

HEALTH AND THE 2006-07 FEDERAL BUDGET

A REPORT BY
ACCESS ECONOMICS PTY LIMITED

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EXECUTIVE SUMMARY

Budget in the broad

- The continued strong growth of the economy and the fiscal drag combined to ensure strong revenue growth in the current (2005-06) year. On a cash basis, revenue is estimated to be 9% higher than in 2004-05, trumping last year's growth of 8.9%.
- The Budget outcome, an underlying surplus of nearly \$15b, would have been closer to double the budgeted \$9b were it not for spending brought forward into this year. In the health portfolio, \$264m of spending was brought forward.
- Some commentators have called this the "magic pudding" Budget given spending initiatives and the reductions in income and company tax. The income tax reductions appear large. The cost to revenue rises from \$6.4b in 2006-07 to a projected \$10.4b in 2009-10. These amounts are assumed to include the revenue foregone from reform of superannuation. Governments have a track record of being too bullish in the good times and too pessimistic in the bad times. If the revenue estimates are hopeful, then so too are the claimed savings. One key message is that the tax system itself is aggressive by design. Were it not for repeated tax cuts, Federal revenue would claim an ever growing share of GDP. The Budget figures imply that, but for the revenue and spending measures a massive surplus of \$22b was in prospect in 2006-07.
- The Treasurer has not lost his affection for Budget surpluses. Whereas a year ago the forward estimates of the underlying balance were in the range of \$8b to \$9b, this year they are \$10b to \$12b after earmarking even more for the Future Fund. However, the Budget balance is the difference between two very large numbers and it only takes small errors in revenue or spending for the balance to vary significantly.
- Is the Budget strategy sustainable in the longer term? The Government is foregoing a great deal of revenue down the track and counting on an uninterrupted resources boom. Economists are accused of doom and gloom but history is on their side. Australia has enjoyed 14 years of uninterrupted growth. Yet the Australian economy is a speck in the world economy and our economic destiny does depend on the world economic cycle. Booms don't last indefinitely. We'll see ups and downs.
- Is the Budget strategy risky in the short term? Well ... yes. For one thing it puts a lot of money in the hands of consumers which inevitably raises questions about demand-driven inflation and the current account deficit (already very large). The company tax reform encourages business investment which can be import intensive. This Budget has increased the odds of further increases in interest rates this year.

The Health Budget

- Taken at their face value, the Budget figures indicate that the Government attaches no special priority to health spending but is rather more focussed on increasing spending in other areas, notably defence. Against a long history of health spending increasing



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as a proportion of total Budget outlays, the share edged up only slightly in 2005-06 (18.3% cf. 18.2%). Also, the estimated health spending in 2005-06 was only slightly above the Budget figure (a larger blow-out is the norm).

