public Debate

Before discussing the merits and flaws of the GDP comparison as a form of analysis and policy ambition, it is important to chart the rise of the GDP comparison in the Australian debate, as well as the adoption of a two per cent of GDP target by both major political parties. Australia's leading expert in relation to assessments of defence funding is the Australian Strategic Policy Institute's senior analyst of Defence Economics Mark Thomson. His analysis of the defence budget and his financial assessments of defence white papers are seen as authoritative and they are widely cited. Therefore it is of note that in an article for the special edition of *Security Challenges* in 2009 assessing the Rudd Government's Defence White Paper, *Force 2030*, Thomson made no mention of defence funding as a percentage share of GDP but rather charted 'real growth' in defence funding and the cost of major capability acquisitions (current and future). He argued that an "analysis of the underlying trend in the cost of delivering military capability shows that real funding growth of around 2.7 per cent per year is needed to maintain a modern defence force."¹²

However by the time of his 2013 *Security Challenges* article on the new Defence White Paper, defence spending as a percentage of GDP had become a feature of the public debate and thus was given additional focus in his analysis. Thomson rightly despairs in his 2013 article that the rise of the GDP measurement meant that

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 spend two per cent of GDP on defence—without any explanation of why this is necessary or when it might be achieved.¹³

The use of GDP to measure and assess Defence's budget can be attributed to a number of factors, but primarily to an eye-catching comparison between Australia's defence budget in 2012 and 1938. This comparison struck a public nerve due to a growing sense that Australia's defence budget was underfunded and conjuring up immediate pre-Second World War vulnerability. The origins of this will now be discussed, including the continued rise of regional powers and a series of forced and voluntary cuts and deferrals to Defence's budget since 2009.

While the years 2009 to 2012-2013 were peaceful in the Asia-Pacific, they saw the intensification of a number of regional disputes and potential

¹² Mark Thomson, 'Defence Funding and Planning: Promises and Secrets', *Security Challenges*, vol. 5, no. 2 (Winter 2009), p. 91.

¹³ Thomson, 'Defence Funding in 2013', pp. 55-6.

flashpoints. Central to these developments was the rise of China. This period witnessed a “new assertiveness” from Beijing,¹⁴ featuring a number of disputes with regional neighbours such as over islands in the South China Sea and East China Sea. In turn, the region responded with a steady growth of regional military spending.¹⁵ New threats such as in the cyber domain also became more apparent in these years. In partial response, the United States announced in 2011 that it would “pivot” or “rebalance” to the region and this has come to be seen as placing more pressure on Australia to increase the size and capacity of its armed forces so as to support its major ally.¹⁶

Alliance politics also played into this debate. During the period of 2012-2013 a number of prominent US commentators weighed into the argument over Australian defence spending. Admiral Samuel Locklear, Commander of US Pacific Command as well as former Deputy Secretary of Defense in the Bush administration, Richard Armitage and Senator John McCain, then ranking member of the US Senate Armed Services Committee, all commented on the decrease in Australian defence spending.¹⁷ Locklear stated that Australia's defence spending had fallen below the level the United States expected of its allies. The *Sydney Morning Herald* noted that he had specifically stated that he had just returned from a meeting of the “North Atlantic Treaty Organisation where the standard for defence spending

¹⁴ David Shambaugh, ‘The year China showed its claws’, *Financial Times*, 16 February 2010, <<http://www.ft.com/cms/s/0/7503a600-1b30-11df-953f-00144feab49a.html#axzz2jdJJ53H6>> [Accessed 13 November 2013].

¹⁵ ‘Asia: Military Modernisation Continues’, chapter 6, *The Military Balance* (London: International Institute for Strategic Studies, Routledge, 2013), pp. 245-352. See also Commonwealth of Australia, *Defence White Paper 2013* (Canberra: Commonwealth of Australia, 2013), pp.14-15, it noted that “Australia's relative strategic weight will be challenged as the major Asian states continue to grow their economies and modernise their military forces.” The Prime Minister Julia Gillard also cited one of the key factors for bringing forward the 2013 White Paper was the “accelerated shift of economic and strategic weight to our region ... and the global financial crisis”. ‘Government Releases 2013 Defence White Paper’, *Defence News*, 13 May 2013, <<http://www.defence.gov.au/defencenews/stories/2013/may/0503.htm>> [Accessed 13 November 2013].

¹⁶ Nick O'Malley, ‘Abbott Criticises Australian Defence Cuts in US’, *The Sydney Morning Herald*, 18 July 2012, <<http://www.smh.com.au/federal-politics/political-news/abbott-criticises-australian-defence-cuts--in-us-20120718-22989.html>> [Accessed 13 November 2013]. The 2013 Defence White Paper calls the US Alliance Australia's “most important defence relationship and ... a pillar of Australia's strategic and security arrangements.” It also notes that it is “unambiguously in Australia's national interest for the United States to be active and engaged in our region as economic, political and military influence shifts towards it.” See paragraphs 6.8 and 6.10.

¹⁷ Daniel Flitton, ‘US Commander Warns Australia on Defence Spending Cuts’, *The Sydney Morning Herald*, 13 July 2012; Alan Stephens, ‘Australia's Defence Budget Is More than Adequate’, *The Canberra Times*, 26 July 2013; see also Greg Sheridan, ‘US Voices Fears Over Defence Cuts’, *The Australian*, 21 July 2012; Greg Sheridan, ‘McCain Slams Labor for “Imprudent” Cuts’, *The Australian*, 27 April 2013; Christopher Joye, ‘Free Ride on US Defence Must Stop’, *Financial Review*, 19 August 2013.

is 2.5 per cent of a country's economy."¹⁸ Armitage called the new defence funding figures, post the 2012-2013 budget, "inadequate" and accused Australia of wanting a "free ride" on the United States.¹⁹

These concerns are also broadly reflective of the United States' desire for burden sharing. The United States has produced a number of reports on *Allied Contributions to the Common Defense* that discuss issues such as the 'Evaluation of Fair Shares'. The 1995 report noted that "there is no single, universally accepted formula for calculating each nation's 'fair share' of the responsibility for cooperative security." The report noted that while GDP "is seen as a key indicator of economic well-being" it is just one of the "different measures and analyses ... [that include] quantitative analysis and subjective judgment."²⁰ However by 2002 the report noted that

National contributions are generally assessed relative to ability to contribute by measuring each nation's share of total allied contributions relative to its corresponding share of total allied Gross Domestic Product (GDP). A nation is considered to be doing its *fair share* in a particular category if its share of total contributions is in balance with its share of total GDP.²¹

There were also a number of domestic factors which suggested the Australian Defence Budget was underfunded. At the release of the 2009 White Paper, the Rudd Government had promised a "new era" of growth for Defence's budget thanks to the funding plans in the *Force 2030* White Paper. The onset of the Global Financial Crisis (GFC) in late 2008 and into 2009-10 meant that there was a growing concern about the fiscal plausibility of Australia's defence portfolio more broadly. The Rudd Government's promises to Defence lasted only ten days before it changed tack and began delaying and deferring the new funding.²² Though Australia avoided a recession, there was a significant hit to the overall strength of the economy

¹⁸ Flitton, 'US Commander Warns Australia on Defence Spending Cuts'. This may well have been a misrepresentation as the standard NATO GPD spending is 2 per cent not 2.5 per cent of GDP.

