Briefing Paper

Government Debt and New South Wales: Past Development and Present Realities

by

John Wilkinson

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1 THE DEVELOPMENT OF GOVERNMENT BORROWING: FROM THE RECENT PAST TO THE PRESENT DAY

(a) The Development of International Government Borrowing

Lending by bankers, and others, to governments has a long past. In the history of Western Europe the rise of banks accompanied the early development of commerce in Genoa, Florence and later in Venice. Fernand Braudel has noted that it was "in Genoa that the first gold coins were minted in the early thirteenth century, with Florence following suit in 1250. . .Cheques and holding companies were invented ... in Florence. Double-entry book-keeping too was first introduced in Florence... The useful simplification of the procedure for maritime insurance, eliminating the need for a notary, was devised. . .in Florence."[1]

One of the earliest examples of lending by these newly emerging banks in Europe was that of the loans provided by the Frescobaldi banking house to Edward I and Edward II of England. According to the *Encyclopedia Britannica*'s account of the Fescobaldi,

> Important in Florentine public affairs from the 12th century, the Frescobaldi belonged to the wealthy 'magnate' class. . .Opening a branch in England in the 1270s, in two decades the Frescobaldi firm rose to the position of royal bankers, formerly occupied by the Riccardi family of Lucca, which had been driven into bankruptcy by loans for Edward I's wars in Wales and France. Between 1302 and 1310, the Frescobaldi loaned £150,000 to Edward I and Edward II. In return they were given virtual control of the revenues of England, including the mint and the customs, and were granted lands, honours and privileges. In 1310 Edward II's barons, jealous of the Italians' power, drew up ordinances forbidding the assignment of customs to foreigners and calling for the arrest of foreign merchants and seizure of their goods. Before the ordinances could be implemented, the Frescobaldi fled to the Continent, taking refuge at Avignon and then at Florence.[2]

Accompanying the obligations incurred in procuring the loans from the Frescobaldi was the development of the means to pay them back. B.E.V. Sabine, in his history of taxation in Britain, has written that, of the English monarchs of the 1200s, Edward I's reign was the most significant in relation to fiscal matters,

> for in those thirty-five years were laid the foundations of direct taxation in the shape of the fractions of moveables and of indirect taxation in the shape

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[1] Fernand Braudel, *Civilisation and Capitalism 15th-18th Century*, Vol.III, *The Perspective of the World*, translated by Sian Reynolds (Harper and Row, New York, 1984), p.128.

[2] *Encyclopedia Britannica*, fifteenth edition, vol.5 (Encyclopedia Britannica Incorporated, Chicago, 1992), p.2.

of Customs and Exise. It also saw the virtual replacement of feudal levies as a major feature of the fiscal scene, and the vital element of parliamentary consent slotting into their place. The extent of progress, however, should not be over-emphasised. Although he made considerable reforms, it is clear that Edward I was perpetually in debt, especially to his Italian bankers.[3]

From these beginnings in the 1200s and 1300s lending to governments grew. During the 1400s, Florentine banks continued to lend to European monarchs and Professor Laurits Birck, in his study of the public debt in Europe, has written that during that century "when in difficulties France, England, the German princes and even the Scandinavian kings turned to Florence."[4] Gradually, however, the centre of lending in Europe shifted northwards (as did the centres of commerce) to Lyons and Antwerp. Birck recorded how "From 1450 to 1550 Lyons was the most important exchange in Europe. . .Towards 1500 there were 87 banking houses in the town without counting the merchants and manufacturers who. . .were credit purveyors to the State. . From 1450 to 1550 Antwerp became the world-centre which rivalled Lyons in power, and where all the commercial houses of Europe had counting-houses and branches; here were financial representatives of the foreign kings".[5] During the 1500s, Charles V of Spain, as regent of the Netherlands, in Birck's description, "contracted large loans at 10, 20 and even 30 per cent. . .Add to this that France and England were frequent borrowers and that the House of Tudor tried to centralise its foreign debt in Antwerp."[6] Like the houses of Florence before them, some of the banking houses of Antwerp even gained control of state revenues and Birck has described how the house of Fugger, the largest in Antwerp, had amongst its debtors "the Archduke Sigismond, who in various sums borrowed up to a total of some 200,000 guilders. . .and gave as security the Austrian mines; both in Austria and in Hungary Fugger farmed the mines and the royal dues, the returns from these serving to cover the interest and amortisation of the loans made to the princes."[7] In the late 1500s and early 1600s, with the expansion of commerce in the Dutch provinces (and the capture of Antwerp by Spain in 1585), the centre of

3 B.E.V. Sabine, *A Short History of Taxation* (Butterworths, London, 1980), p.37. The tax on moveables, according to Sabine, was a "tax on property which, unlike lands and houses, could be moved from place to place, and included large and small beasts, grain and other crops, carts and farm furnishings in rural districts, and personal and household property as well as cooking and eating utensils, jewels and cash in urban districts." See ibid., p.35.

4 L.V. Birck, *The Scourge of Europe: The Public Debt Described, Explained and Historically Depicted* (George Routledge and Sons, London, 1926), p.167.

5 ibid., pp.169-172.

6 ibid., pp.172-173. According to Birck, writing in 1926, "When in 1552 her crown agent in the town was Thomas Gresham, England owed £123,000 in Antwerp, and in the course of the following four years he procured for his prince loans from the town to the total amount of 2 million pounds sterling". see ibid.

7 ibid., p.176.

European lending moved to Amsterdam which remained prominent during the 1600s and the 1700s.[8] In the 1600s, for example, Dutch bankers lent large sums of money to the Danish monarchy which, by the mid-1700s, owed 12 million florins to Dutch concerns. In the late 1700s, Catherine II of Russian sent her crown jewels as collateral for loans raised in Amsterdam and the newly emergent USA negotiated one of its earliest loans, for 2 million florins, amongst the Amsterdam financial community.[9] Dutch pre-eminence, however, was in turn challenged by England which during the 1600s waged three wars against the Dutch to eventually wrest European commercial supremacy from the Netherlands, changing the locus of financial transactions in Europe to London.[10] By the 1800s, following the end of the Napoleonic Wars, London became the centre of international lending: in the 1820s, for example, 26 foreign governments (including those of Prussia, Greece, Spain and Peru) had loans on issue in London aggregating more than £52 million in total.[11]

As international lending changed in locus from Florence, to Antwerp, to Amsterdam and then to London, procedures for loans and international transactions evolved towards the system of international finance which exists today. According to Fernand Braudel, the procedure for placing a loan in the market, as established in Amsterdam during the 1600s and 1700s, was as follows:

> the firm which had agreed to put the loan on the market, in the form of stocks which would afterwards be quoted on the Bourse, would open a subscription list, in theory to the public (In practice, if the loan had good guarantees, the subscriptions would have almost all been taken up before the public announcement). Interest rates were low. . .5% was considered a high rate of interest. . .As a rule, the private firm which had issued the loan would itself deliver the capital to the borrower and undertake to distribute the interest it received - all in return for a commission. The firm would then sub-contract with the professional brokers who would, each in his different circle, place a number of bonds. . .Finally, the bonds would be introduced on the Bourse.[12]

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8 The Amsterdam stock exchange (or Bourse), and the Amsterdam Chamber of Insurance, were opened in the 1590s and the Bank of Amsterdam was opened in 1609. See Braudel, op.cit., pp.184,208.