- In 2006-07, the Budget provides for health outlays to grow by 5.9% to be 18.1% of total budget spending (ie, health outlays grow more slowly than total outlays). In the forward estimates period, health spending is projected to grow by only 4.5% a year on average, implying a share of total outlays edging down to 18%. That will be a tough call given the ageing of the population and the high expectations of access to costly new health technologies. Growth of 4.5% will be barely enough to cover health inflation, thus implying a reduction in real health spending per capita (even more so when age-adjusted). If it is achieved (somewhat doubtful), it will require a shifting of the burden of health spending off the Federal Budget and onto household budgets.
- Future governments will have a choice between spending more on health (and raising the ire of taxpayers) or lowering expectations of health care subsidies (and raising the ire of patients).
- The Government's current confidence is reflected in the inclusion of only four savings measures in the Health Budget. Of the four, three are trivial. In a public relations exercise gone mad, one savings measure is comically described as "Better Access to Radiation Oncology".
- A number of the measures in the Health Budget were announced in the weeks leading up to Budget night. The \$1.8b mental health initiative, foreshadowed following the February 2006 COAG meeting, was announced early April. The health portfolio share of the new mental health program totals \$875m over 4 years (the Budget year and the three forward estimate years) with the States' effort yet to be disclosed. The Federal program takes time to get up to speed and spending is back-loaded. This may allow space for the workforce measures to cut in so that the spending is effective.
- The body of this report addresses the other new health spending contained in the Budget. There is potential for good outcomes in health and medical research (\$805m over 4 years) and some of the preventive health measures. New funding for aged care is minimal.
- At the same time, the Government has passed up opportunities to improve health outcomes and improve the functioning of the health system by ducking areas like obesity (a looming health prevention issue), nutrition, health effects of climate change, pressures on public hospitals and reform of the GP consultation item structure.
- The Government is very slow moving in areas like electronic billing under Medicare (a significant opportunity to reduce the cost of the health payments system), initiatives in post-graduate medical training (a looming puzzle when the extra graduates start emerging from the medical schools) and Aboriginal and Torres Strait islander (ATSI) health. There is extra money for Indigenous health and it looks well targeted (eg, extending *Opal*) but the gap between funding and need is still a gaping one. Visionary national leadership is sorely needed in this area.
- In summary, functional areas of spending enjoy their time in the sun. The health portfolio had its last turn in 2003-04. In 2006-07, just two functional areas (defence, public order and safety) are marching off with half of the increase in total Budget outlays. That is the real story of the 2006-07 Health Budget.



1. EVEN MORE REVENUE

In 2004-05, the Federal Government enjoyed rapid revenue growth (8.9% in cash terms), a large real increase given low price inflation. In last year's Budget, the Government handed back \$3b in personal tax cuts but still expected cash receipts to grow by 5.8% in 2005-06. The outcome was much stronger than that. Cash receipts are estimated to have grown by 9% in 2005-06 while, on an accruals basis, receipts soared by \$20b or 10%. Some extraordinary growth rates emerged, petroleum resource rent tax up by 35% (a sharp contrast to the budgeted 7.5% fall), company tax up by 24%, FBT up by 20%, indirect and other tax up by 18%, and non-tax revenue up by 18%. Despite the \$3b in personal income tax cuts, personal income tax surged 6.4% (without tax cuts it would have been over 9%).

Revenue (Accruals Basis), Growth in the Year, 2005-06

Revenue category	Estimated 2004-05	Estimated 2005-06	Change \$m	Change %
Income tax individuals	107,930	114,890	+6,960	6.4%
FBT	3,050	3,660	+610	20.0%
Income tax companies	40,610	50,480	+9,870	24.3%
Income tax super funds	6,380	6,420	+40	0.6%
Petroleum resource rent tax	1,460	1,970	+510	34.9%
Excise duty	22,010	21,900	-110	-0.5%
Customs duty	5,714	5,171	-543	-9.5%
Indirect and other tax revenue	3,047	3,594	+547	18.0%
Non-taxation revenue	12,465	14,779	+2,314	18.6%
Total revenue	202,666	222,864	+20,198	10.0%

Source: Abridged from Budget Paper No. 1, Statement No. 5, table 4

The extra \$8b in receipts — not spending restraint — kicked the Budget balance up to nearly \$15b. A larger figure was in prospect but some new spending announced in this Budget will be rushed through before 30 June.

On a cash basis:

Budget Versus Estimated, 2005-06

	Revenue (cash) \$m	Expenses (cash) \$m	Underlying balance \$m
Budget estimate (last year)	214,515	205,132	+8,921
Estimate (this year)	222,400	207,512	+14,805
Difference \$m	+7,885	+2,380	+5,884
Difference %	3.7%	1.2%	66.0%