¹⁹ Joye, 'Free Ride on US Defence Must Stop'.

²⁰ 'An Overview of the 1995 Report on Allied Contributions to the Common Defense', Office of the Secretary of Defense, Washington DC, 1995, <http://www.defense.gov/pubs/allied_contrib95/alliedov.html> [Accessed 13 November 2013].

²¹ 'Report on Allied Contributions to the Common Defense', Office of the Secretary of Defense, Washington DC, 2002, <http://www.defense.gov/pubs/allied_contrib2002/allied2002.pdf> [Accessed 13 November 2013], p. 1. This document reinforced the 2 per cent of GDP measure and noted that in 2002 NATO members on average spent 1.9 per cent GDP. As part of the Coalition's aspiration for two percent of GDP the Shadow Defence Minister Senator Johnston quoted the NATO standard as part of the rationale for the Coalition's funding target at the ASPI defence debate during the 2013 election campaign. See Senator Johnston's comments at ASPI-Hewlett Packard Defence and Security Lunch: 'The ASPI-HP Great Defence Debate', ASPI, 29 August 2013, <<http://www.aspi.org.au/events/aspi-hewlett-packard-defence-and-security-lunch-the-aspi-hp-great-defence-debate>> [Accessed 13 November 2013].

²² Thomson, 'Defence Funding and Planning', p. 93.

and the government's tax revenue base, which, almost certainly, now faces long term structural problems.²³

The Australian political debate also changed between 2009 and 2013. Julia Gillard replaced Kevin Rudd in 2010 and re-committed to achieving a promised return to an overall budget surplus by 2012-13.²⁴ As Defence accounts for around six per cent of government outlays, the Gillard Government saw additional cuts to Defence as a way to achieve its promise in the face of deteriorating revenues. One of the major problems was that the government's cuts, deferrals and delays to Defence's budget came with a pledge not to impact on current operations in the Middle East²⁵ while at the same time not adjusting the existing plans for new capabilities. This left the department with a long shopping list and shrinking purse to pay for it. Lastly, in late 2009 the Liberal party switched leaders to Tony Abbott, who embraced a more politically combative style and approach. It was in this atmosphere of a changing regional environment and cuts and delays at home that the comparison of Australia's Defence budget in 2012-13 with 1938 was first identified and soon captured the public debate.

The Lowest Defence Spending since 1938!

In his budget reply speech of 10 May 2012, Tony Abbott made a single reference to defence spending, noting that

The Treasurer insisted that military spending could be cut—breaking more commitments in the process—without harming our defence capability even though defence spending, as a percentage of GDP, will soon be at the lowest level since 1938.²⁶

This seems the first time public attention had been drawn to the comparison between Australia's intended Defence spending in 2012-13 and its record in 1938. Technically Abbott was not the first to note it, as another Coalition MP (now Assistant Minister for Defence), Stuart Robert mentioned it during a speech in Parliament earlier that day,²⁷ suggesting the Coalition had recognised early on the potency of the line and shared it around. After

²³ 'Statement 5: Revenue', *Budget 2013-14*, Department of Treasury, Canberra, Commonwealth of Australia, <http://www.budget.gov.au/2013-14/content/bp1/html/bp1_bst5-02.htm> [Accessed 13 November 2013].

²⁴ Wayne Swan, 'Budget Speech 2010-11 on the Second Reading of the Appropriation Bill (No.1) 2010-11', Canberra, Commonwealth of Australia, 10 May 2010; 'Gillard Defends Defence Spending Cuts', *The Sydney Morning Herald*, 4 May 2012.

²⁵ Defence receives explicit supplementation for the net additional cost of operations in the Middle East and elsewhere, although because of the blurring of operational preparation activities and routine training, especially in Army, there may well be some shortfall with the drawdown from operations.

²⁶ Tony Abbott, *Appropriation Bill (No. 1) 2012-2013 Second Reading Speech*, 10 May 2012.

²⁷ Stuart Roberts, House of Representatives Ministerial Statements, Afghanistan Speech, 10 May 2012.

Abbott's televised budget reply speech included the 1938 comparison, the line was quickly embraced in the public debate.

In the days after the Opposition Leader's speech, two of Australia's leading commentators Paul Kelly and Greg Sheridan both wrote articles on the Defence budget and prominently highlighted the 1938 comparison. Kelly argued that defence spending based upon proportion of GDP was "the measure that matters".²⁸ Notably both relied on the comments and work of ASPI (Australian Strategic Policy Institute) analyst Mark Thomson to lead their pieces rather than the Opposition leader. Thomson's work may well have been the source for the Coalition's calculations, as he had previously used percentage of GDP to assess the 2011-12 Budget while ASPI's *2011-12 Defence Almanac* lists GDP spending figures going back to 1901 although GDP is not a prominent focus of either publication.²⁹

It was the Coalition who first identified and highlighted the similarity between 2012 and 1938, and in turn led to the embrace of GDP spending as a valid method of assessing the Defence budget. Other journalists and analysts soon followed either reciting the 1938 comparison or using GDP as the way to measure defence's budget such as Peter Hartcher,³⁰ Ross Babbage,³¹ Christopher Pearson,³² Dennis Shanahan,³³ Peter Cosgrove,³⁴ Rodger Shanahan,³⁵ Jim Molan,³⁶ Peter Layton³⁷ and David Uren.³⁸ In contrast some commentators and analysts such as Bruce Haigh,³⁹ Alan Kohler,⁴⁰ Alan Stephens,⁴¹ Andrew Davies⁴² and Mark Thomson⁴³ pushed back against the 1938 comparison and use of GDP to measure defence funding.

²⁸ Paul Kelly, 'Military Spending Slumps to 1930s Level', *The Australian*, 11 May 2012; Greg Sheridan, 'Our Forces Reduced to Impotence', *The Australian*, 12 May 2012.