9 Braudel, op.cit., p.247.

10 ibid., pp.260,379.

11 Ellis Powell, *The Evolution of the Money Market (1385-1915): An Historical and Analytical Study of the Rise and Development of Finance as a Centralised, Co-ordinated Force* (The Financial Times, London, 1915), pp.326-327.

12 Braudel, op.cit., p.247. Braudel has recorded that in the 1780s Dutch financiers had a total of 335 million florins on loan to foreign governments. The principal borrowers were England (280 million florins), France (25 million florins) and the remainder (30 million florins) was on loan to a variety of other governments. See

Laurits Birck, describing in 1926 the development of international transactions in such bonds, wrote that it was in the 1700s that the printed bond entered,

> into general use. . .The bearer bond originated in Holland as a bond with the name in blank. . .the bond being drafted in a definite name but the interest coupon being made out to bearer. The loans once having been negotiated, the Banking House generally offered the bonds for subscription at the State's risk. The House administered the loans it negotiated, receiving in one lot the amounts due as interest and amortisation, and distributing the sum among the subscribers to the loan. . .almost everywhere. . .there existed a regular quotation. . .for State bonds. . .an international bond market came into being; in 1763, forty-four listed securities were negotiated on the Amsterdam Exchange; forty years later there were 110.[13]

During the nineteenth century Britain continued to be the major lending country in the world, with France the second most important.[14] Germany, also, towards the end of the nineteenth century, began to accumulate substantial capital for internal and overseas public investment.[15] According to Birck, "Until 1914 London was the centre of the capital power of the world; it was there Europe went for loans, as well as the United States, the Colonies, Africa, South America and Asia".[16] British investors, for example, became the biggest subscribers to the bond issues of the newly established states of the USA.[17] Merchant banks were established in Britain

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Braudel, op.cit., p.267.

[13] Birck, op.cit., p.199.

[14] During the earlier part of the nineteenth century French investors purchased large numbers of Belgium Government bonds and by the mid-1800s substantial amounts of French funds were also flowing to Spain and Italy. By the end of the nineteenth century, the focus of French lending had shifted to Russia with an estimated 18 billion francs worth of Russian Government bonds being purchased by French investors up to the beginning of the Great War. See Charles Kindleberger, *A Financial History of Western Europe* (George Allan and Unwin, London, 1984), pp.226-228.

[15] Gustav Cohn wrote in 1889 that of "The number of securities of which daily quotations are permitted on the Berlin stock exchange. . .by the far the greater portion is made of public loans: 55 German Imperial, State, and Municipal Loans. . .9,294 million marks; 108 Foreign State and Municipal Loans. . .28,359 million marks. . .Total. . .37,653 million marks." See Gustav, *The Science of Finance*, translated by Thorsten Veblen (University of Chicago Press, Chicago, 1895), p.758.

[16] Birck, op.cit., p.218.

[17] C.K. Hobson, *The Export of Capital* (Constable and Company, London, 1914), pp.96,110,132-134. Hobson writes that "in the year 1865", for example, "an Italian loan for £8,000,000 was issued simultaneously in London, Paris, and Lyons; a Peruvian loan for £10,000,000 was issued in London and Paris; a

which have remained associated with the business of foreign lending. N.M. Rothschild was formed in London in 1804 and S.G. Warburg was founded in 1864.[18]

However war once more changed the centre of international lending: the Great European War of 1914-1918 having severe financial effects on Britain, while production in the USA leapt forward as American companies expanded on the basis of war contracts for Britain and France. As Gerd Hardach has observed, after the Great War "and largely as its direct consequence, New York replaced London as the financial capital of the world."[19] According to Kees van der Pijl, "of the thirteen most prominent investment banks operating in the late 1920s" in the USA "eight had been started during World War One". A demonstration of the shift of international lending to New York is illustrated, as van der Pijl adds, by the fact that "Between 1924 and 1930, $1.239 billion of German bonds were sold to American investors".[20] Again banking houses came to prominence, in the USA, which remain in the forefront of foreign lending today. While well-established in the USA before 1914, the banking house of J.P. Morgan became prominent during the Great War by becoming a financial intermediary for British and French purchases of munitions in the USA. During the 1920s, J.P. Morgan became the most important American financial concern in the organising of loans for European governments.[21]

During the latter part of the twentieth century a new centre of lending emerged to world to closely rival New York: Tokyo. Until the mid-1960s Japan was a net borrowing country but from the 1970s accumulation of capital, particularly by banks and life insurance companies, grew rapidly. According to a presentation by the vice president of the Meji Mutual Life Company at a seminar in Sydney in 1984 there were, by that time, "23 private companies in the life insurance industry. At the end of the 1983 fiscal year, their life insurance in force reached 752 trillion yen or

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Brazilian loan for £5,000,000 was issued in London and Amsterdam; a Buenos Aires loan for £2,500,00 was issued in London and Amsterdam; a Russian loan for £6,000,000 was negotiated in London and Amsterdam; a Spanish loan for $50,000,000 was offered in London, Paris, Madrid, Hamburg, Frankfurt, Brussels, Antwerp and Vienna". See ibid., p.138.

18 Robin Pringle, *A Guide to Banking in Britain* (Charles Knight and Company, London, 1973), p.71.

19 Gerd Hardach, *The First World War, 1914-1918* (Penguin Books, London, 1987), p.98.

20 Kees van der Pijl, *The Making of an Atlantic Ruling Class* (Verso Books, London, 1984), pp.63-66. During the 1920s loans were raised in New York by the governments of Belgium, Poland, Colombia, Bolivia, Peru and Chile amongst other foreign borrowers. See Sidney Homer, *A History of Interest Rates* (Rutgers University Press, New Brunswick, New Jersey, 1963), p.389.

21 Victor Perlo, *The Empire of High Finance* (International Publishers, New York, 1957), p.141.

roughly 3 trillion 370 billion US$, that is the second largest scale in the world behind the United States." A significant part of Japanese banking and insurance funds are invested in government bonds.[22]

By the early 1990s, according to Carolyn Cummins writing in *The Australian*, the world's bond markets are collectively valued at close to US$10.5 trillion (a sum which, presumably, includes both all lending by domestic financial concerns to their own respective national governments and to foreign governments and other bodies).[23]

Electronic means of transfer have also changed the nature of trading in bonds and, instead of transactions being made in the form of printed bearer bonds, bond transactions are now electronically registered by computer.[24]

(b) The Development of Domestic Government Borrowing

As can be seen from the above, monarchs and governments appear to have traditionally preferred to borrow overseas rather than at home: as in the case of Edward I of England cited above. Nevertheless, borrowing domestically also has a long past. Gustav Cohn, in his study of finance, recalled how, in the case of England, Richard II, in the late 1300s, had succeeded in having a law passed "which recognised the right of the crown to levy forced loans". Subsequently, as Cohn described,

> Henry V succeeded in obtaining from Parliament (1416) a subsidy of £60,000 to cover pressing necessities in the war in France. But as it was feared that the money would not come in fast enough, the attempt was made to borrow the money on the hypothecation of the subsidy, at the same time giving three royal princes as hostages. Scarcely one-fourth of this loan could be obtained; the king was obliged to mortgage the crown and the crown jewels to raise the remainder.[25]

During the late 1500s, Elizabeth I revived Richard II's law regarding the raising of forced loans, but in the end had to have recourse to Antwerp for the finance she

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22 Presentations by Y. Sakai, vice president of Meiji Mutual Life Insurance, and by K. Narusawa, economic adviser to the Bank of Tokyo, at an Australia-Japan Economic Institute seminar on *Australia-Japan: Scrutinising the Financial Links*, Sydney, 1984, pp.37,90.