Forward Versus Budget, 2006-07

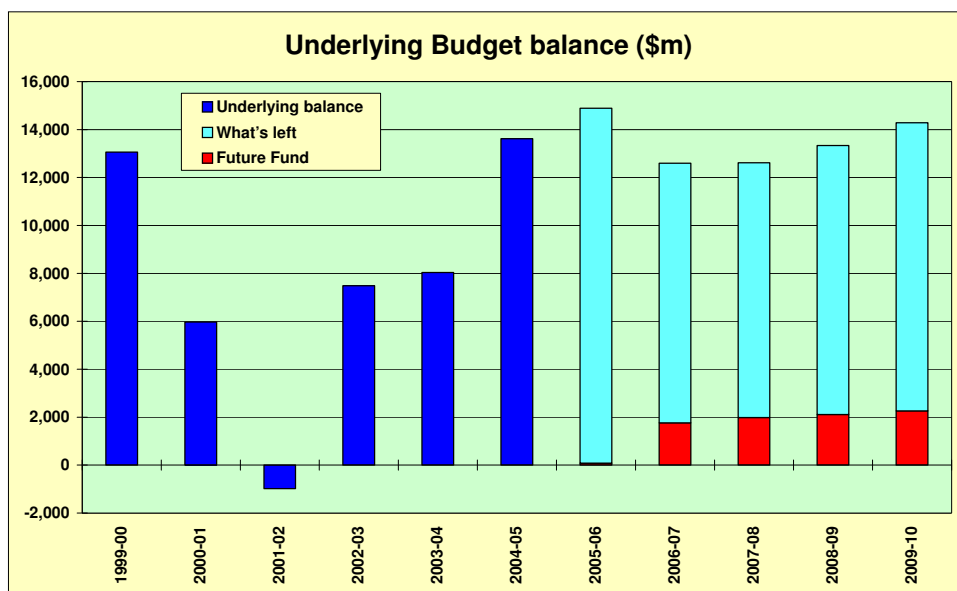
	Revenue (cash) \$m	Expenses (cash) \$m	Underlying balance \$m
Forward estimate (last year)	221,891	213,015	+7,933
Budget estimate (this year)	230,819	218,225	+10,828
Difference \$m	+8,928	+5,210	+2,895
Difference %	4.0%	2.4%	36.5%

Source: Budget Overview 2006-07, Appendix G and corresponding data from 2005-06 Budget papers

2. BUDGET STRATEGY

The Federal Treasury foresees Australia's GDP growing at 3¼% to 3½% in 2006-07 through 2009-10. Inflation is forecast to settle at 2½% p.a. and earnings steady around 4% p.a. Employment grows steadily at 1¼% p.a. and the unemployment rate stays low at 5¼%. Even the current account deficit stays in check (if you think that 6%+ of GDP means in check). World economic growth likewise rolls along. It all adds up to an economic Nirvana, a smooth ride, no bumps. Such a rosy picture understandably breeds political confidence. The Government is content to allow spending (cash basis) to grow at over 5% p.a. so that it sits at a steady 21.6% of GDP from 2006-07 through to 2009-10 (an appearance of contrivance).

Rather than allow fiscal drag to ramp up receipts in real terms, the Government has committed to sizeable tax expenditures. Even so, the underlying Budget balance remains steady at a high level whether or not the transfer to the Future Fund is regarded as an appropriation of the "profit" (the Budget balance) or an accounting provision that reduces it. The Government now envisages larger transfers to the Future Fund (in broad terms doubling them).