²⁹ Mark Thomson, *The Cost of Defence: ASPI Defence Budget Brief 2011-2012* (Canberra: Australian Strategic Policy Institute, 2011); Rascal Khosa, *Australian Defence Almanac 2011-12* (Canberra: Australian Strategic Policy Institute, 2011).

³⁰ Peter Hartcher, 'Toothless among Asian Tigers', *The Canberra Times*, 21 July 2012.

³¹ Quoted in Peter Hartcher, 'Defence is Headed for its own Crisis', *The Sydney Morning Herald*, 29 January 2013.

³² Christopher Pearson, 'Coalition has cred on Defence', *The Australian*, 29 September 2012.

³³ Dennis Shanahan, 'Incoming Defence Chief's Warning on Spending Cuts', *The Australian*, 18 September 2012.

³⁴ 'Defence in Depth', Lowy Institute for International Policy.

³⁵ *Ibid.*

³⁶ *Ibid.*

³⁷ Peter Layton, '2% of GDP: It Might Be Logical, but is it Rational?', *The Strategist*, 10 September 2013.

³⁸ David Uren, 'Government Spending to be Slashed', *The Australian*, 26 August 2013.

³⁹ Bruce Haigh, 'Getting by on Less Defence Spending', *The Drum*, 17 May 2012.

⁴⁰ Alan Kohler, 'What's GDP got to do with Defence', *Business Spectator*, 6 May 2013.

⁴¹ Alan Stephens, 'Australia's Defence Budget is more than Adequate', *Canberra Times*, 26 July 2012.

⁴² Andrew Davies, 'Biding their Time: The Opposition's Defence Statement', *The Strategist*, 3 September 2013.

⁴³ Mark Thomson, '2%—can we, should we, will we', *The Strategist*, 10 September 2013. (Although Thomson did use the 1938 comparison in his 2012 Budget Brief.)

The partisan origins of the comparison with 1938 are worth highlighting since it is a comparison which on first reading suggests an atmosphere of inadequacy, incompetence and to some degree indifference to defence policy. This is a particular powerful analogy, linked as it was to a retrospective view of a specific period of Australian history in the lead up to the onset of a global war. The spectre of 1938 allowed the public, policy community and commentariat to conjure up images of the period just prior to the Second World War; a period commonly associated with defence unpreparedness during an era of intense escalating threats. In this respect, it was a rather effective rhetorical tool. However as a point of historical comparison and form of analysis of Australia's contemporary strategic environment and defence spending it is a gross distortion and misrepresentation.

One notable irony of this comparison being used by the Coalition in the lead up to the 2013 election is that in 1938 the country was being run by the conservative United Australia Party Government led by Joseph Lyons. While the level of GDP was indeed similar,⁴⁴ in 1938 Australia's military forces included only 2,795 full time soldiers out a total permanent force, including Air Force and Navy, of just 10,885 personnel. In addition the Royal Australian Air Force (RAAF) had no frontline modern planes in service and the government had only just signed a contract to turn the Wirraway, a training aircraft, into an all-purpose frontline aircraft.⁴⁵ In addition the Defence Act at the time did not allow for a permanent Army field force. This force was, instead, provided by a volunteer part-time militia equivalent to today's Army Reserve. In comparison the present day Australian Defence Force (ADF) consists of three regular Army brigades plus support troops and enablers for a total force of 29,847 regular personnel. Combined with the Royal Australian Navy (RAN) and RAAF the personnel strength of the ADF in 2013 is 58,645.⁴⁶ The figures are even starker when the number of public servants in the defence is considered. In 2013 there were 21,217 Australian Public Service (APS) civilians in the Department of Defence (including 5,670 in the Defence Materiel Organisation).⁴⁷ In his Centenary History of Defence volume on the *Department of Defence* historian Eric Andrews noted that prior to the Second World War "the number of staff in the department [of

⁴⁴ In 2012-13 the Australian Government intended to spend 1.56 per cent of GDP on Defence, which would be the lowest figure since the 1.55 per cent of GDP spent in 1938. Due to changes in spending and the economy, the Australian Government ended up spending 1.60 per cent of GDP on Defence for 2012-13. For 2013-14 the Australian Government intends to spend 1.59 per cent of GDP which is also on track to be the lowest since 1938, but again the final figures may change by end of the financial year.

⁴⁵ Gavin Long, *To Benghazi*, Series 1, volume 1, Australia in the War of 1939-1945 (Canberra: Australian War Memorial, 1952), p. 14.

⁴⁶ Mark Thompson, *The Cost of Defence: ASPI Defence Budget Brief 2012-2013* (Canberra: ASPI, 2012), p. 38. These numbers are based on the 2013 Defence budget allocation.

⁴⁷ *Ibid.*

defence] grew slowly as the effects of the depression eased—from 42 in 1935 ... to 57 in 1938.”⁴⁸ These are hardly comparable figures.

In real terms, as opposed to GDP, Defence’s financial position in 2013 is also a long way from the late 1930s era. 1938 was year one of a new defence rearmament program. In 1937-38 the defence budget was 11.5 million pounds, an increase of three million pounds over the year before. In the 1938-1939 budget 16.7 million pounds was allocated (around \$1.1 billion in 2011-12 dollars⁴⁹). In a public address in 1938 the Federal Treasurer R.G. Casey noted that

I can tell you this, that defence is the only department of the Commonwealth Government that, from the financial point of view, has been able to write its own ticket. Any money defence wants it can get, and I assure you this situation will remain.⁵⁰

The Treasurer’s response in 1938 to defence spending was due to the deteriorating international security situation. While great power tensions in the Asia-Pacific region may well be on the rise in 2013, they are nothing in comparison to 1938. At that time it was becoming increasingly clear that war clouds were gathering. In 1935 Fascist Italy had invaded Abyssinia, in 1936 Nazi German had sent forces to fight in the Spanish civil war and Imperial Japan had invaded China in 1937. In 1938 the Nazis effected an Anschluss (unification) with Austria and then acquired the Sudetenland from Czechoslovakia after negotiating an agreement with Great Britain, France and Italy in Munich in September. This is a vastly different to the strategic circumstances facing Australia in 2013.

There are however three aspects in relation to defence policy, funding and the public debate that are comparable between 1938 and 2013. First, a need for budgetary caution based on an uncertain fiscal outlook is recognisable in both years. In 1938 the government was “conscious of... unemployment... [and] the fears of another economic recession.”⁵¹ Second, in both 1938 and 2013 the government undertook a review of defence and set out new policy directions. Finally, as in 2013, the “Opposition had alleged that the [Government] ... had failed to show leadership in regard to urgent national problems and referred *inter alia* to its handling of defence,”⁵² although in this instance it was a Labor opposition attacking a conservative government.