23 Carolyn Cummins, "The Money-Go-Round" in *The Australian*, 18 February 1993, p.29.

24 Martin Mayer, *Markets* (Simon and Schuster, London, 1989), p.183.

25 Cohn, op.cit., pp.650-651.

sought.[26]

The formal inauguration of a system of public credit began in England in the aftermath of the revolutionary overthrow of James II in 1688 (and the continuing conflict with France) and the establishment of the Bank of England in 1694. As Cohn has described,

> The reign of William III opened amidst financial difficulties which had been aggravated by the war. . .the customary revenues declined in consequence of the war. . .The same taxes which had yielded net receipts of £2,000,000 before the Revolution, yielded in 1693 only £1,100,000. . .the form of public credit employed was. . .the system of rents or annuities after the Dutch model. In 1692 an attempt was made to borrow one million by this method, on annuities to run ninety-nine years, at 10 per cent until 1700, and at 7 per cent after that date; but it was impossible to raise the full amount under these conditions. The following year one million was borrowed on annuities of sixteen years' term, with annual payments of 14 per cent. . .In 1697 the Chancellor of the Exchequer, Montagu, invented the exchequer bills, issued to some extent in denominations of five and ten pounds, as an expedient for remedying the scarcity of money. . .The government borrowed from the Bank of England and the East India Company. . .The entire national debt at the close of 1701 amounted to 16.4 million pounds, and the interest charge on the debt to 1.3 million pounds. . .Anticipation of future tax revenues and the sale of annuities remained the staple forms of public credit.[27]

In 1716 the institution of the National Debt was formalised in England, under the Prime Ministership of Walpole, with the passage of the General Fund Act which provided for a Sinking Fund by which the surplus of certain duties and funds was to be "appropriated, reserved, and employed to and for discharging the principal interest of such national debts. . .as were incurred before. . .1716".[28] From a total of around £50 million pounds at the time of the establishment of the Sinking Fund, the debt rose, through Britain's participation in the Seven Years war against France in the mid-1700s, to £139 million by the end of the 1760s. Expenditure on war against the colonists in America caused the debt to increase to £250 million by the 1780s and expenditure on further war against France (under Napoleon) increased the debt to £840 million by 1815. Although the debt was reduced to around £700 million just before the outbreak of the Great War, vast British expenditures on the war caused the debt to escalate massively to around £7,500 million by the end of hostilities.[29] While around £1 billion of that debt consisted of loans raised in the

[26] ibid.

[27] ibid., pp.653-654.

[28] G. Findlay Shirras, *Science of Public Finance*, Vol.II, third edition, p.886.

[29] ibid., p.883.

USA (beginning in 1915 with a loan placed in New York for $500 million) the rest of the debt was mainly internal, resulting from several large issues of War Bonds.[30] Again, when conflict began with Germany a second time, indebtedness was increased by the raising of War Loans, during 1939 to 1945, to support the war effort. By 1955 the British National Debt had reached £26 billion.[31]

Britain was not the only major country in the world to contract a national debt during the nineteenth and twentieth centuries. France was renowned for the size of its national debt (a significant part of which was subscribed to by a large number of small bondholders) and just before the outbreak of the Great War the French national debt had reached 32,974 million francs. As a result of large-scale issuing of loans to finance its participation in the First World War, France's national debt, by 1921, had reached 297,368 million francs.[32] In USA, similarly, the beginnings of its present large national debt occurred as a result of borrowing to finance its part in the European and Pacific Wars of 1939-1945. Vernon Mund observed in 1960 that "As a result of government borrowings to finance public works and military expenditures, the gross public debt of the federal government rose from some $22 billion to nearly $43 billion in 1940. . .with the entrance of the United States into World War II, the national debt increased rapidly and by the close of the war it had reached a total of over $258 billion. Although some of the borrowed funds were secured from the savings of individuals, a very large part was secured by the sale of government bonds to the commercial banks and the creation of bank deposits and Federal Reserve notes."[33] Over the subsequent decades the American national debt rose to $542 billion by 1975; to just over $1,500 billion by 1984; to around $3,000 billion by the end of the 1980s; and to the present figure of $4,667 billion.[34]

2 GOVERNMENT BORROWING IN AUSTRALIA

(a) Nineteenth to the mid-Twentieth Century

At the beginning of settlement in the continent of Australasia the main source of revenue, according to Noel Butlin, was "Treasury Bills drawn on Britain". Subsequently the British Government decided to make customs and excise play a

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30 Philip Bagwell and George Mingay, *Britain and America 1850-1939: A Study of Economic Change (Routledge and Kegan Paul, London, 1970), p.240*; see also Birck, op.cit., p.267; Shirras, op.cit., p.903.

31 Homer, op.cit., p.190.

32 Kindleberger, op.cit., pp.167,296; Birck, op.cit., pp.277-278.

33 Vernon Mund, *Government and Business*, third edition (Harper Brothers, New York, 1960), pp.507-508.

34 figures from the February 1995 issue of the American monthly magazine *Congressional Digest* (Congressional Digest Corporation, Washington DC, 1995), p.38.

greater role in contributing to the colony's revenues and, as Butlin further describes, revenue from customs and excise "lifted sharply in 1825. By the early 1830s, it briefly rivalled Treasury Bills from the Commissariat and peaked in 1841". Government revenue was also obtained from the lease, rent and sale of land. Meanwhile control over revenue raising began to be handed to settlers when the NSW Legislative Council (which had been established in 1823) was given, eleven years later, responsibility for approving appropriations. When land sales collapsed in the 1840s, and revenues declined, as Butlin recalls,

> the colonists turned to a related revenue device, the issue of debentures on the security of prospective land revenues. . .So began an Australian practice of public borrowing on the basis of revenue expectations, a practice continued into the 20th century.[35]

In the case of Victoria (established in 1851) only six years after the colony's foundation the Victorian Government succeeded in having six local banks accept a tender for a government loan of £8,000,000 for the development of railways and roads.[36] Similarly when Queensland was founded in 1860, for example, as Trevor Sykes has described, "The State's first public loan was raised within Queensland in 1862 for £123,800. Its second was placed in London, using the Union Bank of Australia as agent, for £707,436."[37]

Although money for public expenditure was being raised within the colonies, by the end of the nineteenth century the greater part of colonial loans were raised overseas: principally in Britain which was not only the centre of the British Empire but was at that time, as described above, the centre of international finance.

