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Your Defence Dollar:

The 2005–06 Defence Budget

Executive summary

In his 2005–06 Budget speech, the Treasurer didn't get around to national security until the second last item, and defence didn't rate a mention anywhere. Nonetheless, it was an important budget for Defence, in that it delivered the fifth tranche of \$2.3 billion in funds promised by the 2000 White Paper. This, and a number of new initiatives, will see defence spending reach \$17.5 billion in 2005–06. This amounts to 1.9% of gross domestic product and 8.5% of Commonwealth payments.

New initiatives in the Defence budget will account for more than \$1.2 billion in spending across the next four years. The largest single item is \$420 million to fund Australia's ongoing military presence in Iraq. Other significant initiatives include the reprogramming of an additional \$300 million for capital investment in 2005–06, and \$252 million over four years for a variety of security enhancements as part of the government's \$1.1 billion budget package of measures entitled *Providing for Australia's Security*.

But there was also some stringency built into this Budget. Not only is Defence required to deliver \$221 million in efficiency dividends and administrative savings over the next

four years, but fully \$218 million worth of the new initiatives were unfunded. The overall result is that Defence has to deliver \$1.2 billion worth of initiatives with only \$780 million in new funds—a shortfall of \$439 million over four years.

This shouldn't be too great an impost. Over the past several years, the government has funded Defence for additional logistics, facilities and personnel costs, with a clear imperative to achieve effectiveness. Now, with the operational tempo of the Australian Defence Force (ADF) a little less hectic, the spotlight has returned to efficiency. Fortunately, following several years of internal management improvements, Defence is well placed to deliver the required savings.

One area of concern is military personnel numbers. Despite spending \$500 million over five years on initiatives to improve the recruitment and retention of military personnel, the size of the permanent ADF has fallen for two years in a row. While the currently strong economic climate is no doubt a factor, it may be that in the long run a more radical approach will be required to attract young 21st century Australians into the military and to retain them.

On the positive side, good progress is being made in the Defence Materiel Organisation (DMO) following the 2003 Defence Procurement Review. DMO became a quasi-autonomous ‘prescribed agency’ on 1 July 2005, and purchaser–provider agreements are now in place between Defence and DMO for acquisition and sustainment services. This is the most fundamental change to Defence management since the Defence Reform Program of the late 1990s. If all goes to plan, this will deliver a much more businesslike arrangement, with greater visibility of costs and better definition of performance standards.

In terms of actually delivering new equipment, it looks like the reforms of DMO are gaining early traction. Last year, around \$2 billion in planned capital investment was deferred to beyond 2008 because DMO was unable to spend the money. This year, spending on projects has picked up significantly and is projected to exceed the budgeted target. Moreover, \$300 million of deferred spending has been reinstated into the budget for 2005–06. This is a significant boost for the prospect of delivering the government’s \$50 billion decade-long program of capital investment, the Defence Capability Plan (DCP).

Unfortunately, at the same time, the approval of new projects by the government has stalled in the eighteen months since it released a revised DCP in 2004, and unless projects are approved there’s no way they can be delivered. Comparing the projects planned for approval in 2004–05 and 2005–06 with what’s occurred and what’s now planned to occur, we’re already at least a year behind schedule.

Thus, one way or another, it looks like the ADF will have to wait for the capability it needs.

The mounting delays in approving projects in the DCP are rapidly rendering the current version of the plan obsolete. This introduces further uncertainty into an already opaque situation in which our strategic priorities remain unresolved and long-term Defence funding is undecided past the end of the decade (despite a promise last year that the issue would be resolved in the 2005–06 Budget). This last point is particularly important. It makes no sense to try to run a ten-year program of capability development on a five-year funding profile.

This trinity of uncertainty (policy, priorities, funding) has led to calls from many quarters for a new White Paper—calls that the government has consistently resisted. The government has now relented, at least in part, with the recent announcement by the Defence Minister of a new Strategic Update and a revised Defence Capability Plan before the end of this calendar year. Moreover, we understand that this will be accompanied by a decision on long-term Defence funding for release in the next budget.

Thus, despite all the challenges that this year’s budget revealed, we can be cautiously optimistic that long-term defence plans will soon be put back onto a coherent basis. While this is encouraging, it raises the question of why Defence’s overall strategic planning remains aperiodic and ad hoc. Given the excellent progress made in recent years in improving Defence’s annual budgeting and reporting, the time is right to apply the same rigour and discipline to long-term strategic planning.



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