⁴⁸ Eric Andrews, *The Department of Defence*, Centenary History of Defence (Melbourne: Oxford University Press, 2001), p. 89.

⁴⁹ Raspal Khosa, *Australian Defence Almanac 2011-2012*, p. 88

⁵⁰ Paul Hasluck, *The Government and the People*, Series 4, Volume 1, Australia in the War of 1939-1945 (Canberra: Australian War Memorial, 1952), p. 104.

⁵¹ *Ibid.*, pp. 102, 104.

⁵² *Ibid.* Emphasis in original.

The Emergence of a 2% Goal by Both Parties Prior to the 2013 Election

In the closing month of 2012 through to early 2013, the criticism that Australia was now spending its lowest level on defence as a portion of GDP since 1938 (slowly) morphed from a talking point into a policy 'target' of spending two per cent of Australia's GDP on defence. While Tony Abbott and Coalition MP's used their budget reply speeches in mid-2012 to criticise the defence cuts in the 2012-13 budget⁵³ they were, at that juncture, not willing to commit to reversing them. In the weeks after his Budget reply speech Abbott rejected setting an explicit target for Defence's budget, telling Sky News on 18 July "I don't want to put figures on it ... I would want to get the advice of the defence chiefs as to what the impact of this [changes in spending] will be on our military capability."⁵⁴ Part of Abbott's reluctance may have been because complaints about defence cuts sat awkwardly alongside the Coalition's larger critique that the ALP (Australian Labor Party) Government was spending too much, resulting in increasing deficits and rising debt.⁵⁵

To thread the needle of a pledge to increase defence spending while continuing to attack the government for being fiscally irresponsible, the Opposition used two approaches. First, it regularly highlighted the Howard Government's record as proof of the party's capacity and as a guide to its ambitions. As Abbott told a Returned and Service League conference, "for the Coalition, the bottom line is that our military forces should always be at least as capable as they were when the Howard government left office."⁵⁶ This pledge was also repeated in the 2013 *Stronger Defence Policy* the Coalition launched in the week before the election.⁵⁷ Like the two per cent pledge, using a past government's spending and capacity as a baseline also goes against the grain of the wider literature on how to undertake successful defence planning. The other, and more enduring, approach by the Coalition was to announce their desire to change Defence's budget, when "Australia's economic situation" enabled it. In August 2012, the Shadow Defence Minister David Johnston argued that

⁵³ Roberts, House of Representatives Ministerial Statements, Afghanistan Speech. Defence Budget was cut by \$5.5 billion across the Forward Estimates (to 2015-16). Total Defence funding for 2012-13 was set at \$24.2 billion, down from the estimated actual outcome of \$26.3 billion for 2011-12. See Australian Government, *Portfolio Budget Statements 2012-13: Budget Related Paper no. 1.5A: Defence Portfolio*, Commonwealth of Australia, Canberra, 2012, p. 23

⁵⁴ O'Malley, 'Abbott criticises Australian Defence Cuts in US'.

⁵⁵ Paul Osborne, 'Budget Needs Emergency Rescue: Hockey', *The Sydney Morning Herald*, 16 May 2013.

⁵⁶ Tony Abbott, Address to the 2012 Returned and Services League National Conference, 25 September 2012, <<http://www.liberal.org.au/latest-news/2012/09/25/leader-oppositions-transcript-address-2012-rsl-national-conference>> [Accessed 13 November 2013].

⁵⁷ 'The Coalition's Policy for Stronger Defence', September 2013, <<http://paweb-static.s3.amazonaws.com/13-09-02%20The%20Coalition%27s%20policy%20document%20for%20Stronger%20Defence.pdf>> [Accessed 13 November 2013], p. 4.

we now require an investment by way of an increase in funding of around six per cent for five years to raise the curve just to get back on track to the 2009 plan ... As soon as the Coalition can repair this unholy, unsustainable mess of Defence, we will deliver it and return to three per cent real growth.⁵⁸

The following month the Coalition leader Tony Abbott made a similar pledge that

our aspiration, as the Commonwealth's budgetary position improves, would be to restore the three per cent real growth in defence spending that marked the final seven years of the Howard government.⁵⁹

At this time in late 2012 the focus of the Coalition was simply on restoring the annual rate of increase at three per cent of the defence budget, rather than achieving a specific dollar figure or share of GDP.⁶⁰

The use of an 'aspirational' pledge was a neat way to combine a criticism of specific cuts, within a larger argument that general cuts to spending and reducing taxes were needed. Still, it left critics wondering about both the size and timeline for restoring Defence's budget. By early 2013 the deep nature of the Gillard Government's cuts to Defence had become clearer, and as the criticism of the government increased, in turn the pressure rose on both parties to suggest how they would address it. On 7 February during a doorstep interview, the Opposition Defence Spokesman David Johnston was asked about increasing Defence's budget. He told reporters that

What we have done firstly is to commit to no further cuts ... What I will do is say look at our track record. We aspired to two per cent and delivered it under Howard, we left at 1.9 per cent ... [but] for me to commit to time frames and dollars is ridiculous, and I won't do it ... we believe that two per cent of GDP is the place to be and we want to get there with three per cent real growth.⁶¹

Johnston was careful not to commit the Opposition to a specific target, but he clearly indicated the desired direction. Notably Johnston also compared Australia's defence budget with the even lower 1937 levels and argued that "the proper measure of expenditure in Defence in comparable economies and countries is a measure of GDP."⁶² On 17 February the ALP's Defence Minister Stephen Smith dismissed the 1938 comparison as "overblown", yet suggested similar to Johnston that "I have an aspiration—I would much

⁵⁸ David Johnston, 'Matter of Public Interest—Defence Funding', Parliamentary Speech, Senate, Canberra, 15 August 2012, <[http://www.senatorjohnston.com.au/Speeches/Parliamentary Speeches/tabid/72/articleType/ArticleView/articleId/266/Matter-of-Public-Interest--Defence-funding.aspx](http://www.senatorjohnston.com.au/Speeches/Parliamentary%20Speeches/tabid/72/articleType/ArticleView/articleId/266/Matter-of-Public-Interest--Defence-funding.aspx)> [Accessed 13 November 2013].

⁵⁹ Abbott, Address to the 2012 Returned and Services League National Conference.

⁶⁰ It should be noted that a 3 per cent target is only marginally higher than the 2.7 per cent figure Mark Thompson has identified to merely maintain the defence budget.

