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IPA RESEARCH NOTE

Government spending the biggest contributor to economic growth

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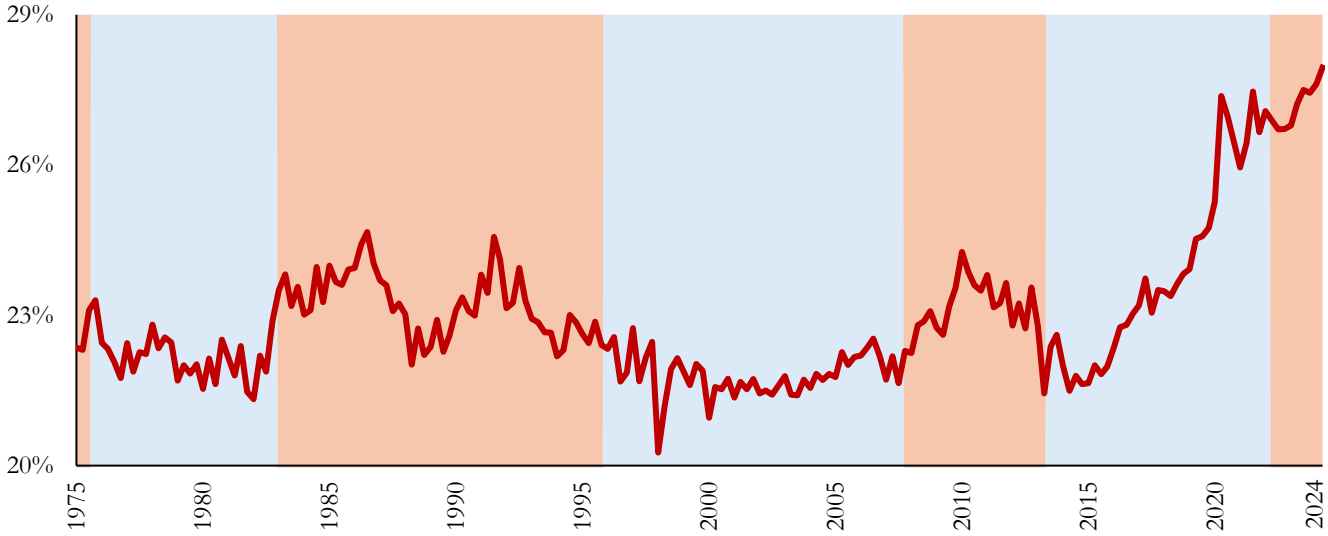
Key findings

Government spending across local, state, and federal governments accounted for a record 28 per cent of gross domestic product (GDP)—economic activity—at the end of the 2024 financial year, up from 21 per cent ten years prior, in the June quarter of 2014.

Chart 1: *Proportion of economic activity (gross domestic product, GDP) directly due to government spending*



Source: IPA, ABS

As well as taking up a larger share of the total economy, increases in government spending have in recent years been the single biggest contributor to economic growth. Specifically:

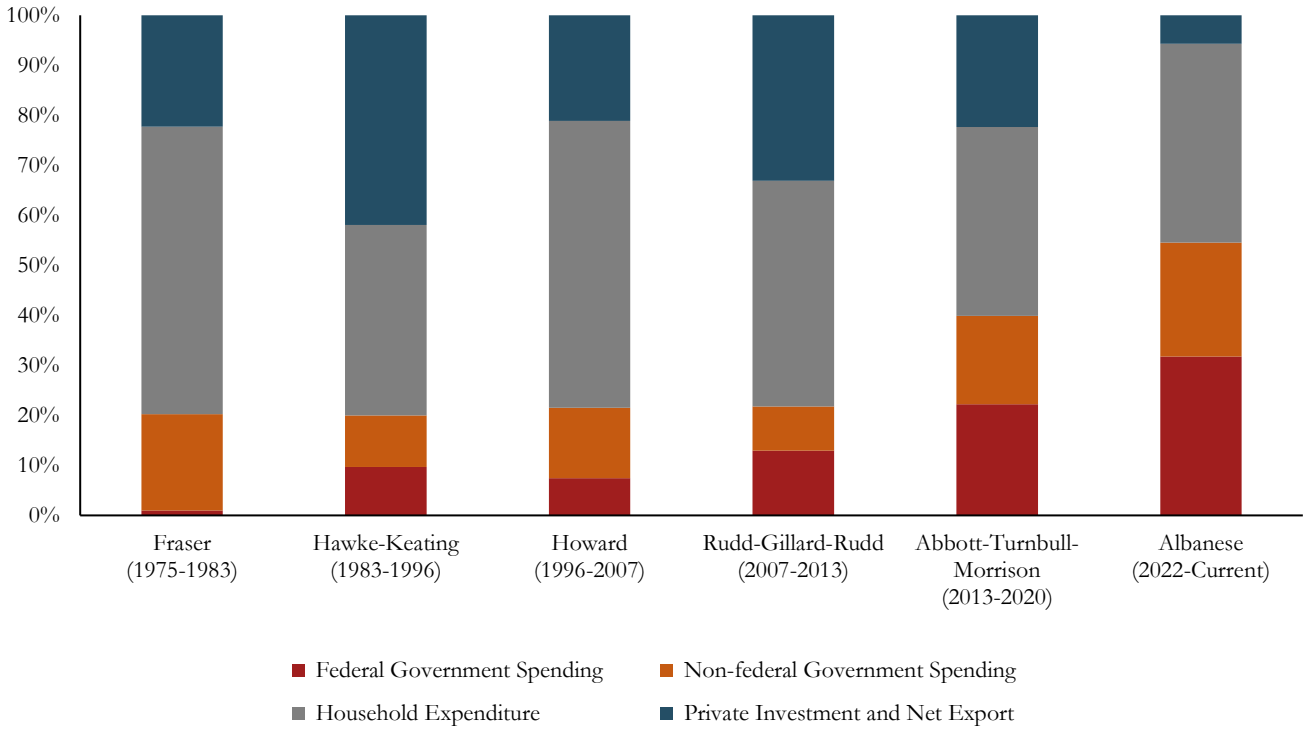
- Between June 2022 and 2024, growth in total government spending (state, federal, local) accounted for 55 per cent of total GDP growth. This was higher than during any other government on record, and up from approximately 20 per cent under the Fraser, Hawke-Keating, Howard, and Rudd-Gillard governments.

- Growth in federal government spending alone accounted for approximately 32 per cent of GDP growth between the start of the Albanese government and the June quarter of 2024. This had increased from 22 per cent in 2013-2020 under the most recent Coalition government, 13 per cent in 2007-2013 under the Rudd-Gillard Labor government, and 7 per cent in 1996-2007 under the Howard Coalition government (it was 34 per cent during the Covid-affected years of 2020-2022).

- Growth in state and local government spending also accounted for a larger share of total economic growth, at 23 per cent, up from 18 per cent in 2013-2020, 9 per cent in 2007-2013, and 14 per cent in 1996-2007.

- Federal government spending under the current government has been averaging just over $70 billion per quarter, which is approximately 50 per cent higher than the quarterly average from 2013 to 2020.

Chart 2: *Components of economic growth by federal government*



Source: IPA, ABS; Covid-19 period has been excluded – see table at end of the note

At the same time, the contribution of private sector investment and net exports to overall economic growth has collapsed to just 6 per cent. To put this in context, the next lowest period excluding the pandemic period was from 1996-2007, when private investment and net exports contributed to 21 per cent of growth. It was 22 per cent in 2013-2020, and also 22 per cent in 1975-1983.

Broader context

The Australian economy is in a period of weakness. Real GDP grew by just 0.22 per cent in the three months to June 2024, following a mere 0.18 per cent increase in the previous quarter, and 0.22 per cent growth in the quarter before that.[1] On a per capita basis, GDP has declined for six consecutive quarters: the longest decline since seasonally adjusted records began in 1973.[2]

There have been more quarters of negative GDP per capita growth under the current federal government than any other federal government since digitised records began. Real GDP per capita has declined in seven of the nine quarters of this term of government so far. Inflation and elevated interest rates, due in part to increased government spending, have played a significant role in aggravating the problem.

Australia has been able to avoid a technical recession and fend-off negative aggregate growth, on paper, partly due to an unprecedented migration intake. But debt-fuelled public spending has also played a significant role.