Expansion of colonial borrowing was largely undertaken to finance construction of each colony's railway system. Even by the 1860s this was becoming a major element in people's professed concern about the public debt. According to an account of the NSW Colonial Treasurer's Financial Statement in 1865, he noted that,

> In 1855 there were only 13½ miles of railway open in the colony, and the capital invested therein amounted to £515,347. In 1864 there were 142 miles

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[35] Noel Butlin, *Forming a Colonial Economy: Australia 1810-1850* (Cambridge University Press, Melbourne, 1994), pp.82-92.

[36] When the Melbourne Stock Exchange opened in 1860, debentures issued by New South Wales, Victoria and South Australia were among the leading stocks on offer. See *The House of Were*, company history of J.B. Were and Son (J.B. Were and Son, Melbourne, 1954), p.77.

[37] Trevor Sykes, *Two Centuries of Panic: A History of Corporate Collapses in Australia* (Allen and Unwin, Sydney, 1988), p.86. By the late 1800s sem-government authorities had also begun to float substantial issues. In 1897, for example, the Melbourne and Metropolitan Board of Works issued tenders for a loan of £500,000. See *The House of Were*, p.145.

> open, and the capital invested was £2,631,790. There were nearly 3,000 miles of telegraph open. . .There has also been expended during the last ten years, out of revenue, £2,158,495 on public works, roads, bridges, etc. This large sum was exclusive of loans. The public debt had assumed gigantic proportions, considering the population. The sums raised by loan, and authorised to be raised, amounted to £8,213,380, the interest on which was equal to £1 per head of every man, woman and child in the colony.[38]

Despite these publicly expressed concerns, borrowing for the railways continued and a statistical survey of New South Wales, published in the 1880s, noted that "the cost of the 1,688 miles of completed railway was £18,726,740, which amount (with the exception of £723,508 paid out of the Consolidated Revenue) was raised by loans."[39] Indeed, according to Boris Schedvin, writing on the combined debts of the newly constituted states, just before the outbreak of the Great War, "as much as two-thirds of the public debt of £313m was domiciled overseas".[40] The different colonies, transformed into states after federation in 1901, used leading London banks to conduct their issuing business: New South Wales and Victoria using the London and Westminster, and Queensland using the Bank of England.[41] Federation inaugurated the Commonwealth Government which also entered the field of international borrowing.

The strains on British lending caused by the First World War, however, turned the focus of Australian borrowing back to the local financial community for funds to support Australia's contribution to the war against Germany. Were's company history later remarked that,

> A new era in public finance was opened up in July 1915, when it was announced that a loan of £20 million at 4½ per cent at par was to be raised for war purposes. Hitherto all Commonwealth Government Loans had been floated overseas, but, with Britain's financial resources strained to the limit, it had been decided to invite the Australian public to subscribe the money locally. A first instalment of £5 million attracted a total of £13.4 million from 18,748 subscribers; whilst a second instalment of £10 million in

[38] *Official History of New South Wales* (Government Printer, Sydney, 1883), pp.407-408.

[39] Augustus Morris, *New South Wales: Its Progress, Present Condition and Resources* (Government Printer, Sydney, 1886), p.143.

[40] C.B. Schedvin, *Australia and the Great Depression: A Study of Economic Development and Policy in the 1920s and 1930s* (Sydney University Press, Sydney, 1970), pp.91-92.

[41] A.R. Hall, *The London Capital Market and Australia 1870-1914*, social science monograph no.21 (Australian National University, Canberra, 1963), p.89.

December 1915 brought £21.6 million from 28,945 subscribers.[42]

Between 1915 and 1921 the Commonwealth Government raised over £250 million through seven War Loans, two Peace Loans and a Diggers' Loan.[43]

Despite restricted access to British finance during the Great War, the States returned to borrowing in London during the 1920s and, to a lesser extent, also began to borrow in the new centre of international finance: New York. Indeed the States had significant plans for expansion which included further infrastructure development, and large-scale immigration and land settlement schemes. Schedvin has written that there was considerable attention,

> devoted to providing facilities for the growing industrial and urban areas. With the development of motor transport, electric power and improved housing standards, the demand for the construction of roads and bridges, electricity and telegraph, and water and sewerage facilities expanded rapidly.[44]

According to Were's company history "between 1921 and 1931, the Commonwealth and the States had raised £624,000,000 by means of external and internal loans. Of this total, £165,989,000 had been raised in London, £33,905,000 in America, and £424,177,000 in Australia. By 1931 Australia's public debt had risen to £1,153,910,000, or £177/11/4 per head of the population".[45]

In 1928 significant changes to loan raising were introduced through the conclusion of a Financial Agreement between the Federal Government and the States (ratified by referendum). The agreement provided that the States would no longer borrow in their own names: the Commonwealth Government would raise loans on behalf of the States through a Loan Council (consisting, essentially, of the Federal and State treasurers). The Agreement also provided for the establishment of a National Debt Sinking Fund to deal with the redemption of State debt.[46]

It was the Depression of the 1930s, during the depths of which Australia's national income fell by about £150 million a year, that once more deflected the focus of borrowing in Australia to the local financial community rather than overseas with loans tending to be raised internally rather than in London, or New York. Indeed,

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42 *The House of Were*, p.179.

43 ibid., p.190.

44 Schedvin, op.cit., pp.68-71.

45 *The House of Were*, p.292,

46 Russell Mathews, *The Australian Council: Co-ordination of Public Debt Policies in a Federation*, Centre for Research on Federal Financial Relations, reprint series number 62 (Australian National University, Canberra, 1984), pp.2-3.

during the worst years of the Depression financial conditions deteriorated in both Britain and the USA and Australia found itself, momentarily, unable to borrow in either financial centre. A J.B. Were company publication noted that in 1937 that the total net debt of the Federal Government and the States still amounted to around £1,200,000,000 but that the composition of the debt had changed to the following: "Loans redeemable in Australia. . .£674,509,000; Loans redeemable in London. . .£543,412,000; Loans redeemable in New York. . .£44,949,000."[47] R.S. Gilbert has commented that "The cessation of foreign lending to the Commonwealth on behalf of the Loan Council in 1929 and its serious effects were long remembered. Over the next twenty years, the Council raised few loans abroad and, in fact, the emphasis was on reducing the amount of government indebtedness abroad."[48]

The loss of national income during the Depression also led to the formal acceptance of short term government borrowing of public savings, to cover budget deficits, through the issuing of Treasury Bills. Were's 1937 publication on Commonwealth Bonds described the inauguration of this, and the progess of it during the 1930s as follows:

> Before the depression, the Federal and State Governments financed themselves over periods of revenue lag by the issue of short-dated Treasury Bills or Revenue Bonds, which were accepted by the banks as security for overdrafts. Treasury Bills were also sold over the counter to the general public, and they afforded a convenient avenue for the disposition of business working capital temporarily exceeding the requirements of its owners. The issue of Treasury Bills in this way was not a public issue in the ordinary sense. As revenue was collected by the borrowing governments the overdrafts and loans were paid off and the Treasury Bills retired. When the economic crisis arose. . .public revenues were immediately affected, and every Australian Government sought abnormal accommodation in order to carry on its ordinary services and to provide for the completion of works already authorised which should have been financed by public loans. This situation created a problem for which there was no solution until the Commonwealth Bank gave way to pressure and conceded to governments the right to draw upon the bank the stored savings of the people required (a) to carry on the public services, and (b) to provide, to a limited extent, for the completion of public works and for indigent sectional relief. The Commonwealth Bank accepted Treasury Bills in steadily increasing measure, and granted proportionately extended credit accommodation to the issuing Government, and it distributed as many of the Treasury Bills amongst the Trading Banks as the latter's individual cash and credit requirements from the central bank from time to time determined. In effect, this meant that the governments had

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[47] *Commonwealth Bonds and other Debentures* (J.B. Were and Company, Melbourne, 1937), pp.8,18.

[48] R.S. Gilbert, *The Australian Loan Council in Federal Fiscal Adjustment, 1890-1965* (Australian National University Press, Canberra, 1973), p.268.

> substituted one form of borrowing for another and applied the proceeds to ordinary instead of extraordinary expenditure. . .under the strict control of the Loan Council, loan raising was resumed in Australia, but the Commonwealth Bank was still required to finance budget deficits by means of Treasury Bills. These Treasury Bills, being discountable on demand at the Commonwealth Bank, were virtually as good as cash to the trading banks, which found in them a ready avenue for the investment of funds which, under the abnormal conditions existing, could not find an outlet in the ordinary banking channels. Under. . .arrangements for the balancing of budgets. . .the requirements of governments for this purpose gradually decreased, while public works were financed mainly through loans raised publicly in Australia.[49]

The advent of a second great war in Europe, and the subsequent war in the Pacific, again led to a large War Loan raising program in Australia in which the focus of borrowing remained on the local financial community. Were's company history has described how,

> During the war period, the public, for patriotic reasons. . .readily subscribed to the huge amount of £1,101 million required by the Commonwealth for war and works purposes between December 1939 and August 1945. . .The cost to Australia of the 1939-45 war up to 30th June, 1949, was £2,872 million. Subsequent expenditure directly attributable to the war would raise the total well in excess of £3,000 million. One item alone, the War Gratuity, which was disbursed in March 1951 to personnel who served in the wartime fighting forces, cost about £80 million. Of the expenditure incurred during the actual war period, approximately £730 million was provided by taxation, £958 million by public loans (excluding the amounts raised for public works and for conversions, etc.), War Savings Certificates, interest free loans, etc.; and £343 million by Treasury Bills.[50]

During the war another change occurred which affected public borrowing in Australia when, in 1942, the Curtin Government secured the passage of legislation transferring income tax powers from the States - which had until then, from the days when they had been colonies possessed these powers - away from them. From then on, income tax raising belonged to the Commonwealth Government, meaning that any future borrowing by the States on the basis of future revenue expectations would have to be undertaken on the basis of changed revenue outcomes.[51]

At the end of the war, in 1945, Australia's total indebtedness (Commonwealth and the States) amounted to £2,630 million a significant of this "total Australian

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49 Commonwealth Bonds and other Debentures, pp.18-19.

50 *The House of Were*, p.365.

51 Mathews, op.cit., pp.14-15.

indebtedness" as Were's company history pointed out was that "no less than £2,066 million represented local loans."[52]

(b) 1950s to the 1990s

During the 1950s total public debt increased only gradually due to exertion by the Loan Council of careful control over the contracting of loans and the direction of issuing continued to remain focused on Australia. In 1959 a J.B. Were publication advised that "of the total public debt of Australia, internal and external, amounting to £4,249 million at 30th June, 1959, £2,494 represented State debts. . .of the total public debt of the Commonwealth and the States, no less than £3,590 was owed to Australian citizens, whilst overseas debts amounted to only £659 million." Of the amounts owed overseas, debts of the Commonwealth and the States payable in London, in 1959, amounted to £415 million. Debts of the Commonwealth and the States payable in New York, in 1959, amounted to about £77 million.[53]

During the 1950s certain state authorities began to emerge as some of the biggest borrowers in Australia. Were's company history commented in 1954, regarding borrowing by Victoria's electricity authority, that "The largest of the public body loans issued during 1953 was that of £4,250,000, underwritten by J.B. Were and Son for the State Electricity Commission which, in recent years, had become Australia's largest and most successful borrower."[54]

With its superior revenue position the Federal Government was indeed able, during the 1960s, to actually reduce its debt. In 1965 Wilfred Prest commented, on an overall level, that "in the post-war era the Commonwealth has been able to reduce its net indebtedness while that of the States has been increasing."[55] Indeed, according to E.A. Boehm and P.B. Wade, writing in 1971, "by the end of 1968-69 the net debt of the Commonwealth had disappeared." Expressing the figures in dollars, after the introduction of decimal currency in the 1960s, Boehm and Wade wrote that,

> The net debt of the Commonwealth has fallen from $3,154m in 1945 to zero in the late 1960s. . .For the States, on the other hand, net debt has risen sharply over the same period from $2,004m to $11,335m. . .The increase in the States' debt has occurred mainly in Australia, with overseas debt

52 *The House of Were*, p.408.

53 *Were's Guide to Australian Loans and Debentures*, seventh edition (J.B. Were and Son, Melbourne, 1959), pp.1,8.

54 *The House of Were*, p.506.

55 Wilfred Prest, "Federal-State Financial Relations" in *Economic Papers*, no.20, October 1965, p.21.

generally falling since 1945. . .[56]

In the mid-1970s the public debt of the States remained at around the figure of $11 billion, and the Commonwealth retained its zero debt status. However a new element began to emerge of debts incurred by federal authorities which by 1979 had reached $7.9 billion.[57]

During the period of the Fraser and Hawke Federal Governments, with both endorsing a more unrestricted approach to borrowing, the level of public debt began to increase significantly at both a federal and a state level. At its June 1982 meeting the Loan Council decided that no Council approval would be required over the amounts and terms of domestic borrowing by Commonwealth and State electricity authories.[58] In 1983 the States were permitted to each establish a Central Borrowing Authority (in the case of New South Wales, the NSW Treasury Corporation). The States - still not permitted, by the terms of the Financial Agreement, to borrow in their own right - would be able to access the funds borrowed by the CBAs (which would borrow on behalf of all authorities in a state).[59] By mid-1987 Commonwealth Government indebtedness had reached around $41.5 billion and the States' indebtedness amounted to nearly $61 billion.[60]

By the 1990s this indebtedness had risen even further and Alan Kohler, writing in *The Australian* in 1992 estimated the debts of the States as follows:

Victoria	$31,611 million
New South Wales	$20,305 million
South Australia	$ 9,848 million
Western Australia	$ 9,411 million

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[56] E.A. Boehm and P.B. Wade, "The Anatomy of Australia's Public Debt" in *The Economic Record*, Vol.47, September 1971, pp.315,322,325.