Source: Budget Statement No. 13, 2006-07.¹

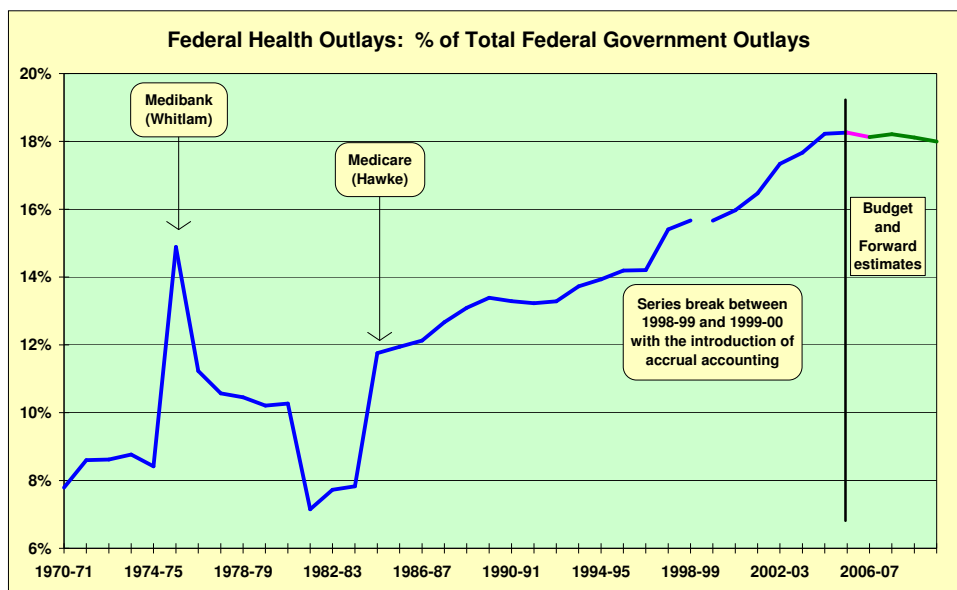
Perhaps we'd all like to believe in this benign picture of the outlook for the Australian and world economies.

Budget Paper No. 1 (Statement No. 3) discusses the risk factors. One potential source of "correction" (polite economic jargon for a slump) is inflation driven by the surge in oil prices. The Australian economy remains vulnerable to shocks from abroad. While commodity prices remain strong, they will underpin the \$A. If commodity prices weaken, a fall in the \$A is indicated and import prices would rise, contributing to inflationary pressure. The Budget strategy depends very strongly on the smooth sailing of the world economy.

¹ All Federal Government data on Budgets must be read with the caution that the Government refuses to acknowledge that the GST is a Federal Government tax on the grounds that proceeds go to the States and Territories. The apparent reduction in Federal revenue to GDP in and post 2000-01 is a fiction.

3. TRENDS IN HEALTH SPENDING

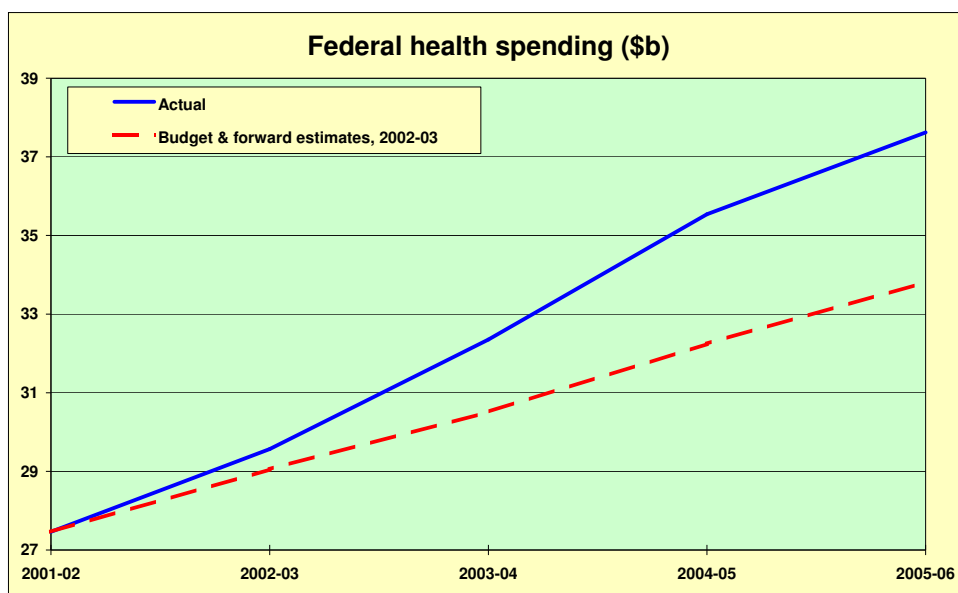
In the 1970s and 1980s, there were wild gyrations in Federal health spending as a share of total Budget outlays while the Whitlam, Fraser and Hawke Governments pushed the public/private spending pendulum back and forth in robust and rowdy disagreement over the appropriate role for the public sector. After the introduction of Medicare in 1984-85, some consensus started to emerge as the major parties competed for the political middle ground. Since then, health spending has risen quite steadily as a proportion of total Budget outlays (from 12% to over 18%) with only occasional short term pauses.