Chief Macro Strategist at Coolabah Capital, Kieran Davies, concludes:

> Strong growth in public demand has accounted for all of Australia's weak GDP growth over the past year as activity in the rest of the economy has slowed sharply. Above-average growth in a broad, but volatile measure of public-sector employment has accounted for about two-thirds of strong total jobs growth over the past year[.][3]

In the working paper, *The Australian Federal Government is Too Big*, published in September 2024, IPA Adjunct Fellow, Professor Sinclair Davidson observed that, in the context of an already bloated public sector:

> [I]ncreases in government spending are reducing economic prosperity. The cost of financing those increases in expenditure are both high and becoming more expensive … the solution to that is not finding innovative ways to finance that bloat, but rather to reduce the size of government.[4]

The study presented in this paper tracks the trajectory of government spending as a share of GDP by quarter and illustrates that government spending is playing an increasingly dominant role in the Australian economy at the expense of private investment and net export. Growth in government spending at the federal, state, and local levels contributed 55 per cent of GDP growth under the Albanese government to June 2024, higher than any other government on record. The contribution of private investment and net export, on the other hand, was only approximately 6 per cent.

Methodology

Data analysed in this paper were sourced from the Australian Bureau of Statistics' (ABS) Australian National Accounts database for the reference period up to the end of the 2024 financial year. The data are quarterly and were released on 4 September 2024.

GDP numbers and its component measures are based on real as opposed to current-price data. This means that the dollar figures are adjusted for inflation. The chain volume measurement in the database is pegged to the Australian dollar as of the financial year ending 2022.

The series type utilised in this report are seasonally adjusted in accordance with common academic and journalistic practice when utilising quarterly as opposed to annual or annualised datasets. This means that each quarter's datapoint has been normalised by the ABS to smooth out seasonal variations.

Composition of gross domestic product

There are different ways to break down economic activities (GDP) into different components. Since the focus of this paper is to analyse the size and growth of government spending, it utilises what the ABS describes as the expenditure approach.[5] Other approaches are used for different purposes, for instance, to determine the contributions of labour vs capital or to investigate the contributions of different economic sectors (e.g., primary, industry, and services).

The expenditure approach breaks down aggregate GDP into final consumption expenditures, investment, and international trade aggregates (i.e., imports and exports). Put simply, the expenditure approach adds up all expenditure in an economy (including capital expenditure or 'capex'), then adds exports and minus imports. In short:

$$GDP = Household\ Spending + Government\ Spending + Private\ Investment\ and\ Net\ Export$$

Government spending, in this paper, is defined as federal, state and territory, and local general government expenditure in addition to public sector capital expenditure, which includes spending associated with the construction of public infrastructure such as energy generation and storage assets.

Components of GDP growth, for the purpose of this paper, is defined as the contribution of the change of each type of expenditure (e.g., government spending) to the overall change in GDP. For instance, quarterly government spending had grown by $20 billion between the start and the end of the Hawke and Keating era. Growth in aggregate GDP was approximately $100 billion between the relevant quarters. This represented a 20 per cent increase. Private investment and net export (combined) increased by just over $42 billion over the same period, thus representing a 42 per cent increase in the private investment and net export component of economic growth.

The Australian National Accounts dataset includes two additional components which are excluded in the growth analysis, namely: 'statistical discrepancies' and 'net change in inventories'. In addition to these, there are additional statistical discrepancies not accounted for in the dataset. On average, the combined volume of the discrepancies is minor and immaterial. However, the older the data, the greater the discrepancies. Quarterly discrepancies before 1975 averaged 15 per cent of GDP, while quarterly discrepancies after 1975 average roughly 3 per cent of GDP. Consequently, only data after 1975 were used in the analysis. In the last financial year, total discrepancies averaged 0.02 per cent of GDP.

Assigning quarterly periods to government

In this study, each quarterly period was assigned a corresponding parliamentary term, identified by its term number and the prime minister (or prime ministers) in office during that period. For instance, the December quarter of 2023 coincided with the 47th parliament, in which the Australian Labor Party was in government and Anthony Albanese was the prime minister. Quarters in which elections occur are assigned to the incoming parliamentary terms.

The period covered in the study is between the first quarter of 1975 and the second (June) quarter of 2024 – namely, the end of the 2024 financial year. This is because, while data are available prior to 1975, the statistical discrepancies in the data are too significant, rendering the analysis more susceptible to error.

Analysis

Government spending at the federal, state and territory, and local levels made up 22 per cent of GDP at the end of the financial year ending 1975. By 2024, this has increased to 28 per cent.

If government spending had stayed at 22 per cent, then annual government spending in the financial year ending 2024 would have been $129 billion less. Accumulated over a period of roughly ten-and-a-half years, this amount could be enough to pay off all Australia's gross debt at the federal, state and territory, and local government levels.