⁶¹ David Johnston, 'Doorstop with Senator David Johnston, Defence funding, Coalition commitments, military superannuation', Defence Alert, 7 February 2013, <<http://www.defencealert.com>> [Accessed 13 November 2013].

⁶² *Ibid.*

prefer to be closer to two per cent of GDP than I am at 1.6 but in a tough fiscal environment ... frankly an aspiration doesn't mean much."⁶³ Soon after in a 1 March essay for *Quadrant Magazine*, Major General Jim Molan (retd.)—who later became an advisor to the Opposition—argued that “the magic number that produces usable military capability for Australia in the strategic environment today is about two per cent of GDP”.⁶⁴

In clarifying the Coalition's position, the record of the Howard Government clearly guided their approach. On 18 March 2013, in a speech to the Parliament, David Johnston stated that “The Defence portfolio, which was once running at about 1.98 per cent of GDP under John Howard—towards the end of the Howard government—is down to 1.49 per cent.”⁶⁵ Johnston's claim is one he commonly made yet is somewhat hard to verify.

Under the Howard Government Defence spending as a percentage of GDP had peaked at 1.87 per cent in 1996. It then trended down over the rest of his term, reaching 1.68 per cent in 2007, with an average percentage of GDP for the four terms of office of 1.78 per cent.⁶⁶ This is despite significant increases over the Howard Government's lifetime, with Defence's budget rising from \$9.9 billion in 1996 to \$19.9 billion by 2007 (or from \$15.0 billion to \$22.3 billion in 2011-12 dollars). The reason the GDP figure does not reflect this is because Australia's economy grew even faster than Defence's budget.⁶⁷ A few days after Senator Johnston's speech, on 27 March 2013, the Coalition announced an addition to its policy 'aspiration' for Defence. During a doorstep interview, Tony Abbott stated that

the Coalition wants to go back with the right budgetary conditions to the circumstances that applied in the time of the Howard Government where we

⁶³ Quoted in AAP, 'Smith would rather defence at 2% of GDP', *Australian Associated Press General News*, 12 February 2013.

⁶⁴ Jim Molan, 'Why Our Defence Forces Face Terminal Decline', *Quadrant Online*, 1 March 2013. Molan appeared with Tony Abbott at a pre-election Press Conference on 25 July 2013 and was later appointed a 'special envoy' to assist the incoming Abbott Government deal with the issue of irregular migration, see David Wroe, 'Abbott Advisor handed new paid role as envoy', *The Sydney Morning Herald*, 6 September 2013.

⁶⁵ David Johnston, Speech to Parliament 'Bills: Appropriations Bill (No. 3) 2012-2013, Appropriation Bill (No. 4), 2012-2013, Second Reading, 18 March 2013, <<http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22chamber%2Fhansards%2F4def9134-f2c6-41b0-800e-52463ea41273%2F0032%22>> [Accessed 13 November 2013].

⁶⁶ Raspal Khosa, *Australian Defence Almanac 2011-2012*, pp. 90. The authors contacted Senator Johnston's office to clarify his figures, but had not received a response at the time of publication.

⁶⁷ *Ibid.* A reduction in growth of GDP spent on defence while achieving a real growth in defence spending is not isolated to Australia during this time. For instance, between 2003 and 2011 Singapore defence spending reduced from 5 per cent GDP to 3.7 per cent GDP, while at the same time it moved from \$1,353.6B (USD) to \$1,858.2B (USD) at an average of 2.5 per cent yearly real growth. This was because, over the same period, the average real growth Singaporean GDP was 6.58 per cent.

had three per cent real increases in defence spending with the objective of having defence spending at two per cent of GDP. That is our objective.⁶⁸

This seems the first solid embrace of the two per cent target as policy rather than future ideal. In around ten months, the Coalition had shifted from a historical comparison based upon measuring Australian defence spending as a percentage of the country's GDP to adopting a specific GDP spending target as a policy objective.⁶⁹

The ALP obviously rejected comparing Australia's current position to 1938, yet it soon followed in embracing the concept of using proportion of GDP as a way to guide the Defence budget. As noted above, Stephen Smith had suggested his aspiration for a two per cent target in February 2013. At the release of the 2013 Defence White Paper on 3 May 2013, the Gillard Government announced it would "increase Defence funding towards a long-term target of two per cent of GDP in an economically responsible manner, as and when fiscal circumstances allow".⁷⁰ The Defence Minister Stephen Smith told reporters, somewhat implausibly, that this was "an aspiration that the Government has and an aspiration that previous governments have also had ... So, we have had an aspiration as a country for two per cent of GDP since the year 2000."⁷¹ Yet there had been no mention of a two per cent target under the first Rudd Government, and the 2000 Defence White Paper had only identified a figure around two per cent as roughly in line with the pre-existing spending. It also did so in a way that was much more in line with traditional defence budgeting, i.e. using strategic objectives and national interest to determine the appropriate level of spending

If our economy grows on average as fast over the next decade as it has over the last two decades, then the Government's defence funding projections will mean that in 2010 we will be spending about the same proportion of GDP on defence as we are today. That remains 1.9 per cent. We believe this level of funding is justified within our overall national

⁶⁸ Tony Abbott, Joint Doorstop interview, Williamstown, Melbourne, 27 March 2013, <<http://www.tonyabbott.com.au/LatestNews/ArticleswrittenbyTony/tabid/87/ArticleType/ArticleView/ArticleID/9123/Default.aspx>> [Accessed 13 November 2013].

⁶⁹ During the election campaign Senator Johnston reiterated the 1938 GDP comparison and the Coalitions commitment to 2 per cent of GDP after "ten years". See ASPI-Hewlett Packard Defence and Security Lunch: 'The ASPI-HP Great Defence Debate'.

⁷⁰ Julia Gillard, 'Media Release—Release of the 2013 Defence White Paper', 3 May 2013, Canberra, Commonwealth of Australia, <<http://pmtranscripts.dpmc.gov.au/browse.php?did=19297>> [Accessed 13 November 2013].