In the Budget and forward estimates period, health outlays are forecast to fall slightly as a share of total Budget outlays. That might be achievable were there considerable restraint in new on-Budget health spending combined with a determination to make households pay a larger share of national health spending. However, history is against it. In the 2002-03 Budget papers, the forward estimate for health spending in 2005-06 was \$33.8b. Actual spending in 2005-06 (as currently estimated) is \$3.8b (11.2%) higher at \$37.6b.

Early forward estimates typically underestimate the actual spending and the size of the “error” in this case is nothing out of the box. The pattern in the chart over the page has been repeated many times over the years. It is far more likely that actual spending will exceed the forward estimates of spending for the same years than fall short of them.

As to the future, whether or not health spending continues to “blow out” ultimately boils down to political choices — on one side, the interests of taxpayers and, on the other, the interests of the so-called “health consumers” (more correctly, those people who are the recipients of investment in health care).



Some suspect that the generation of post-war baby boomers will use their growing power at the ballot box more aggressively to claim health care subsidies. Their potential demands on the Budget are not slight. There are a lot of them and their expectations are high. Interesting times lie ahead as governments try to persuade Australians that we can have our cake (tax cuts) and eat it too (government hand-outs).

4. ROUND-UP OF THE HEALTH MEASURES

Health measures comprise new spending and savings initiatives. A number of the measures discussed in this section were announced in advance of the Budget. The following table condenses the measures (there are over 80 line items in the detailed DoHA list).

Health Budget 2006-07

New measures (\$m)	2006-07	2007-08	2008-09	2009-10	4-yr total
Health research	34.0	106.4	183.9	266.4	590.7
Mental health	103.2	214.0	259.3	298.0	874.5
Health workforce	3.8	3.4	18.2	18.7	44.1
Drugs & alcohol	12.7	27.0	29.1	24.5	93.3
Indigenous health	16.6	26.7	34.0	38.8	116.1
Promoting health throughout life	95.0	124.4	128.3	122.1	469.8
Medicare	72.0	83.5	64.8	68.5	288.8
PHI	12.9	19.1	10.9	15.5	58.4
National health systems	50.9	53.1	68.3	40.8	213.1
Programs for older Australians	20.3	26.1	24.7	22.2	93.3
Other measures	67.9	90.7	107.2	125.6	391.4
Total new spending	489.3	774.4	928.7	1,041.1	3,233.5
Total savings measures	-21.3	-25.5	-20.0	-27.4	-94.2
Net new spending	468.0	748.9	908.7	1,013.7	3,139.3

Over the Budget and forward estimates period (2006-07 to 2009-10), new spending commitments total \$3,324m while savings measures were only \$94m giving net new spending of \$3,139m over the four years. However, the Government has also bundled



\$264m of spending into the current year (2005-06), so the total new money over five years is estimated at \$3,401m.