[57] J.P. McAuley, *The Structure of the Australian Public Debt*, research monograph no.34 (Centre for Research on Federal Financial Relations, ANU, Canberra, 1980), pp.10,45.

[58] Kevin Foley, "Quangos and the Australian Loan Council" in the *Australian Journal of Public Administration*, Vol.XLII, no.2, June 1983, p.145.

[59] Russell Mathews, *The Australian Loan Council: Co-ordination of Public Debt Policies in a Federation*, Centre for Research on Federal Financial Relations, reprint series no.62 (ANU, Canberra, 1984), p.17.

[60] Economic Planning and Advisory Council, *Trends in State Finances and Fiscal Policy*, discussion paper 90/09 (Australian Government Publishing Service, Canberra, 1990), p.4.

Queensland $ 8,821 million[61]

Federal Government debt, in 1993, was estimated to have risen to $70 billion.[62]

3 CONSIDERATIONS IN REGARD TO GOVERNMENT BORROWING

(a) Acceptability of Government Borrowing

Borrowing in itself, as the outline above indicates, is not something out of the ordinary. The world functions, in part, through international borrowing. In a sense it is a second level of public contribution to government - apart from the tax which financial concerns provide to their domestic governments, those same financial institutions are also enabled to "invest" in governments: both in their own and in others. Public debt can also be over-emphasised in discussions over the issue of public borrowing in relation to State and Federal finance. Sidney Homer, in his history of interest rates, cites Thomas Babington Macauley, commenting in 1885 on the national debt in his history of England, as a precaution against exaggerating the role of debt in a nation. Macauley wrote, as Homer recalls, that from the 1700s,

> the nation owed about fifty millions; and that debt was considered, not merely by. . .fox-hunting squires. . .but by profound thinkers, as an encumbrance which would permanently cripple the body politic. Netherless . . .the nation [became] richer and richer. Then came the war of the Austrian Succession; and the debt rose to eighty millions. Pamphleteers, historians and orators pronounced that now, at all events, the case was desperate. Under the prodigal administration of the first William Pitt, the debt rapidly swelled to £140 million. . .Men of theory and men of business pronounced that the fatal day had now really arrived. . .It was possible to prove by figures that the road to national ruin was through the national debt. It was idle, however, now to talk about the road; we had reached the goal; all was over; all the revenues of the island were mortgaged. Better for us to have been conquered by Prussia. . .And yet [one] had only to open his eyes to see improvement all around him, cities increasing, marts too small for the crowd of buyers, harbours insufficient to contain the shipping. . .houses better furnished. . .smoother roads. . .The prophets of evil. . .saw that the debt grew; and they forgot that other things grew as well as the debt.[63]

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[61] Alan Kohler, "Hard Task Ahead for Kennett" in *The Australian*, 15 August 1992, p.16.

[62] Robert Garran, "$13.4bn Blowout in Government Debt" in *The Australian*, 19 June 1993, p.4 citing Australian Bureau of Statistics, *Australian National Accounts: Financial Accounts*, publication number 5232.0.

[63] Homer, op.cit., pp.189-190 citing Thomas Babington Macauley, *History of England* (1885), Vol.IV, p.432.

Although Macauley's description leaves out certain important details,[64] the essential issues regarding the state of a nation are its productive capacity and its trading capacity.[65] Debt can dealt with constructively if these two spheres of activity are functioning positively. In Australia's case, however, it must be noted that there are questions over Australia's present trading relationships. While the USA was a borrower nation during the 1800s (with British investors supplying the greatest amount of funds for government bond issues and direct investment in railways and the like), and while the USA was nothing like the exporting nation which Britain was in the nineteenth century, the huge internal market within the USA allowed for the rapid expansion of American industry. Australia at present, although similarly receiving large amounts of overseas funds, does not have a comparable internal market and its external trading position is currently the subject of considerable public discussion.[66]

(b) Reasons for Borrowing

On a primary level the foremost reason for borrowing, as seen in the above outline, is for war. Even in the present day this continues to be the case. During the 1980s the USA, in its contest with Russia, placed further large public issues in financial centres contributing to the increase in government debt noted above. While the greater part of the debt was taken up by American financial concerns a significant part was taken up by foreign, particularly Japanese concerns.[67]

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[64] these would include the great strength of Britain's trading position in the nineteenth century re-inforced by the predominance of the British Navy.

[65] John Stuart Mill stated the case quite baldly in his study of economics when he wrote in 1857 that "This perpetual consumption and reproduction of capital affords the explanation of what has so often excited wonder, the great rapidity with which countries recover from a state of devastation; the disappearance, in a short time, of all traces of the mischiefs done by earthquakes, floods, hurricanes, and the ravages of war. An enemy lays waste a country by fire and sword, and destroys or carries away nearly all the moveable wealth existing in it: all the inhabitants are ruined, and yet in a few years after, everything is much as it was before." See John Stuart Mill, *Principles of Political Economy: With Some of Their Applications to Social Philosophy*, Vol.I, fourth edition (John W. Parker and Son, London, 1857), p.93. Laurits Birck, writing in 1926, observed that although Spain, for example, reached a state of bankruptcy during the 1500s "The economic basis of the state, it is true, was permanent, since it consisted in domains, prerogatives and licences and taxes on trades, consumption and circulation." See Birck, op.cit., p.181.

[66] See Rob Fraser ed, *Paying the Banker: Facing Australia's Foreign Debt Problem* (Australian Mining Industry Council, Canberra, 1987).

[67] Peter Hartcher, reporting in the late 1980s and citing figures from the Japanese Ministry of Finance, wrote that out of "total Japanese holdings of US Government bonds", "Japan's life insurers account for about a quarter". See Peter Hartcher, "Healthy US Costs Japan Billions" in the *Sydney Morning Herald*, 8 June 1988, p.41. This could be compared to the situation in the 1700s where

On a secondary level the essential imperatives behind borrowing, as exemplified in Australia, have been outlined quite simply by the historian of J.B. Were and Son (underwriters for many public loans in Australia) when he wrote that, following the creation of Victoria as a colony,

> the government of the recently constituted colony. . .found itself under the necessity of raising loan funds to finance development by means of railways, roads, telegraph and other services, whilst the municipalities and other public bodies also found that current revenue was insufficient to meet the requirements of the increasing population.[68]

The objective behind the borrowing, indicated by the above, was (by borrowing from the business community) to lay the basis (which until then had not existed) for a society based on business. Borrowing was the means chosen because at that stage of its existence Victoria in the late 1850s and early 1860s, as well as Queensland (which also borrowed), did not have the revenue base to fund these undertakings by taxation.