The increase in government spending at the start of the Hawke premiership coincided with the Prices and Incomes Accord, whereby the Australian Council of Trade Unions agreed to moderate demands for wage increases in exchange for an expansion in the welfare state. Medicare was created in the 1980s to permanently establish universal healthcare. Efforts to reduce budget deficits to control inflation were juxtaposed with periods of expansion in public services, thus creating a mixed legacy of fiscal management.

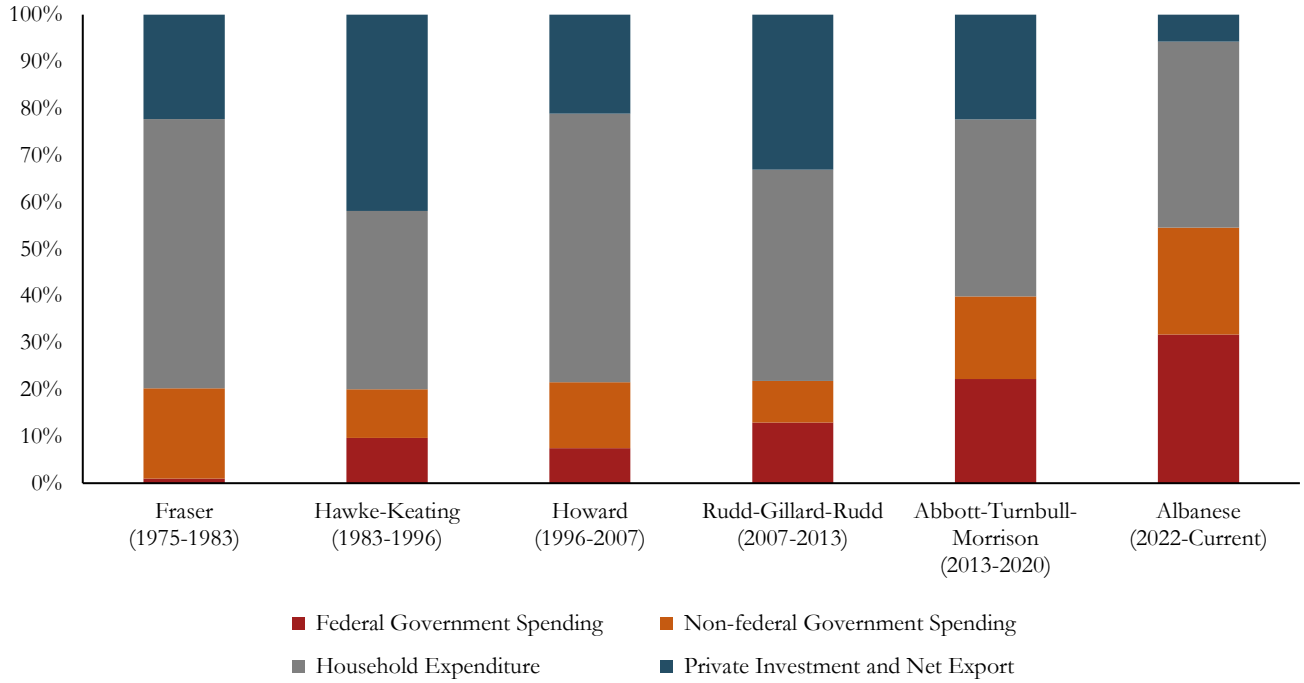
Fiscal discipline was enforced under the Howard government, with budget surpluses from 1998 to 2001; there was a small deficit in 2002, but surpluses returned from 2003 to 2008. Net federal government debt was paid off in April 2006.[6] The Rudd government produced a budget surplus in its first year in office, but the additional stimulus spending incurred in response to the Global Financial Crisis brought the budget into deficit the following year.

In an attempt to deliver a budget surplus, the Gillard government subsequently took steps to reduce government spending, which contributed to spending as a share of GDP falling back to 21 per cent in the June quarter of 2013 from a height of 24 per cent in the March quarter of 2010.

The targeted effort by the Abbott government to cut red tape successfully reduced regulatory burdens on the private sector.[7] Government spending was kept under control throughout the Abbott premiership and exports rallied. These had the effect of controlling the growth of public spending as a component of GDP.

