Under pressure: calls on Australia's 2016 aid budget

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It might be assumed that Australia's overseas aid budget is now at maximum compression. As this post aims to show, that's quite an unsafe assumption, even if the overall aid envelope contracts no more than has already been foreshadowed. The lid might have finished sinking, but there is now the potential for increased pressure inside the pot.

Labor's $5 billion 2012-13 aid budget was effectively reduced by $350 million when that amount was abruptly reallocated, in December 2012, to meet domestic asylum-seeker costs. The reallocated expenditure still figured as Official Development Assistance (ODA) but had to be taken from international programs and organisations. Labor's $5.7 billion 2013-14 aid budget, which was cut mid-year to $5 billion when the Coalition was elected, reserved the same amount for asylum-seeker costs. The Coalition's $5 billion 2014-15 aid budget dropped the reservation but, before any of the freed-up funds could be allocated to long-term programs, the Coalition's 2015-16 budget imposed a $1 billion cut. Moreover, that budget's forward estimates showed a further cut of $224 million to be applied in the 2016-17 aid budget, which would normally be announced in May.

If we allow that Labor's $700 million increase in 2013-14 was still largely unprogrammed before it was cancelled by the Coalition, the net effect of these various decisions was a three-step reduction in the amount of money available for 'normal' programming ($350 million in 2012-13, a net $750 million over 2014-15 and 2015?16, and $224 million in 2016-17). The total will have fallen from $5 billion in 2013-14 to $3.8 billion in 2016-17, at least 55 individual aid activities will have been cancelled, slowed or scaled back—we know this from a woefully uninformative response [pdf] to a Question on Notice from Senator Wong (October 2015, no. 13)—and our standing in numerous multilateral organisations will have declined substantially. Of course each budget brings surprises, and the $3.8 billion figure for 2016-17 is not quite set in stone, but it's probably a safe bet that this will be the envelope. If so, and once the remaining cuts of $224 million have been allocated, isn't the storm finally over?

Maybe, but it would be best not to count on that. The 2016-17 budget faces three potential pressures underneath the sunken lid, which are collectively quite substantial.

Climate change financing

The first and least of them derives from the Prime Minister's commitment at the Paris climate change conference to spend at least $200 million per year for the next five years on climate change mitigation and adaptation programs.

This commitment was no great stretch. It is already the case that the government can comb through its aid portfolio and find programs with annual expenditure of around $200 million that are at least slightly relevant to climate change. In fact, DFAT advised the parliament in recent hearings that the figure was $229 million in 2014-15.

However, Turnbull's commitment having been made, it is likely that Australia will face greater scrutiny than it has over the last several years with respect to climate change financing. Slightly relevant might not be good enough, especially if the power to decide what's included is stripped from individual donors. In addition, $200 million is 5.3% of a $3.8 billion budget, whereas last year's expenditure of $229 million was 4.6% of a $5 billion budget, and it is likely that programs related to climate change were among the first on the chopping block in the 2013-15 period.

It is, therefore, quite possible that the government will have to shift funds toward the most highly relevant programs, or in some cases establish new programs, in order to meet the Prime Minister's commitment in a sufficiently credible way.

To take a wild guess, possibly more than $50 million per year might need to be so shifted.

Asian Infrastructure Investment Bank

The second pressure is a potential but likely one, despite statements to the contrary from DFAT. It relates to the Asian Infrastructure Investment Bank (AIIB).

After some dithering, the government decided to become a member of the institution. Indeed it offered to pay quite a high price for membership, arguably much higher than was necessary. Normally, subscribing to shares in such an institution does not involve much in the way of actual expenditure.

In the cases of the International Bank for Reconstruction and Development (IBRD, the World Bank's non-concessional arm), the Asian Development Bank and the European Bank for Reconstruction and Development (EBRD), only a tiny proportion of the value of their members' shares is actually paid in. The value not paid in is termed callable and in reality never called. The AIIB is unusual in that it requires a 20% paid-in contribution (the IBRD required the same on establishment but subsequent capital increases have reduced the paid in share to around 3%). As a result of this and Australia's large shareholding, the government will need to pay in some $932 million evenly distributed over the five years following ratification of the bank's Articles of Agreement, which happened last November.

In the case of the other institutions named above, paid-in contributions qualify as ODA. This is not because these institutions provide assistance on grant or soft-loan terms—the EBRD doesn't even have a concessional financing arm—but because they have a developmental mandate (they 'conduct all or a significant part of their activities in favor of development and aid recipient countries'). On the basis of this mandate, they have been included in the OECD's list of multilateral and other organisations to which contributions can be counted as ODA. The list is updated annually (see for example this [pdf] recommendation to add the UN Green Climate Fund, among others, last May).

The case of the AIIB, which was created only last October, will likely be considered in a few months' time, soon after Australia's 2016-17 budget is announced. A DAC donor will first have to propose the case for consideration, but this will undoubtedly happen if it has not already. It seems highly probable that capital contributions to the AIIB will be treated in the same way as contributions to the very similar EBRD and to the non-concessional arms of the other multilateral development banks—namely, that they will be 'assimilated to grants' and considered ODA-eligible. In fact, contributions will probably be deemed 100% eligible given that the AIIB's client base, unlike the EBRD's, will comprise only developing countries (for this reason, EBRD contributions are only 43% eligible).