⁷¹ Stephen Smith, 'Minister for Defence—Speech at the Launch of the 2013 Defence White Paper', 3 May 2013, <<http://www.minister.defence.gov.au/2013/05/03/minister-for-defence-speech-at-the-launch-of-the-2013-defence-white-paper/>> [Accessed 13 November 2013]. This position was later rejected by Mike Kelly during the election campaign. Kelly had emerged as the Government's spoke person on defence when the current Defence Minister Stephen Smith announced that he was going to retire from politics after the election. Kelly warned against the use of GDP share and instead argued for the commitment of spending over the forward estimates on specific measure and capabilities. See ASPI-Hewlett Packard Defence and Security Lunch: 'The ASPI-HP Great Defence Debate'.

priorities and will ensure that we can achieve the strategic objectives we have identified.⁷²

This is a very different approach to simply setting a two per cent target. Julia Gillard was replaced as Prime Minister on 26 June 2013 and her successor, Kevin Rudd, announced his support for the two per cent target during the election campaign.⁷³ Like Gillard, Rudd did not set a timetable for achieving the target, while the Coalition sought to achieve it “within a decade”.⁷⁴ To see why the 2000 Defence White Paper took a different approach, and why the two per cent target is contradictory to the consensus on Defence budgeting, this article will now demonstrate why the use of GDP is a poor way to measure and shape defence spending and argue that the Abbott Government should abandon the two per cent target.

Why GDP % is a Poor Way to Plan Defence Spending

As the preceding sections highlight the measurement of Australia's defence spending as a percentage of GDP has the advantage of providing sound-bite ready historical comparisons and easily identifiable funding targets. Yet there are also at least five significant arguments against measuring and organising defence budgeting via a nation's gross domestic product. These are;

- First, there is no automatic link between the security of a nation and the percentage of its GDP spent on defence;
- Second, increases in the GDP variable can be negatively associated with security;
- Third, the GDP variable is highly misleading as a form of historical and regional comparison;
- Fourth, very few other portfolios are measured in such a way;
- Fifth and finally, by starting with the funding ambition this approach contradicts proper strategic planning logic.

Together these five arguments strongly suggest that the use of proportion of GDP as a method of analysis and policy development hinders more than it assists. These five arguments will be taken in turn, before discussing the

⁷² Department of Defence, *Defence 2000: Our Future Defence Force* (Canberra: Commonwealth of Australia, 2000), p. 118.

⁷³ AAP, 'PM wants to spend more on Defence, DFAT', *The Australian*, 27 August 2013, <<http://www.theaustralian.com.au/news/latest-news/pm-wants-to-spend-more-on-defence-dfat/story-fn3dxiwe-1226704895788>> [Accessed 13 November 2013].

⁷⁴ 'The Coalition's Policy for Stronger Defence', p. 4.

implications for the incoming Abbott Government and its approach to defence spending.⁷⁵

The first major counter-argument to the use of the GDP comparison is that there is no logical link between a nation's security and its spending on defence as a percentage of GDP. While more spending on security issues probably helps the nation defend itself, it is not automatic or inevitable. Higher spending may be directed towards the wrong threats, such the United States found in 2001 when its vast military was a target rather than protector against non-state actors. Higher defence spending may also come at the cost of the nation's overall economic strength, as the USSR found to its detriment in the 1980s. Despite claims by some, there can never be a 'magic number' of spending which ensures security. What a nation needs to spend on its defence to ensure its security is a function of the threats it faces, and the interests and objectives it seeks in order to develop a sufficiently flexible planning capability and dynamic military posture.⁷⁶ Once that assessment has been made, only then does the nation's capacity to spend and budgeting become relevant. Guiding defence spending according to a specific proportion of GDP provides an illusion of safety by suggesting a quantifiable answer can be provided to an inherently unquantifiable question.

Australia was not at risk in the lead up to the Second World War simply because it was spending less than two per cent of its GDP, it was at risk because it was not spending sufficient to address the plausible threats it faced (in part this was because it was struggling to spend at the level required due to resource and capability development problems as well as working with a fundamentally flawed one dimensional strategy).⁷⁷ What is more, when nations face pressing existential threats they exhibit very different spending patterns to those who do not. For example, while Australia spent 1.06 per cent and 1.55 per cent of GDP in 1937 and 1938, by 1941 it was spending 23.42 per cent of GDP on defence and 34.02 per cent

⁷⁵ The new Defence Minister Senator Johnston reiterated the 2 per cent GDP commitment as recently as his speech to the Kokoda Foundation Annual Dinner 'Addressing Divergent Futures in the Asia-Pacific', Trilateral Dinner with Australia, the United States and Japan, Thursday 31 October 2013.

⁷⁶ Colin S. Gray, 'Strategic Thoughts for Defence Planners', *Survival*, vol. 52, no. 3 (2010), pp. 157-178

⁷⁷ Paul Hasluck, *The Government and the People*, Series 4, Volume I, Australia in the War of 1939-1945 (Canberra: Australian War Memorial, 1952), p. 104. For a discussion of the problems of Australian Strategy in the inter-war period see David Horner, *High Command: Australia's Struggle for an Independent War Strategy 1939-1945* (Sydney: Allen and Unwin, 1982), chapter 1; David Day, 'A Great and Impotent Friend: The Singapore Strategy', in Martin Crotty and David Roberts (eds), *The Great Mistakes of Australian History* (Sydney: UNSW Press, 2006), pp. 125-6; Ian Hamil, *The Strategic Illusion: The Singapore Strategy and the Defence of Australia and New Zealand, 1919-1942* (Singapore: SUP, 1981); and Augustine Meaher IV, *The Road to Singapore: The Myth of the British Betrayal* (Melbourne: Australian Scholarly Publishing, 2010).

in 1942.⁷⁸ The United States and the United Kingdom saw similar substantial changes in their defence spending between their pre-war and wartime budgets. Against such significant changes between peacetime spending and wartime spending on defence, the assumption that pervaded the Australian debate in 2012/13 that 1.5 per cent of GDP puts Australia at risk, while two per cent would ensure some measure of security is unsustainable.

Second, it is sometimes the case that a rising proportion of GDP spent on defence *negatively* correlates with a nation's security. One of the foundational assumptions of defence planning is that countries with strongly growing economies have much greater capacity to respond to security threats than nations with slower growing security threats. As the experience of the Howard Government from 1996-2007 shows, a rapidly growing economy enabled the Australian Government to double its defence spending (from \$9.9 billion to \$19.9 billion), and thus take an increasingly leading role in addressing domestic, regional and even global security concerns. Yet an assessment based on proportion of GDP over this same period would actually suggest Australia was increasingly at risk because the GDP figure trended down from 1.87 per cent to 1.60 per cent. The only time it has significantly moved up toward two per cent (reaching 1.94 per cent in 2008-09) was during the Global Financial Crisis, which saw a slowdown in the Australian economy and shrinking government revenue, but a rise in defence spending through 2009-10. Yet no one would sensibly assume that Australia was more secure during this austere period than in the more prosperous years before.