The DoHA media materials persist with announcements of “continuation funding”. Some programs are only committed for a short period of time (usually four years). At the end of the period, a new four-year program is announced with much fanfare. This undoubtedly leads some punters to think that it is new money but, of course, it is nothing of the kind. These are not temporary programs. The only purpose in having the 4-year commitment is to allow the funding to be re-announced every four years. The “Budget at a Glance” sheet makes that clear because the continuation items are shown as a series of dashes unless a bit more money is tipped in or some money pulled out. The grand announcements of continuation money are both predictable and farcical.

Mental health

At the conclusion of the February 2006 COAG meeting, more action on mental health was foreshadowed. In early April, the Prime Minister announced that the Commonwealth itself would put a new \$1.8b into mental health over five years 2006-07 to 2010-11. In the four years of the Budget (Budget year and the three forward estimates), new Federal spending on mental health totals \$1,413m with the majority of this spent in two portfolios, Health and Ageing (\$875m) and Families, Community Services and Indigenous Affairs (\$410m). The precise amount for the final year (2010-11) is not reported in the Budget papers which stop at 2009-10, although the Prime Minister’s April Press Release mentioned a figure of some \$500m in the final year. There are some indications that the total Commonwealth spending may have crept closer to \$1.9b but that may include Departmental costs of policy and program delivery. The implication is that half the total will be spent in the last two years (2009-10 and 2010-11). That is reasonably typical of a new program.

Cross-Portfolio Summary of the Mental Health Initiative

New measures (\$m)	2006-07	2007-08	2008-09	2009-10	4-yr total
Dept. of Health and Ageing	103.2	214.0	259.3	298.0	874.5
Dept. of Families, Community Services & IA	21.7	92.9	148.5	146.8	409.9
Dept. of Education, Science & Technology	13.1	24.9	28.3	31.1	97.4
Dept. of Employment & Workplace Relations	6.7	8.3	9.3	7.3	31.6
Total all portfolios	144.7	340.1	445.4	483.2	1,413.4

The efforts of the States and Territories will become known over the next couple of weeks as their Budgets are delivered.

The detailed materials indicate that the mental health money is being widely distributed. A range of employment, education and community programs are allocated nearly 40% of the total. The health portfolio holds the largest component as expected and that covers significant components to expand the mental health workforce (psychiatrists, psychologists, GPs and nurses).

It is very encouraging that the Government is paying a lot more attention to workforce issues. Too often, in the past, new spending was announced with little or no regard for workforce shortages and no strategy to deal with them.

The mental health initiative is still being brought together and it is premature to assess the likely outcomes. That said, the Government seems to have wisely ignored most elements of the Senate Committee’s plan to create a myriad of services all over Australia, each needing



a CEO, a CFO and so forth. That plan would have dissipated large amounts of funding in overhead administration costs. The benefit entitlement programs are a far more efficient mechanism.

Health Research

It is not always easy to follow the threads in the customary profusion of Budget kits. To take health research as an example, there is \$590.7m over 4 years (the Budget year and the three years of the forward estimates), plus \$215m to be handed out to recipients (but obviously not spent) before 30 June. That latter amount is part of a whole of government strategy to spend some of the large surplus before this year is out in situations where it is convenient for the money to be warehoused by another party.

The total spending over 5 years is \$805m. The press kits say \$905m. The explanation is that one of the elements (new research fellowships) is committed over 9 years.

The Government has made a very strong commitment to health research. In past years, spending of this nature has produced some very strong returns to the benefit of the Australian people, indeed the whole world. Australian health researchers are world class. This is a proposal to build on our strengths.

Health Workforce

Apart from the health workforce initiatives in the mental health initiative, measures are focussed on more undergraduate places. More consideration is required in relation to the geographical allocation of the places. The faster population growth and more rapid ageing of the population in Queensland and WA in particular would suggest that these are logical places to ratchet up medical education. Per capita allocations of places are unwise.

The missing links are the steps to make sure that when the graduates start emerging from the medical schools, there are enough appropriately supported post graduate training places. Time is running out for this issue to be resolved.