Under the Turnbull government, however, public spending as a share of GDP started to steadily increase once again. Expansionary fiscal policies under the Morrison government during the pandemic resulted in the historic rise in government spending to more than 27 per cent of GDP. The record was subsequently surpassed during the Albanese premiership. By the end of the 2024 financial year, government spending made up 28 per cent of Australia's GDP.

Chart 3: *Components of economic growth by federal government*



Source: IPA, ABS; Covid-19 period has been excluded – see table at the end of the note

Chart 3 shows the contributions of the change in the components of GDP to economic growth between the start and the end of each federal government.[8] Increases in government spending contributed to roughly 20 per cent of the increases in GDP during the Fraser, Hawke, Keating, Howard, Rudd, and Gillard governments. The last Coalition government had a mixed record.

The contribution of government spending to economic growth fell under Abbott's premiership, which coincided with a larger role played by net export in growing the economy. But government spending increased considerably during the Turnbull and Morrison premierships. Overall, growth in government spending was responsible for 48 per cent of GDP growth under the Coalition between 2013 and 2022, or 40 per cent excluding the pandemic period.

Under the Albanese government, the contribution of government spending to economic growth increased further to 55 per cent, most of which was attributable to federal government spending. The contribution of private investment and net export fell to just 6 per cent of total economic growth. Household spending, which contributed the most to economic growth under the Fraser, Howard, and Rudd-Gillard governments, also grew more slowly under the Albanese government. This was logical in the context of a declining real GDP per capita. Adjusted for inflation, Australian households' disposable income fell by 8 per cent in the two years to March 2024, making Australia the poorest-performing economy in the Organisation for Economic Co-operation and Development (OECD) according to an analysis by the *Australian Financial Review*.[9]

Appendix: What happened during the pandemic?

The table below breaks down components of GDP growth under different governments at the federal level. Discrepancies discussed in the Methodology section of this paper have been excluded from the final count.

Table 1: Share of economic growth by growth components

Government	Federal government expenditure	Non-federal government expenditure	Household expenditure	Private expenditure and net exports
Fraser (1975-1983)	1%	19%	57%	22%
Hawke-Keating (1093-1996)	10%	10%	38%	42%
Howard (1996-2007)	7%	14%	57%	21%
Rudd-Gillard-Rudd (2007-2013)	13%	9%	45%	33%
Abbott-Turnbull-Morrison (2013-2020)	22%	18%	38%	22%
Morrison (Pandemic 2020-2022)	34%	38%	72%	-45%
Albanese (2022-current)	32%	23%	40%	6%

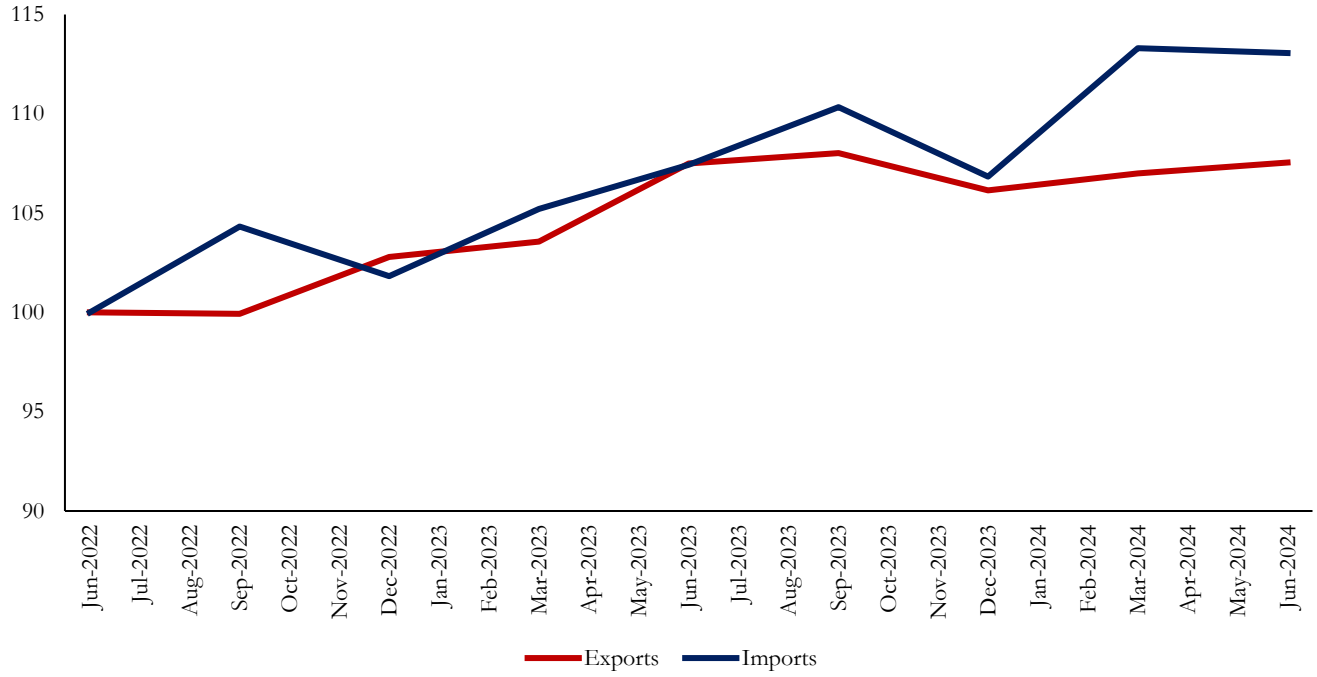
Source: IPA, ABS; *Covid-19 period has been excluded from the associated chart*