This is a fundamental problem with this measurement. If a fixed ratio of GDP spending is established then changes to the economy will change the size of the defence budget. So a two per cent target could be reached by keeping spending equal while the economy slows down (as effectively happened in 2008-09). Poor economic performance would ironically make it easier for the Abbott Government to reach its two per cent target than if the economy booms during its time in office. While GDP is used as a measurement to tell us what nations are spending, because it is tied to an external variable (the size of the economy) sometimes it masks declines (or increases) in capacity. Likewise, in the globalised market economy of the twenty-first century we should be increasingly sceptical of those suggesting a link between the size of a nation's economy and the spending capacity of that nation's government.

Third, no specific figure for spending can ever guarantee security, not without reference to the regional environment. Yet using proportion of GDP to assess the defence spending of multiple states is a potentially highly misleading approach. Unless comparing two countries with very similar

⁷⁸ Kohosa, *Australian Defence Almanac 2011-12*, p. 88.

sized economies, the use of the GDP comparison does not provide a very meaningful picture. For example, in Asia today, Japan is constitutionally limited to spending only one per cent of its GDP on defence.⁷⁹ Yet, it has the second largest defence budget in the region (fifth largest in the world), worth 20 per cent of total regional spending. Australia accounts for eight per cent of regional defence spending with its 1.60 per cent of GDP spent, while Singapore has to devote 3.7 per cent of its GDP to purchase just 3.1 per cent of the total regional spend on defence.⁸⁰ All three are developed economies with advanced militaries, and all with concerns about the impact of rising powers and a changing regional environment. Yet no sensible interpretation about the nature of their concerns, the nature of their response, or even their national security can be drawn from these figures alone. Without context these factors suggest an absence of concern (Japan, Australia) or fear (Singapore) when an analysis of their internal debates may suggest otherwise. The use of GDP also “disregards differences in the efficiency of forces”,⁸¹ meaning that it is not possible to suggest similar outcomes from similar spending levels, or the overall effectiveness of similar levels of investment. Thanks to Australia’s advanced bureaucracy and alliance-derived access to world class hardware, it should consistently be able to use its defence dollars in a more efficient manner than Laos or Myanmar. For this reason, those analysts who are currently seeking to understand regional arms spending and especially those testing whether an arms race is occurring tend to recognise the dangers inherent in using the GDP comparison and either ignore it or use it as only one of several types of measurements.⁸²

If GDP is poor at comparing two different states, it is equally poor at comparing two eras within one country. While there may be a similarity in GDP proportion spent in 1938 and 2012, there is no comparable similarity between the capacity, size, or scope of Australia’s defence forces, nor and more fundamentally is there any similarity between the security of Australia in 1938 and 2012-13. When assessing security by reference to GDP spending, the past really is another country. We are no more informed about

⁷⁹ At the time of writing the Japanese Government is still considering moves to change the Japanese Constitution, while also pursuing alternate funding arrangements for its military, see Reuters, ‘Japan Eyes Government Support for Military Aircraft Exports’, *Reuters*, 4 November 2013, <<http://uk.reuters.com/article/2013/11/04/uk-japan-military-exports-idUKBRE9A30Y820131104?feedType=RSS&feedName=topNews>> [Accessed 13 November 2013].

⁸⁰ ‘Asia: Military Modernisation Continues’, chapter 6, *The Military Balance* (London: International Institute for Strategic Studies, Routledge, 2013), pp. 245-352.

⁸¹ Ellen Hallams and Benjamin Schreer, ‘Towards a ‘Post-American’ Alliance? NATO Burden-sharing after Libya’, *International Affairs*, vol. 88, no. 2 (2012), p. 315.

⁸² Geoffrey Till, ‘Asia’s Naval Expansion: An Arms Race in the Making?’, *Adelphi Series*, vol. 52, no. 432-433 (2012), pp. 249-51; Thomson, *The Cost of Defence: ASPI Defence Budget Brief 2012-2013*; Desmond Ball, ‘Asia’s Naval Arms Race: Myth or Reality?’, Paper prepared for the 25th Asia-Pacific Roundtable, Kuala Lumpur, Malaysia, 29 May-1 June 2011, <http://www.isis.org.my/files/25APR/paper_cs_2_desmond_ball.pdf> [Accessed 13 November 2013].

Australia's security in 2013 thanks to the comparison with 1938 than we would be if we remained ignorant of the historical similarity. Indeed, as Thomson rightly notes, we are the worse for it as it distracts us from what matters.⁸³

Fourth, the use of proportion of GDP tends not to be used or prominent in other portfolios. Even when government spending becomes the key debate (such as the tussle over education and the 'Gonski reforms' in the 2013 election⁸⁴), it is far more often that specific dollar terms become the focus of the debate rather than trying to establish a link between the amount invested and the size of the economy. This uniqueness and use of abstract GDP figures may prevent the general public engaging with the Defence funding debate, understanding why this level of spending is needed and how it provides for Australia's security. Without public understanding and support, it will be very difficult for the Abbott Government to achieve its two per cent target⁸⁵ and even more unlikely they can sustain it long term. As Mark Thompson has noted for the Abbott government to achieve the 2 per cent GDP over a decade it would require a 5.3 per cent growth per annum (assuming steady growth).⁸⁶ This is a growth rate that has only been achieved in wartime and never over a ten year period. While the two per cent target is far more central to the Coalition's policy than the use of GDP has been in earlier eras, it is worth noting both the 1987 and 1994 Defence White Papers identified GDP related funding targets which were subsequently not achieved.⁸⁷ Without a clear and compelling rationale for the specific dollars spent, the public will rightly wish for limited government funds to be re-directed to other policy challenges or returned in the form of reduced taxation.

Indeed it is unlikely that advocates of the two per cent target actually believe the two per cent figure is important in-itself. For example, it is highly implausible they would support a future government cutting funding from Defence should the Australian economy stall and thus the proportion spent on defence in reference to the size of the economy rise above two per cent. Rather they see two per cent as a minimum, and latched onto the 1938 comparison use of GDP as a bid to support higher spending. Thus not even those advocates of setting a two per cent target support a firm ratio being established between the size of the economy and size of defence funding.

⁸³ Thomson, 'Defence Funding in 2013', pp. 55-6.

⁸⁴ Justine Ferrari, 'Gonski Reforms Overhaul of Schools to Cost \$6.5bn', *The Australian*, 23 July 2012.

⁸⁵ Paul Dibb and Richard Brabin-Smith, 'Australian Defence: Challenges for the New Government', *Security Challenges*, vol. 9, no. 4 (2013).

⁸⁶ Mark Thompson, '2% – can we, should we, will we?', *The Strategist*, 10 September 2013, <<http://www.aspistrategist.org.au/2-percent-can-we-should-we-will-we/>> [Accessed 8 November 2013].