On an overall level, Professor Findlay Shirras, writing in 1936, summarised as follows the advantages of borrowing by governments:

> Public credit enables capital to be borrowed by those who are able to use it to the best advantage. It does not create capital; it enables capital to be employed more effectively. It has made possible very many undertakings which require for their creation and upkeep an amount of capital which no individual could have supplied himself, and in the construction of which the cost could not have been met from the current revenues of the State. Countries have been developed and international trade expanded by public credit. . .Most countries could not have developed their resources as they have done without public loans, including loans in the case of the younger and undeveloped countries from the older creditor countries of the world.[69]

(c) Bond Purchasers

The pre-eminent purchasers of government bonds are the major financial concerns. Malcolm Hill, writing in 1985, commented that in the case of Australia marketable bonds were "the main category of securities accounting for two-thirds of the Australian total." In regard to the question "who holds government securities", Hill wrote that, apart from holdings by official institutions such as the Reserve Bank and major Commonwealth trust funds, "It is clear that financial institutions (if we

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the greater part of British official borrowing overseas was subscribed to in Amsterdam.

[68] *The House of Were*, p.71.

[69] Shirras, op.cit., Vol.II, pp.785-789.

include life and general insurance offices) account for a very large part of non-official holdings." This financial concerns, overall, include the trading banks; the savings banks; life insurance and general pension funds; and authorised money market concerns.[70]

(d) Government Borrowing Strategy

On an overall level, borrowing allows governments to avoid increasing taxes for eventualities lying beyond the simple administration of government. B.E.V. Sabine commented, on England's financial policy during the 1700s, that

> Despite inevitable increases in the rates and subject of taxation, these never became as onerous as they might have been owing to the ease and cheapness of borrowing; and although credit facilities were to a certain extent defective and could result in wild speculation, borrowing enabled England to spend far more on war than was consonant with the tax revenue.[71]

Repayment of the debt has indeed been based on a strategy relied on by governments over the centuries, as outlined by Joseph Martin writing in 1969,

> a sound and growing economy should be able to absorb without much difficulty the rising costs of the National Debt. In Australia the interest on the bill on the National Debt grows at a slower rate than does either the national income or government receipts. Furthermore, the real burden of the interest repayment is made more tolerable by the fact that it is not in direct correlation with the actual debt incurred. In a world subject to a persistent depreciation of the value of the monetary unit through inflation, the borrower - be he a private person or the government - is always at an advantage. Inflation makes it easier to pay debts that are fixed in money terms.[72]

In practice, the form in which this takes place has been described by John Jackson and his colleagues as follows:

> as portions of the debt fall due each month. . .the government simply refinances the debt - that is, sells new bonds and uses the proceeds to pay off holders of the maturing bonds.[73]

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[70] M.R. Hill, "Bond and Money Markets" in M.K. Lewis and R.H. Wallace (eds.), *Australia's Financial Institutions and Markets* (Longman Cheshire, Melbourne, 1985), pp.313-318.

[71] Sabine, op.cit., p.110.

[72] Joseph Martin, *A Guide to Economic Policy in Australia* (West Publishing Corporation, Sydney, 1969), p.24.

[73] John Jackson, Ron McIver and Campbell McConnell, *Macroeconomics*, fourth edition (McGraw Hill, Sydney, 1994), p.280.

A principal consideration in government borrowing strategy is the relationship between the government and the financial houses with which it negotiates its debt. In 1869, for example, the NSW Colonial Treasurer informed the Parliament that "The mode of raising money upon Treasury Bills was considered dangerous, as they placed the Government at the mercy of the banks".[74] In the 1920s, Professor Laurits Birck warned that "A serious and dangerous effect" of public debt "both for the general public and for the State is that both national and international high finance get the opportunity of interfering with governments."[75]

It was in fact these considerations which led to the original establishment of the Loan Council, on an informal basis, in 1924. The aim of the Federal Treasurer - and the Treasurers of New South Wales, Victoria and South Australia - who together made up the informal Council, was to gain, from the financial houses, interest rates which were to the governments' advantage. Schedvin has described how, between 1924 and 1927,

> the Council operated with moderate success despite the absence of New South Wales between 1925 and 1927. A number of loans were floated in the local market in the name of the Commonwealth on behalf of the States, and in 1927 a large issue was made in New York on this basis. . .In this period the rate of interest fell to around 5¼%. . .[76]

During the 1980s, however, the financial concerns have been able to exercise power back in the opposing direction. In 1982, for example, at a seminar on public sector borrowing in Australia, the chairman of Bain and Company stated that it was his opinion that "The main need, as we see it, is for the authorities to become price-takers and not price-makers in the bond market."[77] In 1983 the newly elected ALP Federal Government under Bob Hawke began to wind down constraints on interactions between Federal and State Governments and the bond market. In 1992 the Keating Government actually began to return the situation back to the early 1920s by proposing that States once more be able to issue securities in their own names. This proposal was formalised in the subsequent decision, by the Federal Government and the States, to each introduce a *Financial Agreement Bill 1994* amending the Financial Agreement to provide for this.

(e) Problems of Borrowing

As long as the productive capacity and the trading position of nation can be

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74 *Official History of New South Wales*, p.451.

75 Birck, op.cit., p.139.

76 Schedvin, op.cit., pp.92-93.

77 J.K. Bain, "Government Debt and the Capital Market" in R.L. Mathews ed., *Public Sector Borrowing in Australia* (Centre for Federal Financial Relations, ANU, Canberra, 1982), p.51.

maintained, reasonable levels of borrowing, as we have seen above, can be sustained. Unfortunately, business cycles rise and fall, and trading relations change (as in the case of Australia, established to trade with Britain, still experiencing problems with the re-orientation of its trade following the change in Britain's trading position after the Second World War). In cases of trade recession or depression, or decline in the productive capacity of the nation, national income declines - particularly so in the case of Australia in the early 1930s (earning far more of its income from overseas sales than at home) when it encountered diminished trade conditions and consequently found itself in difficulties in paying the interest on accumulated loans. Although Australia is no longer as dependent, as it once was, on one single market to sustain its export trade, similar trade deteriorations pose similar threats (the trade deterioration of 1986 and the recession of the early 1990s being recent examples), so debt must be carefully contracted to cope with these eventualities.

Today the development of the analytical means of economics allows measurement of such capacities in respect to their role in sustaining debt. One basic measurement, on a national level is that of national debt to Gross Domestic Product (GDP) or at the State level that of state debt to Gross State Product. This will be looked at in the last part of this section, and in the fourth section of this study.

Bonds taken up by foreign investors, and for which they receive payment in their own currencies, can create problems for government when the issuing government's currency declines in value - particularly if there is a government policy of allowing the currency to find its own level in the business and financial community. This scenario appeared to be possible in Australia in 1986 when the returns from Australian goods exported declined dramatically in 1986.