Drugs and Alcohol

Australia maintains a higher degree of separation between mental health services and drug and alcohol services than other advanced western nations. Considerable inefficiency arises from this and the end result is that the expenditure is less effective than it could be. More funding (approaching \$100m over 4 years) has been earmarked for drug and alcohol services. Australia should be embracing structural reform to reshape the services so that they treat the patient in an holistic way.

Indigenous Health

The extra funding for Aboriginal and Torres Strait Islanders' health care is patently inadequate. Australia's Indigenous populations experience very poor health outcomes, indeed below those seen in some third world countries. These poor health outcomes reflect the complex web of social and socioeconomic disadvantage they suffer, including their lack of access to education.



Although the Indigenous population is a much younger population (median age 24 years) than the non-Indigenous population (median age 38 years), their level and severity of illness matches that of non-Indigenous people aged 50-54.

Indigenous Australians have much less access to mainstream programs (Medicare and the PBS) than non-Indigenous Australians. The per capita level of health spending on Indigenous Australians from all sources of funding is indeed higher than for non-Indigenous Australians. Given their very poor health status, per capita spending levels should be a great deal higher.

The Health Budget allocation for Indigenous health has increased substantially over the past decade, which helps. But this is still only a modest part of total Indigenous health costs.

The emphasis on primary care and prevention is laudable, so too the effort to reduce the extent of disadvantage for those living in rural and remote areas. The **OPAL** initiative is estimated to generate more savings than it costs if implemented carefully enough. However, it really does seem to be a case of pointing the vehicle in the right direction but keeping the foot too hard on the brakes.

There can be little doubt that Indigenous health outcomes are better than they might otherwise have been as a result of the shift to the health portfolio and the creation of OATSIS. However, we have failed to materially reduce the gap in health outcomes. There are some encouraging successes but Indigenous people still have 20 years off their lives and much higher rates of illness. Other similar countries with substantial Indigenous populations (US, Canada, NZ) may not have shut the health outcomes gap completely but they are travelling a lot better than we are. Australia is just as capable of solving this problem and culpable for ignoring it far too long. The failure is a failure of choice. Indigenous health has not been given appropriate priority.

Promoting health throughout life

This item involves significant expenditure (nearly \$500m over 4 years). It seems to be an incoherent mix of programs with no common theme. The two “big ticket” items look set to vanish into State government coffers.

Medicare and the PBS

There is nearly \$300m for minor PBS listing and additions to the MBS schedule, but the “Other measures” category has another \$300m for specific inclusions in the PBS.

Private health insurance

Funding is earmarked to assist private health funds to “enhance choices”, a total approaching \$60m over 4 years.

National health systems

More than \$200m is included in this category, the centrepiece being a national call centre network. The effectiveness of call centres is open to question and their purpose open to abuse (another avenue to promote cost-shifting). The call centres which have worked tolerably well in the past have had a specific focus (eg, the Poisons Information Centre). Separate State services are, however, wasteful. A national approach makes more sense.