The Australian government has stated in various contexts that Australia's AIIB contribution will not be charged to the aid budget. In Senate Estimates hearings in February 2016, DFAT's Secretary Peter Varghese said:

> The AIIB is not an aid-based bank. The contributions to the AIIB are not official development assistance.

A joint DFAT-Treasury submission to a parliamentary inquiry on AIIB-related legislation last year said:

> This investment will not come at the cost of other Government spending and will not directly impact on the Budget bottom line. ... Australia's paid-in capital will not be provided from the aid budget as the AIIB has not been deemed ODA-eligible.

'No cost to other government spending' presumably entails no redirection of ODA, or any other portfolio's budget, to meet the cost. (The contradictory-seeming 'no direct impact on the bottom line' is presumably just bad drafting, since this can only be true of the callable component of Australia's subscription.)

However, Varghese's statement runs together the status of outflows from the AIIB (not ODA) with the status of paid-in capital contributions to it (likely to be deemed ODA). And while the DFAT-Treasury submission does acknowledge that the ODA status of contributions is a matter for decision by the OECD, it appears wrongly to imply that the matter has already been considered and a negative decision reached. If not that, it implies that the expenditure will be taken from the aid budget in the event that it is deemed ODA-eligible.

What are other donors doing on this front? The United Kingdom is one of the largest non-regional AIIB shareholders, with almost as large a shareholding as Australia's. On 19 October 2015, the Chief Secretary to the UK Treasury, Greg Hands, said the following to a House of Commons committee:

> My hon. Friend the Member for Stafford asked a question that was also asked by the hon. Member for Feltham and Heston, which was whether the contribution could be classed as ODA. We are awaiting a pronouncement from the OECD, which monitors the ODA rules. We expect that pronouncement by May 2016 and it would be retrospective as to whether something was ODA.

That is admirably clear on two fronts. First, the matter is expected to be considered in May (though it should be noted that the UK, like other OECD donors, will be a party to the decision and is not merely waiting for a 'pronouncement' from the OECD). Second, if contributions are deemed to be ODA, the UK will report them as such, including retrospectively.

Why on earth wouldn't the Australian government do the same? If it did, the cost would be $185 million per year, for five years.

Refugee resettlement

The third pressure is also a potential one, but perhaps less likely to be realised than the one immediately above. It relates to the 12,000 refugees from Syria and Iraq who are to be resettled in Australia in accordance with a decision of the Abbott government last year.

The costs associated with this decision are large. Initially, the costs were estimated to be $700 million over the four years commencing 2015-16. Subsequently, the government revised this estimate to $827 million in the December 2015 Mid-year Economic and Fiscal Outlook [pdf] (MYEFO). Under DAC rules, substantial costs associated with the resettlement of refugees—essentially those associated with processing, transportation and social service provision—can be counted as ODA for up to one year after their arrival in a donor country.

Australia has until now followed the peculiar policy of occasionally charging asylum-seeker costs to the aid budget, particularly in 2012-13 and 2013-14, while not charging any refugee resettlement costs to it. The logic, if that's the right word, seems to be that we only hit the aid budget for costs associated with people who enter the country via boat without visas. Costs associated with refugees whom we deliberately import under the humanitarian migration program have been regarded as a domestic expenditure. Other donors follow other logics, all of which are consistent with what are currently very vague OECD rules. Some donors include costs associated with so-called 'quota refugees', such as those we are about to resettle.

If Australia were to do this, and if we exclude ineligible costs such as those associated with economic integration (the MYEFO contains a handy cost breakdown by portfolio), it appears that well over $175 million per annum might be eligible to be reported as ODA in each of the three years from 2016-17. At some stage a temptation must arise to charge these unprecedented costs to the aid budget. It might not happen, since it has not happened before in connection with quota refugees, but it could.

Combined impact

If all the above pressures were in fact realised in 2016-17, we would have $224 million in the form of the sinking lid, perhaps $50 million for new climate change programmes, $185 million for the AIIB, and $175 million for refugees. So that totals almost $650 million in a single year that would need to be redirected from programs that are ongoing or in advanced stages of planning. Given the substantial rigidities on the multilateral side of the aid budget, and the likely reluctance to eat much further into NGO programs and scholarships, that's another $650 million that would, in large part, need to come out of country and regional programs—which already fell from $3 billion to $2.2 billion in the last budget. At this rate, Australia might soon be reduced to running little more than Direct Aid Programs in many of its partner countries.

It’s entirely possible the government will resist charging the additional refugee costs to the aid budget. It is possible but, in the end, highly unlikely that it will resist charging AIIB costs to the aid budget. And it is very likely the government will have to spend more on directly relevant climate change programs than it would otherwise have done in order credibly to meet the Prime Minister’s $1 billion commitment. The worst-case scenario is that all these costs are jammed into a $3.8 billion aid budget. A better scenario is that there is only some slight additional pressure associated with the climate change commitment. The best-case scenario, short of an unexpected increase in the underlying aid envelope, is that the government decides to report AIIB and refugee costs as ODA without subtracting them from the existing $3.8 billion allocation. This might be regarded as a dishonest way of suddenly inflating ODA, but we would be doing what various other donors already do or intend to do, consistent with OECD rules. Moreover, there might be some hope that the enlarged envelope stays around the same size in the future, even as refugee costs and AIIB costs fall away.

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