(f) Burden of Repayment

The situation, in a society, of bondholders - and those who do not hold bonds, has been outlined by Roger Waud and his colleagues as follows:

> government bonds outstanding are not distributed equally among the nations citizens. Some people hold none and others hold a great number. However, any attempt to retire some or all of the debt would have to be financed out of taxes that are paid by all citizens. . .This large transfer payment would result in a redistribution of income. Some citizens would end up paying out an amount of taxes larger than their holdings of government bonds.[78]

One of the considerations which consequently arises in matter of repayment of debt is that of equity. One of the very early economists, Sir William Petty, wrote in 1662 that, "It is generally allowed by all that men should contribute to the public charge but according to the share and interest they have in the public peace; that is,

[78] Roger Waud, Philip Maxwell and Josef Bonnici, *Macroeconomics*, second Australian edition (Harper Collins, Sydney, 1992), p.282.

according to their estate or riches."[79]

Professor Laurits Birck remarked in 1926 that with regard to the borrowings raised by Britain, France and Germany to finance their war with each other between 1914 and 1918 "the national debt. . .throws the burden on the general public; in the struggle between the classes as to who shall bear the burden of war it has so far been the lower class which has had the worst of it". Birck illustrated his point by summarising the attitude of the financial community in London and New York towards repayment policy after the end of the war,

> the. . .opinion of the City and Wall Street may be summed up as follows: The State should finance a war by means of short loans and convert these, immediately after the war, into fixed loans to be amortised over 50 years, the tax on income being left, in a less proportion however than today, to take its share of the interest and amortisation of these loans; on the other hand indirect taxation must be considerably increased, in order that some of the amortisation of the debt can be covered by lesser consumption on the part of the people without means; at the same time the so-called social expenditure (housing, health, children and old age) must be cut down. . .[80]

This is precisely what happened in Australia when, having accumulated a debt of £624 million during the 1920s, the depression of 1930s began in 1929.[81] In 1987, following the trade deterioration of 1986, commentators such as Rob Fraser were advising that "The message for the Government is that the first step. . .must be the recognition by all Australians that we have suffered a loss in living standards and that further falls are probably inevitable."[82]

(g) Overall Ability of Australia to Repay Debt

In their outline on the Public Debt, John Jackson and his colleagues wrote the

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[79] Sabine, op.cit., p.110. Divisions in society were acknowledged by later economists. Professor Alfred Marshall, one of the founders of micro-economics, remarked in 1890 on the issue of shortening working hours that "it would probably be well that most people should work rather less; provided that the consequent loss of material income could be met exclusively by the abandonment by all classes of the least worthy methods of consumption". See Alfred Marshall, *Principles of Economics*, eight edition (MacMillan, London, 1961), p.720.

[80] Birck, op.cit.,pp.136-138. John Stuart Mill, in discussing the national debt in Britain in the mid-1800s, cited the view of Professor Thomas Chalmers that avoiding privation after war by endorsing a policy of repaying debt by further loans "is not averted, but only thrown upon the labouring classes; the least able, and who least ought, to bear it". See Mill, op.cit., p.97.

[81] Schedvin, op.cit., p.249.

[82] Fraser, op.cit., p.75.

following in approaching an estimation of the capacity of Australia as a whole to repay its borrowings, basing their evaluation on the relationship between public debt and Gross Domestic Product:

> a wealthy nation has greater ability to incur and carry a public debt than does a poor nation. In other words, it seems more realistic to measure changes in the public debt in relation to changes in the economy's GDP. . .although the debt increased by 450 per cent between 1969-70 and 1991-92. . .we. . . find that the relative size of the debt declined from 43.2 to 15.6 per cent of GDP during the same period. . .as a percentage of GDP, Australia's net public debt is small relative to that of most developed economies.[83]

4 NEW SOUTH WALES DEBT AND THE GENERAL GOVERNMENT DEBT ELIMINATION BILL 1995

(a) The New South Wales State Debt

Currently the NSW state debt stands at about $22 billion. This is made up, as in the *NSW Budget Papers 1994-1995*, of net budget sector debt of $15,575 million and net non-budget sector debt of $6,287 million.[84] This tends to correspond to the outline entitled "T-Corp's Loans Outstanding to Authorities" in the annual report of the NSW Treasury Corporation.[85]

(b) NSW Capacity to Repay State Debt

Roger Waud and his colleagues, in discussing the issue of debt at a national level, have also written that in regard to "the economy's ability either to retire the public debt or to pay interest on it. . .A reasonable measure of this ability is the size of the GDP relative to the size of the debt and the amount of interest payments that must be paid on it."[86] In the case of New South Wales, Gross State Product (GSP) in financial year 1992-1993 for example - as contrasted with Gross Domestic Product (GDP) on a national level - was $138.886 billion.[87] The ratio for evaluating the capacity of New South Wales to meet the obligations of its debt would be roughly equal to that of NSW State Debt ($22 billion) to Gross State Product ($139 billion).

According to Michelle Coffey, writing in *The Australian* in May 1995, the ratio of

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83 Jackson et.al., op.cit., p.280.

84 *NSW Budget Papers 1994-1995*, Budget Paper no.2, p.9 - 7.

85 NSW Treasury Corporation, *Annual Report to Parliament: Year Ended 30 June 1994*, p.37.

86 Waud et.al., ibid.

87 Australian Bureau of Statistics, *Australian National Accounts: State Accounts 1992-1992*, ABS Catalogue no.5220.0, p.11.

New South Wales net public sector debt to Gross State Product was 15% and on that basis was second only to Queensland in terms of each State's ratio of net public sector debt/GSP and currently enjoys an AAA rating within the financial community.[88]

(c) The General Government Debt Elimination Bill 1995

In early March 1995 the now Premier, the Hon. Bob Carr, issued the draft of a *General Government Debt Elimination Bill 1995* which the then opposition leader said, in an accompanying press release, "would be introduced in the first session of Parliament after the March 25 elections."[89] In his press release the then opposition leader stated that,

> the State's total debt had grown to $22 billion. . .This is equivalent to a debt of almost $4,000 for every man, woman and child in New South Wales. . .the children and youth of New South Wales would be seeking employment in a fiercely competitive global economy. That competition will intensify in the years to come. It is vital therefore that we do not lumber future generations with debt. We owe it to them to plan for their future now. We should give them the same opportunities for a good standard of living as our generation was given. We must not become the first generation to leave the next generation with a fallen standard of living.[90]

The then opposition spokesman on finance, the Hon. Michael Egan, outlined the implementation of the proposal if the ALP gained office in the March 1995 election,

> It will require the Government to first produce a plan to eliminate general government debt by the year 2020. . each year the Government would have to report progress and produce an updated plan to achieve the 2020 target in view of whatever changes occur in the State's financial circumstances. The plans. . .will impose a strong financial discipline on all future governments.[91]

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88 Michelle Coffey, "Victoria in Surplus but Focus Remains on $33bn Debt" in *The Australian*, 3 May 1995, p.1.

89 Bob Carr MP, Press Release, 7 March 1995: *A Debt Free State - Labor's Commitment to the Next Generation.*

90 David Chessell, in his 1989 survey of the views of economists on public debt, wrote that in his view "The question of the burden of debt has long been a subject of divergent views among economists. The generally accepted position at this time is that the burden of the debt falls to a large degree on future generations." See David Chessell, "Managing the Public Debt" in Chris Ulyatt (ed.), *The Good Fight: Essays in Honour of Austin Stewart Holmes* (Allen and Unwin, Sydney, 1989), p.79.

91 Bob Carr MP, Press Release, 7 March 1995.

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