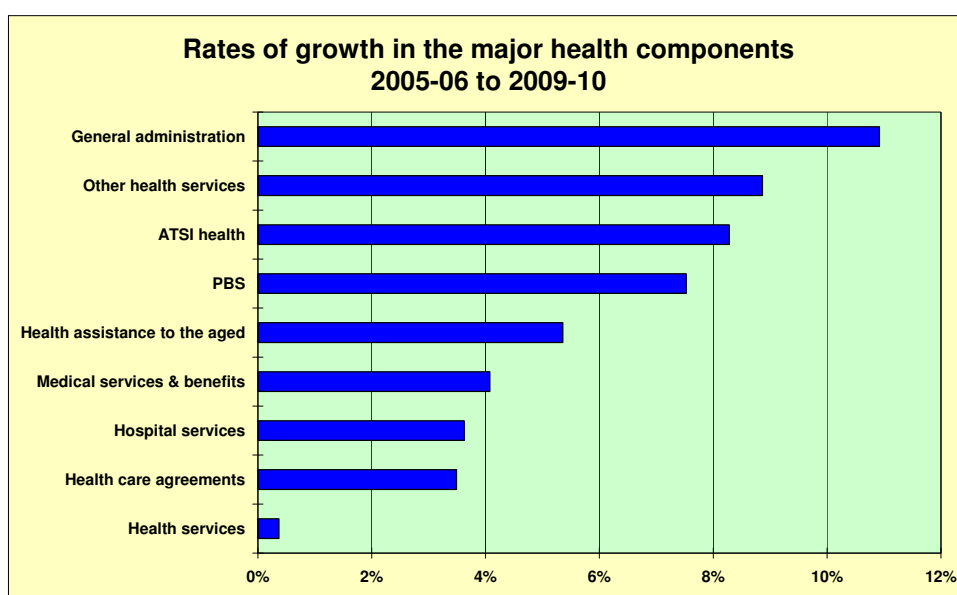
Programs for older Australians

Funding is earmarked for some 16 component programs. The expenditure is very low and the total (just over \$90m) is almost offset by savings expected from the harmonisation of age care and pension arrangements.

5. WHAT'S GROWING QUICKLY, OR SLOWLY

There are quite wide variations in the growth rates of spending in the various major programs in the health portfolio. Over the period 2005-06 to 2009-10:

- ❑ General administration claims fastest growth, 10.0% p.a. on average;
- ❑ Other health service ranks second at 8.9% p.a. This includes faster growing preventive programs;
- ❑ Indigenous health runs third at 8.3% p.a.;
- ❑ The PBS is next at 7.5% p.a., below the average of the growth rates for the previous decade but consistent with savings as drugs come off patent;
- ❑ Health assistance for the aged is set to average 5.4% growth p.a.;
- ❑ Medical services and benefits (a broad church spanning medical Medicare, the PHI tax rebate and some other items) ranks sixth with 4.1% p.a.;
- ❑ Health care agreement money which is largely for State/Territory public hospitals (a very large program) is growing by 3.6%. In addition, the Federal Government has a small program of direct spending on hospital services and growth there is of much the same order (3.6% p.a.).





6. WHAT IS MISSING?

The 2006-07 Health Budget is missing:

- any new ideas to resolve the pressures in public hospitals;
- funding for a superior GP consultation structure;
- serious funding to combat what looks more and more like an epidemic of obesity across all ages;
- funding for nutrition (now more clearly recognised as a particular problem among children, the elderly and Indigenous sub-populations);
- a commitment to address the health effects of climate change; or
- any funding or signs of commitment to the establishment of a long term care scheme to complement the other measures to resolve problems in medical indemnity.

7. THE QUALITY OF BUDGET DATA

DoHA's Portfolio Budget Statement (Budget Related Paper 1.11) has gone through further evolution this year. The number of 'outcomes' (DoFA speak for major areas of spending) has been increased from eleven to fifteen. Changes of this nature sometimes result in better presentation of information for the Budget year (and sometimes not). The main "outcome", however, is to make it much harder for observers to track and analyse changes over time. That said, it does make good sense to break up the old "Outcome 2" which used to comprise the lion's share of the health portfolio spending in one great big bundle.

The information on forward estimates of spending is very tightly restricted, limited to some 10 or so broad expense categories (see table 8, page 6-10 of Budget Paper Number 1) and some 6 categories of PBS spending (see table 8.1, page 6-11). It is not clear why the information about the Government's health spending intentions is so poor.

Even when Departments of State want to be more open, their political masters do not always allow it. Best outcomes in public policy emerge when administrations are open, accountable, prepared to acknowledge that the constituencies have expertise to offer and empowered to engage the constituencies in constructive dialogue. In contrast, a closed and defensive approach may be less bother but it is undoubtedly less effective.

—oOo—