Household expenditure made up the largest component of GDP growth throughout the pandemic-affected period by far. This was attributable to various direct pandemic stimulus measures.

Private investment and net export was negative during the pandemic and is struggling to recover for a number of reasons. Business investment has been in decline since well before the pandemic because Australia's economic environment has been deteriorating, as shown by previous research by the IPA.[10]

Imports have also been growing at a faster rate than exports, thus affecting the rate of growth in the net export component of the broader 'private investment and net export' category. Chart 4 below tracks the trajectory of the sub-components of net export since the June quarter of 2022.

Chart 4: *Indexed components of net exports (Index: June 2022 = 100)*



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End Notes

1. Australian Bureau of Statistics, 'Australian National Accounts: National Income, Expenditure and Product', Australian Bureau of Statistics (4 September 2024): https://www.abs.gov.au/statistics/economy/national-accounts/australian-national-accounts-national-income-expenditure-and-product/jun-2024; Stephen Bartos, 'This is the weakest economy outside of a recession. Here's what the GDP figures show', *The Conversation* (4 September 2024): https://theconversation.com/this-is-the-weakest-economy-outside-of-a-recession-heres-what-the-gdp-figures-show-236128.

2. Daniel Wild, 'Australians are in recession with out-of-control migration crushing living standards', (Media release, Institute of Public Affairs, 4 September 2024): https://ipa.org.au/publications-ipa/media-releases/australians-are-in-recession-with-out-of-control-migration-crushing-living-standards.

3. Kieran Davies, 'The public sector's role in propping up growth and jobs', *Live Wire* (4 October 2024): https://www.livewiremarkets.com/wires/the-public-sector-s-role-in-propping-up-growth-and-jobs

4. Sinclair Davidson, *The Australian federal government is too big* (Institute of Public Affairs, Working Paper No.02/24, September 2024).

5. Australian Bureau of Statistics, 'Measures of GDP', Australian Bureau of Statistics (9 July 2021): https://www.abs.gov.au/statistics/detailed-methodology-information/concepts-sources-methods/australian-system-national-accounts-concepts-sources-and-methods/2020-21/chapter-8-gross-domestic-product/measures-gdp.

6. Peter Costello, 'Debt-free Day' (Speech to the Committee for Economic Development of Australia, 20 April 2006): http://www.treasurer.gov.au/tsr/content/speeches/2006/008.asp.

7. Lachlan Clark and Saxon Davidson, *The Growth of Red Tape: Causes and Solutions* (Research Report, Institute of Public Affairs, November 2023).

8. Reported statistical discrepancies, change in inventories, and unreported statistical discrepancies by the ABS, have been excluded from the aggregation. The pandemic period has also been excluded.

9. Michael Read, 'Australia's fall in disposable income is the worst in the world', *Australian Financial Review* (30 August 2024): https://www.afr.com/policy/economy/australia-s-fall-in-disposable-income-is-the-worst-in-the-world-20240822-p5k4ji

10. Kevin You, 'Australia's economic competitiveness in continuing decline' (Institute of Public Affairs Parliamentary Research Brief, November 2023); Kevin You, Institute of Public Affairs Submission to the Inquiry into Promoting Economic Dynamism, Competition, and Business Formation (31 March 2023).