⁸⁷ *Funding Australia's Defence*, Report of the Joint Standing Committee on Foreign Affairs, Defence and Trade (Canberra: Commonwealth of Australia, 1998), p. 27.

While Defence is an admittedly hard area to quantify outputs for (war or conflicts prevented do not exactly reveal themselves neatly on spreadsheets), it is not impossible to let outcomes and other forms of measurement be the guide. Indeed, if we turn to the fifth and final argument against the proportion of GDP used as a way to measure defence spending, we will see that there is a considered literature which has thought deeply about this problem and come up with a much more sophisticated way to guide defence spending than a simplistic focus on a GDP input.

The fifth and final argument against the GDP comparison is that it goes against the established wisdom of the wider strategic literature. As a wide variety of scholars and practitioners have advocated, best practice for defence spending involves a considered process of assessment, negotiation and policy judgements, between the strategic environment the nation faces, the strategic interests it wishes to protect, the strategic objectives it seeks to achieve, the necessary and desired capabilities for achieving these interests and objectives and the nation's overall budgetary situation.⁸⁸ To allow one of these factors to over-rule all others is to distort the analysis, potentially resulting in poor judgement and policy. Sometimes the accusation is made that governments allow a desire for a smaller defence budget to influence their willingness to acknowledge the true nature of the strategic environment.⁸⁹ This wilful analytic distortion is just as troubling as the less common case when a nation indulges its defence budget and therefore again finds its spending and purchases out of alignment with reality.

Conclusion: Why the Abbott Government Should Abandon the Two Per Cent Target

The authors believe that for the above reasons:

⁸⁸ This strategic planning logic is evident throughout the history of Australian strategic policy. For the period from 1945-1976 see Stephan Frühling, *A History of Australian Strategic Policy since 1945* (Canberra: Department of Defence, 2009). In the period from 1976 see the various Defence White Papers and reviews at <<http://www.defence.gov.au/oscdf/se/publications.htm>>. The following academic studies investigate various elements of this logic in both Australia and overseas: P. H. Liotta and Richmond M. Lloyd, 'From Here to There: The Strategy and Force Planning Framework', *Naval War College Review*, vol. 58, no. 2 (Spring 2005); Terry L. Deibel, *Foreign Affairs Strategy: Logic for American Statecraft* (New York: Cambridge University Press, 2007); James Fallows, *National Defense* (New York: Random House, 1981), chapter 1; Colin S. Gray, 'Strategic Thoughts for Defence Planners', *Survival*, vol. 52, no. 3 (June-July 2010), pp. 159-178; Hugh White, 'The New Defence White Paper: Why We Need It and What It Needs To Do', *Lowy Institute Perspective*, Lowy Institute, Sydney, April 2008; Hugh White, 'Strategic Interests in Australian Defence Policy: Some Historical and Methodological Reflections', *Security Challenges*, vol. 4, no. 2 (Winter 2008), pp. 63-79; Robert Ayson, 'Understanding Australia's Defence Dilemmas', *Security Challenges*, vol. 2, no. 2 (July 2006). Of course these strategic documents are all conceived within an political environment see Peter Jennings, 'The Politics of Defence White Papers', *Security Challenges*, vol. 9, no. 2 (2013), pp. 1-14.

⁸⁹ Neil James, 'Beyond the once-over analysis and partisan waffle', *The Strategist*, 9 May 2013, <<http://www.aspistrategist.org.au/beyond-the-once-over-analysis-and-partisan-waffle/>> [Accessed 13 November 2013].

- that there is no automatic link between the security of a nation and the percentage of GDP spent on defence;
- increases in the GDP variable can be negatively associated with security;
- that the GDP variable is misleading as a form of regional and historical comparison;
- that very few other policy areas are measured via this form of input and;
- by starting with the funding ambition it puts the 'cart before the horse', contradicting strategic planning logic.

This as a result this breeches strategic planning logic—thus, in our view, the use of a GDP target for Australia's defence spending should be abandoned.

Ending the pledge to reach two per cent of GDP for defence funding within ten years government would not be out of place with the broad approach to public policy that the Abbott Government has demonstrated since the 2013 election. It has moved cautiously in regards to major policy reform. As such, a return to the traditional formula for determining the size of the defence budget would be in line with this strategy. This also fits the Abbott Government's 'messaging' on policy reform as it attempts to avoid a sense of policy 'on the run' and takes a more considered, and an 'adult' approach to policy formulation. Indeed Abbott recognised this in mid-2012 when, though using the 1938 comparison as a talking point and critique, he rejected using GDP as a policy guide, preferring to seek "the advice of the defence chiefs as to what the impact of this [change to spending] will be on our military capability" when setting the Defence Budget.⁹⁰

In addition, abandoning the two per cent pledge is likely to be viewed positively both at home and in the region. Furthermore with some clear and unambiguous discussion about future spending the government would be able to present a robust justification to the United States, its major alliance partner. Without the furore of an election, an Abbott Government could persuade the Australian public that a long term thoughtful approach to funding defence, based on credible assessments of Australia's environment, provides more plausible strategic guidance to the portfolio. While some in the Defence community who championed the two per cent pledge may be disappointed, if reassured that ending the pledge does not mean a reduced desire to support the Defence Force and the government outlines a long term and sustainable approach to funding, they should logically be supportive. Likewise many in the Asia-Pacific will appreciate a more

⁹⁰ O'Malley, 'Abbott criticises Australian Defence Cuts in US'.

considered approach from Australia rather than what could look superficially like an arbitrary defence build-up. As was seen with the release of the 2009 White Paper, promises of significant new spending without a clear rational and carefully justified case can cause diplomatic headaches for Australia and tension in the region.⁹¹

Australia's security in the coming century will depend on a range of factors, of which the amount it spends on its defence force is just one small part. To ensure that spending is at the right level, on the right equipment and enjoys sustainable public support, defence spending needs to be re-oriented away from sound-bite-policy ideas like using a proportion of GDP. Instead the government should return to providing the Department of Defence with budget certainty based on sound strategic assessments. The 2015 Defence White Paper provides an ideal opportunity for the Abbott Government to quietly drop the policy of spending two per cent of Australia's GDP on defence and establish a more coherent approach. This may well require higher defence spending, but such assessments cannot and should not be made simply based on what proportion of GDP is spent.

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⁹¹ Czeslaw Tubilewicz, 'The 2009 Defence White Paper and the Rudd Government's Response to China's Rise', *Australian Journal of Political Science*, vol. 45, no. 1 (2010), pp. 149-57.